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# INVESTMENT SERVICES AND ACTIVITIES AGREEMENT ON CAPITAL MARKET

**Cristian GHEORGHE**[*]

**Abstract**

*Investment services and activities on the account of the investors shall be supplied under a contract drafted in accordance with Capital Market Laws.*

*Intermediaries (investment firms) hold the market access monopoly to trading systems of the regulated market or multilateral trading systems. Contracting them is the only way for investors to have access (indirectly) to trading through market orders.*

*The legal framework shaped by the contract regarding investment services and activities is the premise, the mandatory and preliminary condition for the sale or purchase of financial instruments. The contract of investment services and activities is thus a sine qua non for trading on the capital market.*

**Keywords:** *capital market, investment services and activities agreement, regulated market, trading system, investment firm.*

## 1. Investment services and activities.

Investment services and activities have a legal demarcation. The main services for investors are: reception and transmission of orders in relation to one or more financial instruments, execution of orders on behalf of clients, portfolio management, investment advisory services, underwriting of financial instruments and placing of financial instruments on a firm commitment basis or without a firm commitment basis. Along with these main services the law also sets ancillary services which consist of safekeeping and administration of financial instruments for the account of clients, granting credits to an investor to allow him to carry out a transaction, advice to undertakings on capital structure, foreign exchange services connected to the provision of investment services, services related to underwriting.[1] Main services includes also services and activities that exceed the provision of customer services: dealing on own account, operation of an MTF (multilateral trading facility) or operation of an OTF(organized trading facility). Contemplating these services and activities it is easy to extract the essence of the investment services and activities agreement: performing legal acts and deeds regarding the financial instruments or following the order of the client.

## 2. Legal nature of the investment services and activities agreement.

At the declarative level, although the legislator is not legally consistent, the intermediary (services provider) works on

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[1] Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU, Annex I, Section A and B.

behalf of the client, suggesting the existence of a legal relationship based on a full power of attorney (mandate with representation).

The effects of the intermediary"s activity will be reflected in the client"s assets by the purchase or sale of financial instruments. Investment firms (SSIF in Romanian Capital Markets Laws) will undoubtedly work on their client"s account. European rules use this formula, the client"s account, to compare with the transaction that employs the SSIF"s own funds, dealing on own account. Therefore "execution of orders on behalf of clients" means acting to conclude agreements to buy or sell one or more financial instruments on behalf of clients and "dealing on own account" means trading against proprietary capital resulting in the conclusion of transactions in one or more financial instruments[2].

The execution of stock transactions takes place through stock exchange mechanisms, on behalf of the intermediary. Orders are executed by intermediaries (investment firms) in the multilateral market system in their own name (between two initial SSIFs, then between each SSIF and the CCP (central counterparty clearing house, a specialized legal entity of the regulated market mechanism)) with the effects being made on clients" accounts.

The agreement concluded between investment firms and clients seems to be, from the perspective of the entire mechanism of the conclusion and execution of the market orders, as a mandate without representation.

In fact, the conclusion of transactions by the intermediary exclusively on behalf of the client would compromise the stock market celerity, would mean the multiplication of the legal relations between the specialized market participants (market operator, central securities depository (CSD), central counterparty (CCP)) with the number of investors participating in the stock exchange.

Otherwise, direct legal relationships only concern investment firms which deal in their own name and the rest of the capital market specialized participants.

Investors just take advantage of these pre-existing legal relationships as the investment firms works on their own behalf as part of the legal relationship with the trading market institutions. The intermediary provides services to the client and concludes legal acts in his own name but on the client"s account.

The service provider generally carries out proprietary trades. However, the service provider may act in the name of and on account of the client.

## 3. A priori assessment of the adequacy and appropriateness of the services and activities offered to investor.

The investment firm shall collect information from the clients about their knowledge and experience regarding financial investments in order to determine their financial skills, provide appropriate warnings about the risks inherent in transactions on capital market and provide client tailored services.

Pursuant to the regulations, the client shall be classified in the retail or professional clients category[3] and shall be informed of its right to ask for a different categorization, under the conditions defined in the regulations. The client shall also be informed

[2] Directive 2014/65/UE (MiFID II), Art. 4 para (1) no 5.

[3] Annex II, Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU.

of the consequences which could result concerning its degree of protection[4].

*Retail clients* are afforded the most regulatory protection while *professional clients* are considered to be more experienced and able to assess their own risk and make their own investment decisions so they are afforded less regulatory protection.

According to Capital Markets Laws, the following shall be regarded as *professionals* in relation to all investment services and activities and financial instruments: entities which are required to be authorised or regulated to operate in the financial markets (as well as credit institutions, investment firms, insurance undertakings, collective investment schemes and management companies of such schemes, pension funds and management companies of such funds and other institutional investors), large undertakings meeting two of the following size requirements, on a proportional basis: balance sheet total at least 20.000.000 Euro, net turnover at least 40.000.000 Euro, own funds at least 2.000.000 Euro, national and regional governments, public bodies that manage public debt, central banks, international and supranational institutions (such as the World Bank, the International Monetary Fund, the European Central Bank, the European Investment Bank and other similar international organisations) and other institutional investors whose main activity is to invest in financial instruments, including entities dedicated to the securitisation of assets or other financial transactions[5].

Any clients not falling within this list are, by default, retail clients. Even if they are on the list above such entity can ask for a higher level of protection where it deems it is unable to properly assess or manage the risks involved.

Clients may be treated as professionals on request following some identification criteria as well as: frequent significant transactions, portfolio size or financial expertise[6]. Such clients may waive the benefit of retail client status only where the following procedure is followed: they must state in writing to the SSIF that they wish to be treated as professional clients (either generally or in respect of a particular investment service), SSIF must give them a written warning of the protections and investor compensation rights they may lose and they must state in writing, in a separate document from the contract, that they are aware of the consequences of this professional status.

*Eligible counterparties* are entities (to which a credit institution or an investment firm provides the services of reception and transmission of orders on behalf of clients or execution of such orders) as well as: investment firms, credit institutions, insurance companies, UCITS and UCITS management companies, pension funds and their management companies, other financial institutions authorised or regulated under Union law or under the national law of a Member State, national governments and their corresponding offices including public bodies that deal with public debt at national level, central banks and supranational organisations[7].

The retail client has the right to request the different classification of professional client but he will be afforded a lower level of

[4] Art. 25, Directive 2014/65/EU.

[5] Directive 2014/65/EU, Annex II.

[6] Ibidem. The client has carried out transactions, of significant size, on the relevant market at an average frequency of 10 per quarter over the previous four quarters, the size of the client"s financial instrument portfolio exceeds 500.000 Euro, the client works or has worked in the financial sector for at least one year in a professional position.

[7] Ibidem, Article 30 para (2).

protection. SSIF is not obliged to accept this request. Also the professional client has the right to request the different classification of retail client in order to obtain a higher level of protection. The eligible counterparty has the right to request a different classification of either as a professional client or retail client in order to obtain a higher level of protection.

If the client stops providing the information requested by the regulations to the investment firm, the latter would no longer be in a position to assess the appropriateness of the financial instrument and shall draw the client"s attention to the risks it could incur due to the inappropriateness of the financial instrument compared to its profile.

Regarding order execution, the investment firm shall not be required to collect the information needed for client"s assessment if the service is provided at the client"s initiative (and if the investment firm warns the client prior to the execution of orders that no assessment the appropriateness of the service or the financial instrument is provided).

## 4. Execution policy.

Best execution principle implies the investment firm"s obligation to take all reasonable measures, during order execution, to obtain the best possible outcome for its clients, under the conditions defined by regulations[8].

Where an investment firm (SSIF) executes an order on behalf of a retail client, the best possible result shall be determined in terms of the total consideration, representing the price of the financial instrument and the costs relating to execution (which shall include all expenses incurred by the client which are directly relating to the execution of the order).

For the purposes of delivering best possible result where there is more than one place to execute an order for a financial instrument, in order to assess and compare the results for the client that would be achieved by executing the order on each of the execution place, the SSIF"s own commissions and the costs for executing the order on each of the eligible execution places shall be taken into account in that assessment[9].

However, if the client asks investment firm for a quotation for a financial instrument transaction, such firm shall not apply its execution policy. Investment firm, acting as counterparty for its client, shall not be substituted for its client in deciding the best way to carry out such a transaction.

If the investment firm agrees to accept an order including a specific instruction given by the client, it shall execute the order in accordance with that instruction. The client is clearly informed that the investment firm was prevented from carrying out the measures stipulated in the execution policy in respect of the conditions imposed in the clients" instruction.

If the client places a limit order relating to shares accepted for trading on a regulated market and this order is not immediately executed under the conditions prevailing on the market, the investment firm shall take measures to facilitate the order execution as quickly as possible, by making it immediately public in a form easily accessible to other market participants[10].

When the investment firm provides the service of reception-transmission of orders, the entities to which client orders are transmitted for execution are selected on the

[8] Art. 27, Directive 2014/65/EU.
[9] Art. 27 para (1), Directive 2014/65/EU.
[10] Art. 28 para (2), Directive 2014/65/EU.

basis of ensuring the best possible execution. Unless otherwise specified by the client, he shall consent to the executing of his orders outside a regulated market or a multilateral trading facility by signing the investment services agreement.

The execution policy of the investment firm shall be disclosed entirely and separately to the client.

By submitting an order to the SSIF (investment firm) the client explicitly acknowledges to the investment firm"s execution policy.

## 5. Order confirmation.

For the order execution service, the client shall receive a confirmation on a durable medium (fax, letter or email) at the latest on the first working day following the order execution (if the firm receives confirmation of the execution from a third party, at the latest on the first working day following the reception of the confirmation from this third party).

The confirmation shall contain all the information such as the name of SSIF (the investment service provider) issuing the confirmation, the client"s name, the date, type and nature of the order, the name, the volume and price by unit of the financial instrument, the venue of execution.

The client is informed that, given the time taken to send the confirmation, it should generally arrive within 24 hours. The client is therefore asked to notify the firm if said confirmation has not been received within 48 hours of the order having been passed.

Periodic reports shall include details about price, costs, speed and manner of execution for individual financial instruments[11].

Investment firms shall be able to demonstrate to their clients that they have executed their orders in accordance with the investment firm"s execution policy according to the law.

## 6. Conflicts of interest.

SSIF (investment firm) has a written policy aimed at preventing, identifying and, also, managing in an equitable manner any conflict of interest that may arise during the provision of investment services and activities. The conflicts may arise between the interests of the SSIF and its clients, or between the interests of two or more of its clients.

The expanding range of activities that many SSIFs undertake simultaneously has increased potential for conflicts of interest between those different activities and the interests of their clients.

SSIFs shall take effective steps to identify and manage conflicts of interest and mitigate the potential impact of those risks as far as possible. Where some risk of detriment to the client"s interests remains, clear disclosure to the client of the general nature and sources of conflicts of interest to the client and the steps taken to mitigate those risks should be made before undertaking business on his behalf[12].

## 7. Clients" obligations

The investor who is party to the investment services and activities agreement undertakes to pay the SSIF the remuneration due to it in respect of the activities and services provided. Furthermore, the client shall compensate SSIF for any expense or

[11] Art. 27 para (3), Directive 2014/65/EU.
[12] Preamble, no 56, Directive 2014/65/EU.

damage likely to be (directly or indirectly) borne by the latter.

The investor shall provide SSIF full evidence regarding his identification, the identification of his shareholders, representatives, managers, agents and ultimate beneficiaries of the transactions in compliance with the regulations regarding anti money laundering and the financing of terrorism.

## 8. Distance agreement.

A distance contract means any agreement for the purpose of services and investment activities concluded between an investment firm (S.S.I.F.) as a provider and an investor as a beneficiary of services and investment activities, in the context of a system of sales or service and distance investment activities organized by the SSIF which, for the purposes of that contract, uses only one or more means of distance communication[13] .

Such distance communication represents any means which, without requiring physical presence of the parties (SSIF and the beneficiary of services and investment activities) may be used for the purpose of achieving the agreement of the parties.

The investor has a 14 day term from the day of conclusion of the distance contract to terminate the contract without having to justify the termination decision and without incurring punitive fees.

In the case of unilateral denunciation, the investor may be required to pay the services rendered up to that date, according with the terms of the agreement.

The right of withdrawal from a distance contract shall not apply to investment services and activities the price of which depends on the fluctuations in the financial markets that may occur during the withdrawal period of the contract[14].

## Conclusions.

The investment services and activities agreement shall govern relations between the investor and the SSIF (investment firm) in relation to the supply by the service provider of investment services as defined in MiFID II (Directive 2014/65/EU, Annex I) and national law (Law no 126/2018, Annex 1).

The service provider shall reveal his business on the exchange and commodity markets, as well as financial instruments, securities, money market instruments, unit trusts and types of derivatives instruments that it deals with.

SSIF shall indicate regulated markets, multilateral trading facilities (MTF) or organized trading facilities (OTF) where the transactions are carried out on.

SSIF carries out proprietary trades or it may act in the name of and on behalf of the client.

The investment services and activities agreement shall apply to all transactions concluded by the SSIF carried out at the client"s order.

[13] Art. 60 para (3), (4), Law no 126/2018.

[14] Art. 60 para (8), Law no 126/2018 Fluctuations may be generated by: money market instruments, securities participation in collective investment undertakings, futures contracts, including similar contracts with final settlement in funds, forward rate agreements (FRA), interest rate swaps, exchange rates and shares or options.

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# SHORT ESSAY ON THE LEGAL EFFECTS OF SIMULATED CONTRACTS IN REGARD TO THIRD PARTIES

**Adrian-Gabriel DINESCU**[*]

**Abstract**

*The simulation is a lie born out of the will of the parties to evade showing successors or third parties the truth. The Romanian legislation has a tolerant approach towards simulation, and permits it, in general. The New Civil Code does not sanction the mechanism of simulation with nullity, but offering the rather milder sanction of inopposability. This short paper will strive to give a short analysis on the effects of this simulation upon the third parties – the objective successors and the creditors of the parties. The New Civil Code has numerous stipulations in order to regulate these complex effects as to avoid harming the interests of these third parties who usually act in good faith and gain rights from the parties of the simulation. These parties should and are protected by law, exactly because they acted in good faith. The objective successor of the apparent acquisitor will be protected against the true will of the parties, as, in general this true will harms his interests. Also, this paper will analyze the special situation of the creditors of the apparent seller and of the apparent aquisitor, as their situation can vary according to the person they come into conflict with.*

**Keywords:** *simulation, sham contracts, good faith, third parties and creditors, inopposability*

## 1. Introduction

Simulated contracts are quite an often occurrence in our modern era, as more and more people are participating actively in the civil circuit, acquiring goods and services and trying to fulfill their interests.

The Romanian legislator, observing this increase in activity, in order to better protect individuals from the chaos of private initiative increased regulation. The typical example is the New Civil Code which is packed with stipulations. However this influx of legislation can cause a vicious circle as people, seeing all these norms which limit their possibility to engage in trade and other commercial activities, resort more and more often to the complex mechanism of simulation to hide their true intents.

The simulated contract, containing in its mechanism a duality of contracts - a public but sham contract and a secret, but true one - is well known to its parties, as they voluntarily committed to resort to this "lie". More problematic is the effect of this mechanism on third parties who acted in good faith and contracted with one of the parties of the simulation.

Thus, we consider essential in drawing up a short analysis on the effects of simulation upon these third parties, distinguishing between third parties who acted in good faith and those who manifested bad faith.

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## 2. Types of third parties

First of all we must assess what participants form this category of "third parties" as to distinguish them from the parties who elaborated the simulated contract.[1]

The third parties, in general, are considered to be the people who are rightfully ignorant of the simulated contract, who do not know the existence of the hidden contract - the objective successors of the parties as well as the creditors.

The first category, the objective successors, are persons who inherit assets or rights from another person, but these rights and assets are individually determined and not part of an universality of goods. The objective successor thus gains these rights from the people who owned them previously and must adhere to all obligations linked to these assets or rights.

This category is in opposition to the subjective successor who is merely a continuation of the personality of a person who ended his existence. The subjective successor gains the universality of the rights and obligations of a personal, being also named a "universal successor".

The creditors of a person, unlike all other types of parties or successors of these parties, have merely a general claim on the assets of their debtor, all these assets comprising the entire collateral of the creditor. In case of default by the debtors, the creditor can foreclose on any of the assets of the debtor.

The major problem of the creditor is that he only has this general claim on the assets of the debtor and thus he must pay close attention to him and ensure that the debtor does not enter into fraudulent agreements in order to reduce the number of assets and thus harming the interests of the creditor.

It has also been said that, along with the objective successors, the creditors are more often than not the direct victim of the intention of the parties to simulate[2], the debtor trying through all means to reach a state close to bankruptcy or even bankruptcy in order for the creditor to be unable to fulfill his claim.

## 3. Effects of the simulation regarding third parties

The Old Civil Code had very succinct stipulations regarding this issue, for it had only one article dealing with the problem of simulation and its effects on the third parties, including the creditors and objective successors.

At art. 1.175 C.civ., the Old Civil Code merely stated that the secret contract, as part of the simulation mechanism, cannot be enforced against third parties.[3]

The New Civil Code, however, which came into force on October 1st 2011, has a much more elaborate take on the norms concerning the effects of the simulation against third parties.

Art. 1.290 C.civ. stipulates that the simulation cannot be enforced by the parties, their personal successors, their objective successors, nor by the creditors of the apparent seller against third parties who manifesting good faith gained rights from the apparent acquisitor.

Art. 1.291 par. 1 of the New Civil Code stipulates that the secret contract is not effective against the creditors of the apparent acquisitor who, in good faith, registered their foreclosure proceedings in the land registry

[1] For an analysis of the "*third parties*" in simulation see also F. Baias, "*Simulația – Studiu de doctrină și jurisprudență*", ed. Rosetti, Bucharest, 2003, p. 141.

[2] F. Baias, "*Simulația – Studiu de doctrină și jurisprudență*", Rosetti Publishing House, Bucharest, 2003, p. 154.

[3] See also G. Chivu, "*Simulația în teoria și practica dreptului civil*", ed. Argonaut, Cluj-Napoca, 2001, p. 78.

or obtained a seizure of the asset object of the simulation.

It is worth mentioning that the simulated agreement made up by the parties is not, in the Romanian legal system, subject to nullity, but merely the true will of the parties, the true contract, is inopposable to the third parties who, in good faith, gained rights from a sham owner.

This is in opposition to quite a number of law systems in Europe who deal much more "violently" with this type of fraudulent behavior, declaring the entire simulated operation as null and void and incapable of producing effects against any person.

### 3. 1. What is good faith in matters of simulation?

Entire treaties have been written regarding the notion of "good faith", and in our short essay we cannot even hope to give an accurate and complete definition on this complicated affair.

We shall mention, however, that acting in good faith a person must follow only the paths that the law has permitted him to take and must act seeking only just and reasonable goals.

A person acted in good faith in matters of simulation when he was rightly ignorant of the simulation mechanism. This does not mean that he was negligent or he ignored the existence of the simulation with malice, for his own unjust reason, but rather undertook all means at this disposal to make sure that the apparent contract which he himself bases his decisions on is the true contract, containing the true will of the parties.

For example, if he acquired a house from a seller, only if he acted with good will, in good faith, and he took all the necessary measures, including checking the land registry, as to ensure that the seller is the true owner of the house, will he receive the benefit of inoposability in case the person who sold him the house was only a "strawman" or an apparent owner.

If he was of bad faith, if he knew that the person who sold him the right, was nothing more than an apparent owner, than he will not be protected when the true owner claims his right.

### 3.2. Inopposability of the secret contract in regard to objective successors

Thus, the objective successor, in order to gain the benefits awarded by art. 1.290 C.civ. must always manifest good faith and must enter into an agreement with the apparent acquisitor only manifesting this good will.

The objective successor, thus, gained rights from the apparent acquisitor who himself gained these rights from the apparent seller.

For us to better understand these stipulations we must define the notions of "apparent seller" and "apparent acquisitor".

Simulated contracts, usually, take three forms:

- simulation through the interposing of a third person, a so called "strawman" who although is mentioned as part of the agreement, is merely a front in order to present to the "outside" world an apparent and untrue contract.
- simulation through fictitiousness. The parties of the simulation enter into an agreement which is only apparently real, but in true fact, it is merely a sham contract, the true agreement between parties stating the unreal character of the transaction.
- simulation through disguise. The parties apparently choose a type of agreement (for example, a sale contract), although in reality they chose another type of contract (for example, a donation contract). They simulate reality in order to better protect their interests against limiting factors such as third parties or even the law, when the latter does not permit them to enter

into the real agreement.

The "apparent seller" is party to simulation and chooses to fictitiously enter into an agreement with the "apparent acquisitor", all these parties knowing full well that the apparent contract is a sham one.

The real contract may be a contract in which the parties merely have leased the asset. The parties may have even resorted to a fictitious act, where the true owner is still the "apparent seller" who held onto his rights fully.

It is irrelevant for the objective successors the nature of the contract. The only thing that matters is that they, in good faith and considering the apparent contract, entered into an agreement not with the true owner of the right, but with merely an „apparent aquisitor" and thus with a non-owner.

In the absence of art. 1.290, their position might have been quite precarious, as they would have been extremely vulnerable against the „apparent seller", the true owner of the right.

But this is exactly where art. 1.290 comes in and protects the objective successors from losing their right – if they entered into an agreement with the „apparent aquisitor" and in good faith gained rights from this person who is not the true owner, the true contract, the real but hidden one, cannot be effective against them – they can ignore the true will of the simulation parties.

This is the typical sanction of the simulation mechanism – the true intent of the parties of the simulated contract is not effective against the third party who contracted in good faith the apparent aquisitor.

Thus, the third party, the objective successor of the apparent aquisitor, is protected from losing his right, although he did not enter into agreement with the real owner of that right.

All this is because he manifested good faith and accepted the apparent contract as true.

Of course, between the parties of the simulated contract this situation is difficult, as the apparent acquisitor, knowing full well that he is just a sham owner, chose to sell further on this right in order to gain pecuniary advantages, harming in a deliberate manner the ownership right of the apparent seller, the true owner.

The parties of the simulated contract will have to sort this complex legal situation for themselves, as this is completely irrelevant for the objective successors who gained rights from the apparent acquisitor, in good faith.

They will be able to keep the rights they acquired, as if they had entered into an agreement with the true seller.

### 3.3. Inopposability of the secret contract in regard to creditors

As we mentioned above, the creditors merely have a general claim on the assets of the debtor, they, generally speaking, have no special position or special guarantee concerning these assets and thus are prone to all kinds of fraudulent behavior by the debtor who tries to evade them and not satisfy their claim.[4]

This is why debtors enter constantly into fraudulent agreements, including resorting to simulation in order to trick these creditors into thinking they have no assets.

Knowing full well this behavior, the Romanian lawmaker stipulated that the secret agreement born between two parties who hide their true intentions through a sham, apparent contract cannot be effective against third parties, including creditors.

[4] See also F. Baias & other authors, "*Noul Cod civil. Comentariu pe articole*", CH Beck Publishing House, Bucharest, 2012, the analysis at art. 1.290-1.291 C.civ.

This conclusion can be extracted by interpreting the stipulations at art. 1.289 – 1.291 C.civ. It is worth mentioning that the norms at art. 1.290 and 1.291 in the New Civil Code are special applications of the general rule enshrined at art. 1.289 C.civ. They are nothing more than the materialization of the will of the lawmaker to put an end to several debates concerning the effects of simulation in regard to third parties.

Thus, the main rule will be that the parties and their personal successor cannot oppose the secret agreement in regard to creditors, as they are third parties to the mechanism of simulation.

However, although the legislator has not made this distinction, we must further our study and see if it matters if the claim of the creditor is previous to the simulation or if the claim was born after the secret agreement.

*In the case of the creditor of the apparent seller:*

If the creditor"s claim is previous to the simulated contract, then the above shown articles are fully applicable, even if the creditor knew that his debtor would enter into the secret agreement because he couldn"t do anything about it, he cannot prevent his debtor into entering secret agreements.

It if the creditor"s claim is born after his debtor entered into the secret agreement, than his good faith is essential, because if he knew about the simulation, then he accepted the role of creditor knowing the full extent of his debtor"s assets. In this case, he will have interest in claiming that the true contract is the one effective between parties, as this contract is the one containing the true will of the parties.

If he didn"t know and couldn"t of known about the real contract, then he is of good faith and can act in any way he considers fit, but he mostly will act in the same way, having interest in bringing forth the true contract, as this one ensures that the will of the simulation parties is the true one and that the assets he could foreclose upon are still in the possession of his debtor.

Anyway, in general, the sanction which the law enshrines in this case is not nullity, of course, but rather the creditor, having interest, can ask that only the true contract be effective against him, as it is the true contract.

This is one of the cases in which a third party, does not ask for inopposability of the true will of the parties, but rather for the inopposability of the sham contract, having interest in maintaining the true intent of the parties.

*In the case of the creditor of the apparent acquisitor*

This creditor will, in general, have an interest to ensure that the sham contract will prevail over the true one in relation to any other person.

This is because the creditor of the apparent acquisitor gained rights from the apparent buyer and thus has interest to maintain the apparent contract as it offers him more assets to foreclose upon in case his debtor, the apparent acquisitor, can"t settle his claim.

However, the creditor of the apparent acquisitor must have entered into an agreement with the apparent acquisitor, in good faith, ignorant that his debtor has an asset which is the object of a simulation.

If the creditor of the apparent acquisitor knew that the respective asset is, in reality, not his debtor"s, than he will have the status of creditor of bad faith concerning the simulation and will now be able to ask for the benefit of inopposability.

It may be even the case that the creditor is in collusion with the parties of the simulation, being himself a party and trying to further the dishonest and fraudulent

activity in order to harm the interests of other creditors or objective successors.

In this case, of course, the creditor will be held by the true contract which contains the true will of the parties, as he was truly aware of its existence.

However, is the creditor of the apparent acquisitor is of good faith he will be able to prevent the effectiveness of the real, but hidden contract, but only under the special conditions of art. 1.291 C.civ. : the secret contract is not effective against the creditors of the apparent acquisitor who, in good faith, registered their foreclosure proceedings in the land registry or obtained a seizure of the asset object of the simulation.

Thus, unlike the protection offered by the Romanian lawmaker for the creditor of the apparent seller, the legislator offered the special benefit of inopposability for the creditor of the apparent acquisitor only if he fulfills the conditions mentioned above because of one important factor : the creditor of the apparent buyer will fight to obtain an extra benefit, another asset for him to foreclose upon, while the creditor of the apparent seller will fight to prevent a loss, than of an asset. Between these contrary interests, naturally, the Romanian law maker preferred the person who is fighting to prevent a loss, rather than the person fighting to win further benefits.

### 3.4. Effects of the simulated contract between third parties

The lawmaker of the New Civil Code has not only included norms to settle the relationship between the parties of the simulation and third parties, but also between third parties.

Art. 1.290 stipulates that the true contract cannot be opposed by the creditors of the apparent seller against the third parties, objective successors, who gained rights from the apparent acquisitor.

So in this case, the law states that the objective successors of the apparent acquisitor are preferred rather than the creditors of the apparent seller simply because the first ones, in good faith, gained rights in light of the apparent contract, while the creditors of the apparent seller will bring forth the true will of the parties. This true will manifested in the true, but hidden contract, cannot be made effective against the objective successors who entered into an agreement with the apparent acquisitor considering, in good faith, that the sham contract is real.

On the other hand, art. 1.291 par. 2 stipulates that when there is conflict between the creditors of the apparent seller and the creditors of the apparent acquisitor, the first ones are preferred if their claim is previous to the sham contract.

Indeed, this position of the lawmaker is contrary to the previous one, giving priority not to the creditors of the apparent acquisitor who considered, in good faith, the apparent contract to be the real one, but rather to the creditors of the apparent seller.

This is because, as mentioned above, the creditor of the apparent seller is generally the direct ”victim” of the simulation and he fights against a loss, while the creditor of the apparent acquisitor fights only to enrich the assets of this own debtor.

## 4. Conclusions

The typical effect against third parties of the simulation is usually inopposability of the true will of the parties, as the sham, but apparent contract will be the only one to be effective against these third parties because it is the only one who is shown to the world and any person, entering into an angreement with the parties of the simulation will know only of the apparent contract and not of the true will of the parties.

Thus, the Romanian lawmaker gave this important benefit to the third parties taking into consideration that they acted in good faith and deserve to win against the fraudulent intent of the parties who chose to "lie" in order to protect their interests.

However, as we have seen, difficulties may appear when third parties have conflicting interests, some having interests to uphold the real, but hidden contract, while others choosing to uphold the sham, but apparent contract.

In this situation the New Civil Code offers us just solutions, trying to curtail the myriad of interpretation given in the past by the Romanian courts as well as the Romanian law literature.

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# PRINCIPLES REGARDING STATE JURISDICTION IN INTERNATIONAL LAW

**Oana – Adriana IACOB***

**Abstract**

*The concept of state jurisdiction in international law is based on the principle of sovereign equality, establishing that each state enjoys the exclusive right to exercise authority (with the obligation of non-interference for other members of the international community) over a given territory, its population and its goods, as well as over events and acts committed within its territorial boundaries. The central focus of the present paper is jurisdiction, regarded as a manifestation of sovereignty, referring to the state competence to legislate and apply law to particular events, persons and property. Traditionaly, jurisdiction has been tightly connected to the concept of territory. However, of particular interest is what happens in situations that involve elements of extraneity, when several states claim jurisdiction over a certain event. In this sense, the five principles governing the exercise of state jurisdiction in criminal law matters will be analysed.*

**Keywords:** *jurisdiction, sovereignty, principle of territoriality, principle of nationality, principle of universality*

## 1. Introduction

In an international community characterized by polyarchy and, at the same time, by the interdependence between its members, there are two types of interests and concerns in balance - international concerns of the general community and states" particular interests. In the doctrinal analyses of authority in the international order two perspectives on the allocation of authority[1] have been described: on one hand, a vertical allocation of authority between the general community and the particular states – focusing on addressing international concerns – and, on the other hand, a horizontal allocation of authority between the different states in a (still) very state-centered world, governed by the principle of sovereignty.

According to the principle of sovereign equality – basic principle of international law and fundamental pillar of the existing international order – all states, regardless of their differences and asymetries in areas such as military power, geographical and population size, levels of industrialisation and economic development, have equal rights when it comes to the exercise of sovereignty, at international level, as independent entities in relation to other states, and at internal, domestic level, as authorities solely endowed with the competence of exercising power over a particular territory, as well as population, property and events within their territorial boundaries.

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[1] Lung-Chu Chen, *An introduction to contemporary international law. A policy oriented perspective,* Third Edition, Oxford University Press, 2015, pp. 269 – 277.

Although the concept of jurisdiction may seem rather technical, referring to procedural applications of domestic law and practical delimitations of competences between states, it is, actually much more than that.[2] The concept of state jurisdiction refers to the allocation of power between the members of the international community, being rooted in the principle of sovereignty of states.

Although the actual term is quite generic and has been used in a variety of senses in the literature of international law, there are, basically, three (interrelated) types of jurisdiction that a state can exercise:

- Legislative/ prescriptive jurisdiction – to elaborate laws applicable to everyone and everything within its territorial boundaries;
- Enforcement jurisdiction – to enforce its laws and regulations against those who breach them;
- Adjudicatory jurisdiction – to exercise judicial authority within its territory.[3]

Traditionally, the concept of jurisdiction was tightly and inevitably related to the concept of territory ("jurisdiction as a mist above the swamp of territory")[4], revolving around the power of states. In this classical view, jurisdiction became a matter of international law only when it involved elements of extraneity (for instance, activities taking place abroad), having to do with another state"s territorial authority. The major concern was that such extraterritorial elements could lead to conflicts between states. So, in matters of jurisdiction, territoriality was seen as the valid rule, while extraterritoriality was considered suspicious (if not unlawful).[5] This has been the most widely accepted view on jurisdiction for a very long time. However, the increasing interdependence between states has generated a shift in the conception on jurisdiction in international law.

In some instances, it occurred that the exercise of jurisdiction by a particular state came in conflict with the right invoked by another state to exercise jurisdiction on the same issue. Therefore, between the respective states arose a jurisdictional difference. Over the years, international law evolved towards establishing means of resolution for such differences (either conventional or accepted as customary).[6]

The analysis contained in the present paper focuses on this type of situations, on the rules applicable for their resolution and the controversies that they arise in the practice of states.

## 2. Principles of jurisdiction

Jurisdictional differences in civil law matters are, usually, resolved in accordance with rules of private international law, elaborated and implemented by the state.

On the other hand, criminal law matters are tied to a greater extent to the public sphere and, thus, jurisdictional conflicts of such type lead to specific effects in international law.

A major turning point in the law of jurisdiction (that has influenced international law"s approach on the matter ever since) was the 1935 *Harvard Research Draft Convention on Jurisdiction with Respect to Crime*, published in the American

[2] Cedric Ryngaert, *Jurisdiction*, available at https://unijuris.sites.uu.nl/wp-content/uploads/sites/9/2014/12/Jurisdiction.pdf, accessed 12.04.2019.

[3] Ademola Abass, *International law. Text, cases and materials*, Second Edition, Oxford University Press, 2014, p. 239.

[4] Cedric Ryngaert, *op. cit.*, p. 1.

[5] Ibidem, p. 2.

[6] Ademola Abass, *op. cit.*, p. 239.

Journal of International Law.[7] The Harvard Draft enunciates a series of principles of jurisdiction: territoriality, nationality, protection – security and universality.[8] The "star" of the Harvard Convention remains, of course, territoriality, extraterritorial jurisdiction being considered (still) an anomaly in need of strong justification.

In practice, over time, the principles enunciated by the Harvard Convention have been contested and subjected to a variety of interpretations. Of course, the most widely accepted and applied among states has been the principle of territoriality, according to which a state is authorized to legislate and apply its laws to all events taking place within their borders, regardless whether these events involve nationals or non-nationals of the respective state. Nevertheless, the principle of territoriality sometimes clashed with other jurisdictional principles.

For instance, in the 1988 Lockerbie incident, in which an US airliner was bombed by two Libyan nationals in Lockerbie, Scotland, UK, leading to the deaths of 270 people of different nationalities, there were several claims of jurisdiction over the event: UK claimed jurisdiction because the incident took place on its territory; US did the same, based on the fact that an US registered aircraft was bombed and many of the victims were US citizens; also Libya expressed its intention to prosecute the two suspects, under its domestic law, based on their Libyan nationality.[9] Such intricate jurisdictional differences create many controversies in international practice and doctrine.

### 2.1. The principle of territoriality

As showen above, according to the principle of territoriality, a state can exercise jurisdiction over everything and everyone within its territorial borders, with some notable exceptions provided by customary or conventional international law (such as, for instance, the case of diplomatic missions premises, under the provisions of the 1961 Vienna Convention on diplomatic relations). Thus, the state exerts comprehensive and continuing authority over its territory (including internal waters, territorial sea and airspace). The wide preference of states for this principle reflects the importance of territoriality in the present-day state system.[10] Actually, the exercise of territorial jurisdiction seems to be an essential and very visible way of manifesting state sovereignty.

However, in practice, the implementation of the principle is often not so easy and clear-cut. What happens, for example, if the crime is initiated on the territory of a state and completed on the territory of another state? In the Lockerbie incident mentioned above, for example, it was believed that the bombs which exploded in the airliner were loaded in Malta, although the explosion took place in UK.[11] Could Malta have had the right to claim jurisdiction, based on the fact that part of the crime was committed on its territory, also violating its domestic norms?

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[7] Dan Jerker B. Svantesson, *A New Jurisprudential Framework for Jurisdiction: Beyond the Harvard Draft*, AJIL Unbound, vol. 109, 2015, p. 1, available at https://www.asil.org/sites/default/files/Svantesson%2C%20A%20New%20Jurisprudential% 20Framework%20for%20Jurisdiction%2C%20Beyond%20the%20Harvard%20Draft_print.pdf, accessed 12.04.2019.

[8] *Draft Convention on Jurisdiction with Respect to Crime*, The American Journal of International Law, Vol. 29, Supplement: Research in International Law (1935), pp. 439-442.

[9] Mitsue Inazumi, *Universal Jurisdiction in Modern International Law: Expansion of National Jurisdiction for Prosecuting Serious Crimes under International Law*, Intersentia, Antwerpen – Oxford, 2005, p. 165.

[10] Lung-Chu Chen, *op. cit.*, p. 281.

[11] Ademola Abass, *op. cit.*, p. 241.

In such cases, the doctrine and practice of international law does not offer a generally agreed answer. There are two theories suggesting two types of jurisdiction tests to be applied in this kind of situations: the objective test theory and the subjective test theory.

According to the objective test, also known as the "terminatory theory", if a crime was completed on the territory of a state, the latter has the right to exercise its jurisdiction, regardless of where the crime was initiated. It is probably the most favoured theory of the two. An argument formulated in the specialized literature to sustain the terminatory theory is the fact that "the state where the last element of the crime occurs is presumably the sufferer from it, and therefore has the greatest interest in prosecuting it".[12]

The subjective test or the "initiatory theory" suggests that a state can claim the exercise of its jurisdiction if the crime was initiated on its territory, regardless of where it was actually completed. The subjective test proved to have an important practical utility, especially in cases of transborder crimes (terrorism or money laundering).[13]

Another variation on the principle of territoriality is the "effect doctrine", according to which a state has jurisdiction over a crime if its effects are felt on its territory, regardless of the fact that it was not initiated, planned or executed in that respective state. Also, according to the effect doctrine, it is irrelevant whether that particular conduct was lawful in the state in which it was executed.[14] In *LICRA v. Yahoo! (The Yahoo! Auctions Case, 2000),* for instance, two non-profit human rights groups – LICRA (Ligue contre le Racisme et l"Antisemitisme) and UEJF (Union des Etudiants Juifs de France) – filed a lawsuit against Yahoo! in a French court in Paris, because it allowed the auction of Nazi memorabilia on its website, which was accessible to French citizens. The two organizations claimed it violated the French law that incriminates the offering, wearing or public exhibition of Nazi related items under the French Penal Code. Given the fact that Yahoo! is based on the US territory and the acts were not committed in France, the company contesteted the jurisdiction of the French court. Nevertheless, the court rejected Yahoo!"s contestation, finding it had jurisdiction, because the company"s conduct caused damage that was suffered in France.[15] Naturally, the effect doctrine sparked some controversies, leading to efforts to limit its application only in cases in which the primary effect or a substantial effect of a crime is felt in a particular state.[16]

### 2.2. The principle of nationality

The principle of nationality allows a state to impose its jurisdiction on its nationals, wherever they may be: on the the territory of their state, outside the territory of their state and any other states (high seas and airspace over high sea, for instance) or on the territory of another state (with permission). According to this principle, the fact that a state"s nationals have the duty to obey its laws even when they are outside its territory entitles that state to regulate their conduct anywhere.

[12] Glanville Williams, "Venue and the Ambit of Criminal Law" (1965) 81 Law Quarterly Review *apud* Ademola Abass, *op. cit.*, p. 242.

[13] *Ibidem*, pp. 243 – 245.

[14] *Ibidem*, p. 248.

[15] Marc H. Greenberg, *A Return to Lilliput: The LICRA v. Yahoo - Case and the Regulation of Online Content in the World Market*, „Berkeley Technology Law Journal", vol. 18, no 4, September 2003, available at https://scholarship.law.berkeley.edu/cgi/viewcontent.cgi ?article=1435&context=btlj, accessed 10 April 2019.

[16] Ademola Abass, *op. cit.*, p. 248.

The principle of nationality regards not only natural persons – human beings (based on their relation of citizenship with the respective state), but also juristic persons – corporations, ships, aircraft, spacecraft (based on a relation of nationality).

Concerning the nationality of ships, it has been recognized as that of the flag state – the country of registration (although it is most often related to the fiction of territoriality[17]).

The nationality of aircraft, as regulated by the 1944 Chicago Convention on International Civil Aviation, is the state of registration. According to the 1963 Tokyo Convention on Offenses and Certain Other Acts Committed on Board Aircraft, the state of registration has exclusive competence to legislate and enforce its laws on acts committed on board of their ships.[18]

Regarding objects launched into space, the 1967 Outer Space Treaty does not regulate their nationality, but it stipulates that the control and jurisdiction over these objects and the personnel thereof are exercised by the state of registration.[19]

Referring to crimes or offences committed by individuals or corporations on the territory of another state, the principle of nationality proved to be particularly useful when the state where the act was committed refused to prosecute it because, for instance, it was not incriminated according to its domestic laws or, although it was incriminated, the respective state was simply unwilling or uninterested to do it (for example, in child trafficking cases, in some countries where these crimes are either not properly regulated or their prosecution is generally lax).[20] In such cases, the application of the nationality principle allowed the prosecution of the offenders in their countries of citizenship.

The nationality principle has also been very usefully employed in issues of private international law, in cases of evasion of the law, when a state"s domestic legislation forbids certain acts and, in order to avoid these provisions, its national simply commits the acts in another state where the legislation does not contain such legal restrictions (for instance, to circumvent legal conditions related the conclusion of a marriage or divorce). In this type of situations, the nationality principle allows a state to enforce its legislation on its nationals wherever the acts are committed (in such cases, a divorce or a marriage concluded abroad may not be recognised by the state of nationality if they breach its legal restrictions).

### 2.3. The protective principle

According to the protective principle, a state can exercise its jurisdiction over acts committed abroad by their nationals or by foreign citizens, if those acts threaten the interests, security or functioning of the respective state. Although the protective principle bears some similarities with the effect doctrine mentioned above, the main difference is that the former contains no requirement that the effect of the offence should be felt on the territory of the state that claims to exert jurisdiction.[21]

Articles 7 and 8 of the Harvard Draft Convention refer to the protective jurisdiction of states in cases of crimes against "the security, territorial integrity or political independence" of states or acts of "falsification or counterfeiting, or uttering of falsified copies or counterfeits of the seals,

[17] Lung-Chu Chen, *op. cit.*, p. 282.
[18] *Ibidem.*
[19] *Ibidem.*
[20] Ademola Abass, *op. cit.*,pp. 248 – 250.
[21] *Ibidem*, p. 250.

currency, instruments of credit, stamps, passports or public documents, issued by the state or under its authority."[22]

There was an initial reluctance towards invoking this principle, but, in the 1960s, it became more popular (especially for the USA). For instance, in 1985, Alfred Zehe, an East German citizen was prosecuted under US jurisdiction for acts of espionage against the USA, committed in Mexico and in the German Democratic Republic.[23]

The protective principle proved its usefulness in highly sensitive issues. Nevertheless, there were instances in which the invocation of the principle was rather dubious, potentially undermining its integrity.[24]

### 2.4. The principle of passive personality

The principle of passive personality is the most controversial of all. It was not included among the principles of jurisdiction in the Harvard Draft Convention, one of the reasons being that it could be partially included in the principle of universality.

The principle of passive personality allows a state to exercise its jurisdiction over an act committed abroad by a foreigner, if the respective act injures a national of that state. It is linked to the principle of nationality, but in a somehow reverse manner: while in the case of the principle of nationality, the national is the perpetrator, in the principle of passive personality, the national is the victim. It also resembles to some extent the protective principle, but while in the latter"s case the interests and security of the state are affected, in the former"s case the interests of the nationals of that state are injured.

There were some early and notable assertions of this principle. One case that is considered the *locus classicus* of the passive personality principle is the *Cutting Case* (1866). In this case, Mr. Cutting, an American citizen, published in a Texan newspaper, some offensive materials about Mr. Barayd, a Mexican national, an act which was a breach of the Mexican Penal Code. Mr. Cutting was subsequently arrested, while entering Mexico, and charged with breaching the Mexican law. Mexico claimed it had jurisdiction over the case, based on the principle of passive personality. Of course, the United States strongly opposed Mexico"s claim and the case caused some frictions between the two states. Mr. Cutting was later released, because the injured party withdrew the charges. So the case was inconclusive in regard to the application of the principle.

Perhaps the most notable assertion of the passive personality was in the *Lotus Case* (1927), brought before the Permanent Court of International Justice (PCIJ). The case referred to an incident that took place on August, the 2nd, 1926, in which S.S.Lotus, a French steamer, collided with S.S. Bozkurt, a Turkish steamer, in the high seas (north of the Greek city of Mytilene), causing the sinking of the Turkish vessel and the deaths of eight Turkish nationals. Turkey claimed jurisdiction over the event, based on the nationality of the victims (passive personality principle), and wanted to prosecute the French officer who was thought to be at fault for the collision. France opposed Turkey"s claim, contending that, as flag state, it had jurisdiction over the matter (the principle regarding the jurisdiction of the flag state in such cases was later

[22] *Draft Convention on Jurisdiction with Respect to Crime*, The American Journal of International Law, Vol. 29, Supplement: Research in International Law (1935), pp. 439-442.

[23] Ademola Abass, *op. cit.*, p. 251.

[24] For instance, protective jurisdiction invoked by the USA and Germany in cases involving selling and importing of cannabis (Ademola Abass, *ibidem).*

stipulated in the 1958 Geneva Convention on the High Seas). The case was brought before the PCIJ and the Court decided that there was no rule of international law, at the time, stipulating that criminal proceedings regarding collisions at sea are exclusively within the jurisdiction of the flag state and, therefore, because there was no such prohibitory rule, Turkey had not violated international law by instituting criminal proceedings against the French officer (Lotus principle - states can act as they wish unless the conduct is explicitly prohibited in international law).[25] However, the majority of the PCIJ judges rejected Turkey"s justifications, which were based on the principle of passive personality, considering that Turkey had other grounds for holding the French officer liable (effect doctrine or impact territoriality). So, the court"s decision was not conclusive on the passive personality principle issue.

Spain had an interesting approach on the passive personality principle in the *Guatemala Genocide Case*. In 1999, an action was brought before a Spanish court concerning acts committed by certain officials of Guatemala, between 1978 and 1990, in Guatemala, against the Mayan indigenous population. The acts constituted the crime of genocide. During the course of events, some Spanish nationals were also tortured and killed. The Spanish court refused to exercise jurisdiction based on the principle of passive nationality, arguing that the nationality of the victims can not be the sole foundation for the jurisdiction claim. Another essential criterion must be met: the crime invoked before the Spanish court must be the same as the one that forms the basis of the jurisdiction – genocide. The latter criterion was not met in the case, since the Spanish nationals had not been victims of genocide.[26]

As mentioned above, it was considered that there was an overlapping between the passive personality principle and the principle of universality. Thus, the former was seen as somehow redundant. In the *Eichmann Case*, Adolf Eichmann, one of the major organizers of Hitler"s final solution, was captured by the national intelligence agency of Israel (the Mossad) in Argentina, and prosecuted under Israeli jurisdiction. He was found guilty of the commission of war crimes and subsequently executed by hanging (1962). Israel invoked the universality principle as basis for its jurisdiction, but, nevertheless, the District Court of Jerusalem later justified its competence on the ground that the main victims of the defendant"s crimes were Jews.[27]

A case in which the passive personality principle was asserted alongside the universality principle was *Yunis Case*. In this case, Mr. Yunis, a Lebanese citizen, and several accomplices, hijacked a Jordanian airplane in Beirut, in June 1985. The airplane was flown to some locations in the Mediterranean Sea and, eventually back to Beirut were it was blown up. Several victims were American citizens (this was the only actual, direct connection between the event and the United States). The United States went on to prosecute Mr. Yunis, invoking as basis for its jurisdiction the principle of universality (given the international provisions that condemn these sort of heinous acts) and (contrary to their earlier reluctance towards it) the principle of passive personality.[28]

[25] https://intlaw.co.uk/lotus, accessed 14.04.2019.
[26] Ademola Abass, *op. cit.*,pp. 258-259.
[27] Lung-Chu Chen, *op. cit.*, p. 284.
[28] https://www.casebriefs.com/blog/law/conflicts/conflicts-keyed-to-currie/international-conflicts/united-states-v-yunis/, accessed 14.04.2019.

In the practice of states, it was observed that the principle of passive personality can, unfortunately, lead to more jurisdictional differences, especially if the acts are also incriminated in the state where they were committed and/or in the state of nationality of the perpetrator. However, it can be particularly useful in case the latter states are unwilling or unable to exercise jurisdiction.

### 2.5. The principle of universality

A state is entitled to exercise universal jurisdiction over crimes that constitute a threat to the common interests of mankind, regardless of who committed the crimes, where they were committed and who were the victims. These are acts that, because of their gravity, affecting vital interests of the international community, can be prosecuted by any state, which apprehends or exercises effective control over the perpetrator. No conditions regarding nationality or territoriality are imposed in these cases. What matters is the nature of the crime, that causes universal concern.[29]

The universality principle has a special character that differentiates it from other bases of jurisdiction. The other principles of jurisdiction analysed above derive from national entitlements to legislate and implement law (for instance, entitlements based on a link of territoriality or nationality). Meanwhile, universal jurisdiction is based on an entitlement shared with other states, to implement and enforce international provisions that incriminate universal crimes. So the state exercising universal jurisdiction is simply an enforcer of legal international commitments, without any power of its own to decide which conduct falls under universal jurisdiction and in what conditions.[30]

Moreover, the universality principle goes beyond the classical dichomoty territorial-extraterritorial. Universal jurisdiction is neither territorial, in the traditional sense, nor extraterritorial. It is more of a "comprehensive territorial jurisdiction", based on international proscriptions that are universally applicable.[31]

The category of universal crimes is not new *per se,* although the number of offenses included in this category has always been rather low. The first (and, until relatively recently, the only) crime of universal jurisdiction was piracy. Acts of piracy occurring in the high seas – a space that does not fall under the jurisdiction of any state – were considered to pose a threat to all states. Prosecuting crimes of piracy was, basically, left to the state that apprehended the perpetrator. Although, initially, the incrimination had a customary nature, piracy was later regulated through conventional norms – the 1958 Convention on the High Seas and the 1982 Law of the Sea Convention.

After the Second World War, the category of universal crimes expanded, with the creation of the first international criminal tribunals in Nurenberg and Tokyo, and it is now considered to include the most serious breaches of human rights and humanitarian law, such as crimes against humanity, war crimes, genocide, apartheid, and certain crimes of terrorism. Most of these are nowadays incriminated through conventional norms, although some of them have had a prior customary reglementation. For instance, after the war, the principles of the Nurenberg Charter and Judgement

[29] Ademola Abass, *op. cit.*,pp. 252.
[30] Anthony J. Colangelo, *Universal Jurisdiction as an International "False Conflict" of Laws,* Michigan Journal of International Law, vol. 30, issue 3, 2009, p. 882.
[31] *Ibidem,* p. 883.

defined crimes against peace, war crimes and crimes against humanity (at the time, the latter were only considered as such if they were committed in relation to a war). In 1948, the Convention on the Prevention and Punishment of the Crime of Genocide was adopted, and, in 1973, the International Convention on the Suppression and Punishment of the Crime of Apartheid. The Statute of Rome of the International Criminal Court came into force in 2002, incriminating the crime of genocide, crimes against humanity (this time, with no requirement of any relation to a war), war crimes and (without a clear definition) the crime of aggression. Terrorism is considered an international crime, falling under the universal jurisdiction. However, there is no generally accepted definition of terrorism, but only various international proscriptions incriminating different terrorist acts. A resolution adopted by the UN General Assembly in 1985 (GA Res. 40/61), "unequivocally condemns, as criminal, all acts, methods and practices of terrorism wherever and by whomever committed".[32] Terrorist acts have also been included in the Draft Code of Crimes against Peace and Security of Mankind, elaborated by the International Law Commission, in 1996.[33]

Such crimes can, thus, be prosecuted by any state, according to the universality principle, based on states" recognized, shared competence to impose criminal or civil sanctions with respect to what is proscribed by the international law.

Given its specificity, the universality principle should not lead to jurisdictional conflicts between states (as mentioned above, in universal jurisdiction, states are merely enforcers of international law). Nevertheless, its implementation was not without controversy, especially since the category of universal crimes is quite dynamic and in continuous evolution.

For instance, more recently universal jurisdiction has been invoked in respect of human rights violations, based on the argument that "some human rights have become *erga omnes* obligations. One important precedent of universal jurisdiction in this field, with an enormous impact in international law, was the *Filartiga v. Pena-Irala Case*, brought before an American court. In 1978, Dolly Filartiga, a citizen of Paraguay, resident in the United States, lodged a civil complaint before an US court against Americo Norberto Pena-Irala, also a national of Paraguay, former Inspector General of Police in Asuncion. Pena-Irala was, at the time, in the USA, waiting for deportation, after remaining on the American territory past the expiration of his visitor"s visa. Filartiga contended before the court that, in 1976, her seventeen year old brother, Joelito Filartiga, was kidnapped and tortured to death by Pena-Irala, as retaliation for the political activities of their father. Initially, the complaint was dismissed, but, in 1980, the US Court of Appeals for the Second Circuit ruled in favor of Filartiga, considering that "freedom from torture is protected under customary international law, which forms a part of the law of the land in the United States."[34] The court declared:

*"Among the rights universally proclaimed by all nations, as we have noted, is the right to be free of physical torture. Indeed, for purposes of civil liability, the torturer has become like the pirate and slave trader before him hostis humani generis, an enemy of all mankind."*[35]

[32] GA Res. 40/61 available at https://www.un.org/documents/ga/res/40/a40r061.htm, accessed 16.04.2019.

[33] *Draft Code of Crimes against Peace and Security of Mankind,* available at http://legal.un.org/ilc/texts/instruments/english/commentaries/7_4_1996.pdf, accessed 16.04.2019.

[34] Lung-Chu Chen, *op. cit.,* p. 287.

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Thus, the ruling in the Filartiga case was an endorsement that torture is considered an international crime, subject to universal jurisdiction.

Another case with a huge impact, which marked a watershed in international law was the *Pinochet Case*. General Augusto Pinochet, former Chilean head of state between 1973 and 1990, was arrested in 1998 in London, based on an international arrest warrant issued by a Spanish Court (*Audiencia National)* for human rights violations committed in Chile. Pinochet invoked before the Law Lords of the House of Lords (that was then the highest British Court) immunity from prosecution as a former head of state. However, the British court rejected Pinochet"s claim, reasoning that crimes such as hostage taking and torture could not be protected by immunity. This was the first time the principle of universal jurisdiction was applied in such a manner, against a former head of state.

## 3. Conclusions

The rules regarding state jurisdiction in international law, traditionally, seek to establish the allocation of competences between sovereign states, based on legitimate jurisdictional links (like territoriality or nationality), ultimately aiming to prevent normative conflicts. The five identified principles of jurisdiction brought some order and predictability in international relations[36], but they are, nevertheless, dynamic, unstable and open to interpretations and controversies.

Among the principles of jurisdiction, territoriality remains the most important and widely accepted in a world that is still state-centered, governed by the principle of equal sovereignty. However, jurisdiction refers to the exercise of power, reflecting the preferred model of governance of a certain time. In a polyarchic, sovereignty-centered international society, it is no wonder that territoriality remains the preferred principle of jurisdiction. But the increasing interdependence between the members of the international community, the advances in technology and communication, that create a more and more interconnected world, could lead to a shift in the way the exercise of power is perceived and, subsequently, to a shift in the law of jurisdiction.

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# IMPACT OF DIGITALIZATION ON THE REGULATION OF FINANCIAL MARKETS[1]

**Zoltán NAGY***

**Abstract**

*The study examines the impact of digitalization on the money market, primarily from a regulatory perspective. New digital financial services pose a challenge for both supervisors and legislators when they are performed by unregulated financial services providers. The article points out these challenges and examines how legislation responds to them. The problem will be analyzed in the case of the European Union and also Hungary. Comprehensive solutions have not yet been found, but there are attempts to address the problem. The findings of the study may help to further examine the topic and find new solutions.*

**Keywords:** *Digitalization, Financial Market, Financial Services, Innovation Hub, Regulatory Sandbox.*

## 1. Introduction

Technological advancement and innovation are rapidly infiltrate in the industrial, commercial and service sectors. Within the service sector, the financial sector has also undergone constant transformation, and as a result of development, digitalization has transformed financial services in many areas. However, this technological development has taken place within the sector and has been progressing continuously but slowly. The financial and economic crisis has also set these processes aside by the transformation of resources and regulation. From a resource point of view, bank profitability problems hindered innovation developments[1], and banks had to devote their resources to covering the losses resulting from the crisis, leaving them with neither the determination nor the financial capacity to face the challenges of digitization. At the same time, the financial economic crisis also meant a crisis of confidence, which led to a decline in consumer confidence regarding the financial services of the banks, which strengthened their turn away from banks and the search for new financial solutions.

In addition, accelerated digitalization and widespread networking[2], Internet-

[1] This research was supported by the project nr. EFOP-3.6.2-16-2017-00007, titled Aspects on the development of intelligent, sustainable and inclusive society: social, technological, innovation networks in employment and digital economy. The project has been supported by Eurpean Union, co-financed by the European Social Found and the budget of Hungary.

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[1] Eszes Dorottya-Sajtos Péter-Szakács János-Törő Ágnes: A digitalizáció hatása a bankrendszerre, in: *Bankok a történelemben: innovációk és válságok* (szerk.: Fábián Gergely-Virág Barnabás), Budapest, Magyar Nemzeti Bank, 2018, p. 625

[2] Barabási Albert-László: *Behálózva- A hálózatok új tudománya*, Budapest, Libri Kiadó, 2003, pp. 216-220 The author points out that network science is important not only in mathematics and physics, but also in other disciplines.

enabled services, and the strengthening of technology firm"s role in the money market have fueled the money market. The changing economic situation and the emergence of new technology players have created new challenges and competition for financial services providers in the money market.[3] The focus is no longer on the importance of internal technological developments, but on technological innovations of external nonbanking players, which are spreading faster as new generations enter the market, where digitalization and electronic services have a significant market advantage. FinTech innovators, technology companies are emerging on the market, providing financial services via the Internet through the introduction of new technologies. The literature deals with the development of the coming period in several ways. There are three types of output that technology companies can bring to the financial market. If new service technology companies emerge in underdeveloped financial markets, they may face strong competition or crowd out traditional financial service providers. But in advanced financial markets, it is possible to cooperate or even buy another provider.[4]

Technological development also poses a challenge to the legal framework. It is necessary to create a regulatory environment in a highly regulated area which allows the development of services while preserving the operational security of the financial market, ensuring a level playing field for market participants and protecting consumer interests.

Important areas for regulation in connection with technological developments are the emergence of digital money, community funding, new financial services and the emergence of robot advisors.

## 2. Analysis of the Impact of Financial Technology at EU Level

The concept of FinTech (financial technology) has come to the international literature as an accepted concept, although there is no uniform definition for it. Literature approaches financial technology as a broad concept that includes digital ledger technology, robot consultants, compliance and data provision technologies, and virtual money.[5] It is, in fact, the application of innovative digital technology in financial services, embracing the technology-driven development of the entire financial sector.[6]

However, financial innovations are not entirely new, occurring within financial service providers or induced by external technology companies. By the end of the 19th century, we were talking about financial technology, as telegraph and later the phone had already connected financial service providers and customers. The modern beginnings of the development of

Beyond the structure of companies, networks play an increasingly important role in each market. The question is whether a company can adapt to these rapidly changing market conditions. Companies that use strategies which includes the utilization of networks have an advantageous market power.

[3] Richard Scott Carnell-Jonathan R. Macey- Geoffrey P. Miller: *The Law of Financial Institutions*, New-York, Wolters Kluwer, 2013, pp. 183-187

[4] Eszes-Sajtos-Szakács-Tőrös: i.m. p. 626

[5] Kerényi Ádám-Müller János: *Szép új digitális világ? - A pénzügyi technológia és az információ hatalma*, Hitelintézeti Szemle, 18.évf.1.szám, 2019. március, pp. 7-8

[6] Innováció és stabilitás- FinTech körkép Magyarországon, MNB Konzultációs dokumentum, 2017, mnb.hu/letoltes/konzultacios-dokumentum.pdf. (Last access: 2019.07.07.) According to the Financial Stability Board, FinTech is a technology-driven financial innovation that can result in new business models, applications or products that can have a significant impact on financial markets and institutions, as well as financial services.

financial technology were the advent of cash dispensers and the application of digital technology in the financial market. Digitized products and transactions result in automated processes that transform financial services.[7] All these processes have contributed to the globalization of the financial market. A new era in the development of financial technology is institutional change. Following the 2008 economic crisis, technology companies have entered the financial market and financial services are not provided only by regulated, traditional financial market players. New products and services appear on the market, creating competition for traditional operators.[8]

There were several reasons for the emergence of new technological solutions and new entrants.[9] The literature points out that this includes changing consumer habits. The technological background and the spread of the Internet have affected the consumer habits of the new generation. Internet banking and commerce on the Internet have transformed the financial services market. The new consumer prefers the technology, which may be provided by a technology firm that is emerging on the money market. Loyalty to an institutional service provider is less dependent on where and how they use the services.

Another important factor is the extensive and rapid technological development. The spread of digital services is increasingly enabled by the technological background. The development of software and hardware backgrounds is shifting financial services providers towards services available via mobile phones that function as computers. In addition, there was a great deal of innovation made possible by blockchain technology. This enabled financial transactions to be carried out without the intervention of a general ledger or service provider.[10]

It is important to highlight the macroeconomic and regulatory environment, in agreement with the literature. As a result of the financial and economic crisis, the regulatory environment for financial markets has changed, with strong, rigorous regulation in place in some states that served to reduce risks and was less receptive to innovation, and to restore liquidity for banks, as opposed to the development of new innovative services. The result of this regulatory attitude has been that new innovative services have emerged outside the banking system, which in return are carried out by technology firms without strict financial market regulation. The literature defines this phenomenon as the shadow banking system. The term refers to service providers (mostly technology firms) that provide financial services as nonfinancial institutions.[11]

[7] V. Gerard Comizio: *International Banking Law*, St.Paul, West Academic Publishing, 2016, pp. 336-339

[8] Gál Zoltán: A nemzetközi pénzügyi rendszer fenntarthatóságának kihívásai és a FinTech forradalom, in: Környezet-Gazdaság- Társadalom Tanulmányok Kerekes Sándor 70.születésnapja tiszteletére (szerk.: Parádi-Dolgos Anett-Fertő Imre-Marjainé Szerényi Zsuzsanna-Kocsis Tamás-Bareith Tibor), Budapest, Agroinform Kiadó Kft., 2018, pp. 86-89

[9] Kerényi Ádám-Molnár Júlia: A FinTech-jelenség hatása-Radikális változás zajlik a pénzügy szektorban? Hitelintézeti Szemle, 16.évf.3.szám, 2017.szeptember, p. 34-38 The authors list changing consumer habits, revolutionary innovation, technological development, and the macroeconomic and regulatory environment as reasons for it.

[10] Győrfi András- Léderer András-Paluska Ferenc-Pataki Gábor-Trinh Anh Tuan: Kriptopénz abc, Budapest, HVG Kiadó Zrt, 2019, pp. 57-68

[11] Kecskés András-Zéman Zoltán: Az árnyékbankrendszer klasszikus és jövőbeni kihívásai Magyarországon, Gazdaság és Pénzügy 2018/4. The authors point out that investment banking activities are intertwined with

The European Union is also looking for answers to technological and market challenges.[12] EU regulation extends financial technology to the entire financial sector, meaning that the financial operations provided by the technology range from banks to insurance companies, pension funds, investment advice to market infrastructure.

This financial technology offers significant benefits:

- faster, cheaper, more transparent and better financial services,
- creation of new financial services, opportunities,
- increasing the cost-effectiveness of the financial system,
- lower service prices,
- development of alternative lending and investment channels,
- develop the single EU financial market.

At the same time, technological development is a challenge for EU regulation. The current approach to financial market regulation, which is based on two pillars, institutional regulation and activity regulation, needs to be changed. By developing new methods of financial services, non-financial institutions provide non-traditional, innovative services. This creates confusion for conventional regulatory frameworks. As a result, each country is working on different regulatory frameworks, which may also hamper the functioning of the single EU financial market. It is therefore important for the EU to steer the individual Member States towards a uniform regulation. It is important to ensure a level playing field, as financial institutions are subject to much stricter regulatory requirements, even when introducing innovative products. On the other hand, non-financial institutions are not subject to strict regulation when applying technological innovations in their financial services. To this end, the EU has set out principles for the regulation and supervision of financial technologies.

These principles are:

- regulation of financial services, regardless of domicile and institution,
- technology neutral control,
- risk-based supervisory measures.

The EU is also proposing solutions for regulation in order to implement the principles. The most important issue is to stimulate new technologies and reap the benefits of the market. This is a particularly important task for the supervisory authorities. Supervisors should facilitate controlled experimentation with new technologies during licensing and should be professionally prepared to audit financial technology services.

In order to preserve financial stability, it is necessary to obtain information on financial activities which are available in case of the traditional service providers but not in the case of the nonbanking institutions. Therefore, imposing an obligation to provide information on nonbank providers is also an important regulatory and supervisory issue.

traditional banking activities. However, the extent of this cannot be determined due to the lack of transparent records. The study points out that the shadow banking system has several definitions. According to the Financial Stability Board, the shadow banking system is a credit transformation system that includes providers and activities outside the traditional banking system. The definition is overshadowed by the Fed"s definition that the shadow banking system carries out certain financial service activities without a state guarantee and access to central bank resources. http://www.bankszovetseg.hu/Public/gep/2018/364-376%20Kecskes.pdf (Last access: 2019.08.21.)

[12] 2018/C 307/6 FinTech: a technológia hatása a pénzügyi szektor jövőjére- 2016/2243(INI) Az Európai Parlament 2017. május 17-i állásfoglalása a pénzügyi technológiáról (FinTech): a technológia hatása a pénzügyi szektor jövőjére, Az Európai Unió Hivatalos Lapja C 307, pp. 57-66 Az uniós szabályozás a dokumentum alapján kerül elemzésre.

All these problems affect many areas of regulation, both at European Union and Member State level. The banking systems of each country are also seeking answers to the challenges of digitization, which is well illustrated by digitization proposal of the Hungarian Banking Association.[13] The literature points out the most important areas for digitization in the banking sector.

Three such areas are highlighted:

- expanding digital payment options,
- digital lending and customer service,
- improving financial literacy.

Significant cash holdings have significant economic disadvantages for the economy and society. The reasons for the high level of cash stock is explained in the literature. In my opinion, some of the reasons can be the financial habits of the older generation and the mistrust of the banking system, which has been exacerbated by the financial and economic crisis. Although it is about accelerating digitization processes, a significant part of the Hungarian population is "stuck" in the use of cash, and it is difficult to move out of it, especially in smaller villages, where there is no bank or internet banking.[14]

The financial sector is open to the use of digital applications and significant improvements have been made in this area, partly due to competition from technology companies. However, the digitalization of individual services also requires the underlying administrative environment to evolve, which may be an obstacle to the digitization of some services.[15]

The literature also emphasizes the development of financial literacy, particularly in the field of education, which imposes new tasks on public education as well as higher education. In my opinion, this is not only a question related to digitalization, but also to the general financial culture, as Hungary has significant backlogs, and only after can we enter the world of digital banking.

The study of Hungarian relations does not deal with the issue of digital money, although this area may have a significant impact on the banking system, in particular, because it reinforces nonbank financial activities and nongovernmental cash flow.

## 3. Regulatory Solutions and Concepts

The two ends of the regulatory approach are permissive and prohibitive regulation. Neither is a good solution at all. On the one hand, totally prohibitive regulation will make it impossible for new technologies to be applied on the market and thus have a negative impact on economic competitiveness. On the other hand, this type of service goes into the gray zone, consumers use the service but become more vulnerable to non-banking players without regulation, without state control. Enforcement is, however, difficult as it can be provided as a cross-border service from outside Europe. Completely permissive regulation puts traditional bank players at a competitive disadvantage because their activities are subject to strict regulation.

[13] Becsei András-Bógyi Attila-Csányi Péter-Kovács Levente: A jövő bankja, a bankok jövője - A Magyar Bankszövetség digitalizációs javaslatai, http://www.bankszovetseg.hu/Public/gep/2019/299-310%20BecsBodCsaKo.pdf, (Last access: 2019.05.05), pp. 299-302

[14] Becsei-Bógyi-Csányi-Kovács: i.m . p. 300 The study lists several reasons for high cash holdings. These include low money market interest rates, transaction fees, limited free cash withdrawals, cash withdrawals from the black economy and the social sphere.

[15] Becsei-Bógyi-Csányi-Kovács: i.m . p. 301 According to the proposal, e-administration, data asset management and access must be developed.

New technology start-ups have a competitive advantage in services because they are not subject to strict institutional and activity licensing conditions that apply to capital, risk, and personal and technical conditions.

The literature points out that there is usually a good solution between the two extremist regulatory attitudes and that most countries are moving in that direction. The solution lies in the fact that technology companies do not have to be subject to banking regulation but must be regulated from an operational point of view. It is necessary to distinguish between exclusive banking activities which cannot be performed by technology firms and to define the services that non-banking actors can provide. It would be important to define the EU framework when defining the level of regulation. The position of the European Central Bank emphasizes national regulation and supervision on this issue, but in my opinion, this will not be sufficient enough, since a large part of the digitized financial service covers cross-border services. Therefore, global regulation will be necessary in the longer term, but until it is realized, it is necessary to regulate the issue at least at the level of each integration.[16] The literature points out that it is a great challenge for the law to track and prevent technological innovation, as technology is implemented at a global level and legislation is implemented locally. Harmonization of concepts is the first step towards harmonization of regulation. However, so far only resolutions have been issued by central banks and supervisors and there is rarely any regulatory solution to the issue.[17]

In addition to regulation, it is at least as important to develop the supervisory activities that is needed to control digital services. This requires regulatory application of innovation technologies, international cooperation of supervisors, cooperation with non-financial market authorities, and initiating regulatory changes.[18]

The Hungarian Banking Association has also made proposals for the future regulation. A large part of the proposals is a proposal to facilitate the digital switchover, which affects several areas of law.[19] The proposals for the reform of regulation are based on the principle of the same activity, the same regulation. At the moment, this is not the case, so technology firms, unless restricted by the authorities, have a competitive advantage in the money market. Regarding this, institutional regulation in this area should be abandoned and only activity regulation should be prioritized, meaning that the same rules apply to banking

[16] Kerényi Ádám- Müller János: Szép új digitális világ? - A pénzügyi technológia és az információ hatalma, Hitelintézeti Szemle, 18.évf.1.szám, 2019.március, p. 16-19 The literature highlights the supervisory priorities for new technology finance solutions based on the FinTech work plan of the European Banking Authority. Such priorities include mapping and analyzing the regulatory area, enhancing supervisory cooperation, investigating prudential risks, enhancing cyber security, addressing consumer issues, and assessing money laundering risks.

[17] Szalay Gábor: A kriptovaluták nemzetközi szabályozási trendjei- Kriptotőzsdék és ICO-k értékpapírjogi perspektívából, Jogtudományi Közlöny, 2019. 3.szám, p. 133-134 In the context of cryptocurrencies, Malta has adopted an innovation technology package. In addition, the European Banking Authority and the Central Bank of Hungary have issued warnings about the high level of risk associated with virtual assets.

[18] Kerényi-Müller: i.m. pp. 17-18

[19] Becsei-Bógyi-Csányi-Kovács: i.m. pp. 302-306 It summarizes its substantive general proposals on digitization in 11 points, by which they understand the same principle of the same regulation, the possibility of concluding an independent digital framework contract, clarifying the rules for digital payments, the issue of certified electronic copies of paper documents, the full power of digital statement, automated bank signatures, switching to digital document management, re-regulating the civil status of electronic declarations, changing tax rules (transaction fee, bank tax).

and non-banking actors carrying out the same activity. This principle brings the regulatory constraint with it that some services need to be re-regulated and that digital services should be confined within this framework. Another important area of competition is taxation. The transaction fee, the bank tax, puts banking operators at a competitive disadvantage against technology companies who are not subject to these special taxes.

Consumer attitudes towards FinTech are fundamentally influenced by trust in the service provider, which is fundamentally determined by the consumer protection created by the law. It is therefore very important to have a legal regulatory background behind the application of new technologies. From the regulatory point of view, the literature considers the development and application of the internationally recognized Innovation Hub and the Regulatory Sandbox.[20] Within the Innovation Hub, information is exchanged between the regulatory authority and the FinTech companies, with the aim of facilitating the interpretation of legislation and developing a consistent legal practice. At the same time, the established platform will allow the supervisor to assess regulatory gaps and make recommendations to the legislator on legislative issues. This solution can facilitate the acquisition of activity licenses through consulting. The Regulatory Sandbox offers the opportunity to test innovative technologies within a limited framework. Through testing, monitoring will provide an overview of possible operational problems and solutions for the problems. Successful testing will enable entry into the market, reducing the risk that comes with innovation. In addition, the method is also beneficial for innovation firms, as they can test the financial product and business model on consumers without the full regulatory constraints on the service provider. However, only firms determined by the supervisory authority may participate in the testing. Consumers typically participate in testing on a voluntary basis, with consumers being compensated for any losses they may have and a specific redress mechanism ensuring that consumer risks are mitigated.[21]

## 4. Summary

Digitization will bring significant changes to the financial markets in the coming years, which will be a challenge for both supervisors and the legislator. Traditional institutions have tried to incorporate the technological changes that have taken place in their services in recent years, but due to the caution and prudence of the traditional service providers, the process of incorporation was slow, and it has not been induced by the market situation either. The risk-averse behavior of traditional financial institutions has not facilitated rapid technological progress, which has been exacerbated by the financial and economic crisis. However, the entry of new technology companies into the financial market has accelerated the processes, created strong competition and prompted supervisors to take action. At the heart of the regulatory problem is the challenge that banking

[20] Innováció és stabilitás- Fintech körkép Magyarországon, MNB Konzultációs dokumentum, 2017, mnb.hu/letoltes/konzultacios-dokumentum.pdf. (Last access: 2019.07.07.) i.m. pp. 30-33 The purpose of the Innovation Hub is to assist banking and nonbanking actors with legal issues regarding innovation. The Regulatory Sandbox is used to test innovative solutions, providing companies with a temporary exemption from prudential requirements.

[21] Eszes-Sajtos-Szakács-Tőrös: i.m. pp. 665-670 The literature indicates that Regulatory Sandbox is being deployed in more and more countries, including Canada, the United Kingdom, the Netherlands, Switzerland, Australia, among others, and more and more country is considering it.

regulation relies primarily on institutional regulation and that activity regulation is only secondary. This means that financial service activities should be carried out primarily by financial institutions within a defined and separately regulated field. A question has arisen whether technology companies could ever provide certain financial services without the permission of their supervisors. New digital financial constructions, on the other hand, either exist as unregulated cross-border services or outside of traditional designated financial services therefore operate without authorization and control. In my opinion, though, new entrants have not yet fully faced the risks associated with traditional financial services and can only be mitigated if they have the necessary professional skills and operational experience. There was also no significant damage from consumers" side that would undermine confidence in non-traditional banking providers. However, the most likely scenario may be that traditional service providers will blend in with technology firms, meaning that banking expertise and experience is combined with technological innovation. This solution would represent the best opportunity for both the supervisor and the legislator, since regulated institutions would operate in a regulated market, so that activities would continue to be carried out in a controlled manner. It is also necessary to be prepared for the fact that this is not the case with market processes and that currently unregulated institutions will provide a significant part of financial services. In this case, there are a lot of regulatory challenges that a country may not be able to solve on its own, a higher level, integrated regulation is needed, and financial culture also needs to be strengthened. The latter can also have an impact where regulation does not have the means to protect consumers, which will surely be exemplified by the rapid changes of the digital technology.

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# PRECISION AGRICULTURE IN HUNGARIAN LEGAL ENVIRONMENT

**László FODOR***

## Abstract

*The regulation of precision agriculture is still in its infancy; as the general agricultural law, tax law, environmental law regulations are applied to this new form of agriculture that can be characterized by modern techniques, the Internet of Things, and the consideration of place of production conditions. There are precision agriculture farmers in Hungary who have gathered in an interest protection organization, and according to the Hungarian Minister of Agriculture, precision farming is one of the preconditions for the competitiveness of Hungarian agriculture. At the same time, several circumstances obstruct the spread of precision farming. These include the high cost of machinery and other equipments, the lack of professional knowledge of farmers, the unfavorable structure of agriculture (e.g. fragmentation of arable lands, aging of farm population), the general lack of trust and the excessive complexity and the frequent changes in agricultural legislation. This study examines some relevant elements of Hungarian legislation, also with special respect to the views of farmers. It highlights the shortcomings and contradictions of Hungarian law that, as it is already been known, may hinder the spread of the new, innovative solutions in practice.*

**Keywords:** *precision agriculture, Hungary, farmers" opinion and motivation related to precision farming, agricultural law problems, Common Agricultural Policy*

Researches on Precision Agriculture (PA)[1] focus primarily on the question: what advantages does precision farming offer. The answers include the lower ecological impacts, the reduction of costs, higher and more stable yields and higher profits. PA can be a likely answer to climate change and food security as well. It is often viewed as the "cultivation system of the future". Beside the ecological, agronomical, economical, technical, botanical, soil and science aspects of PA, social scientific approaches have come to the forefront recently. Is PA accessible to all types of farmers? What are the social benefits and potential negative social consequences of PA (e.g. from the perspective of employment policy, how does a farmer become redundant?)? To what extent does political and legal environment promote or hinder the spread of PA? This paper is looking for the answers to these questions, under Hungarian conditions.

As far as the narrower subject of the research – legal regulations on the PA – is concerned, there are hardly any previous Hungarian antecedents.[2] The reason for this

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[1] In this study, the terms precision agriculture and precision farming are used with the same meaning.

[2] Legal researches have been launched only recently in Szeged and Debrecen, while agricultural professionals have been publishing PAs regularly since the 1990s. Á. Bujdos PA deals with certain aspects of EU law. Á. Bujdos:

is that PA as a form of farming is relatively new, and the legal (agricultural, environmental, water law, tax law, etc.) regulations that apply to it do not contain requirements adjusted specifically to PA yet.

Issues of legal regulation appear rarely, usually scattered, fragmented in the international literature of PA. At the same time, due to the specificities of national legal systems, foreign regulatory experiences can only be adapted to a limited extent, even within the European Union with a Common Agricultural Policy (CAP).[3] This is an important factor to mention because this research topic is only partly international. CAP regulations apply in all Member States (in the field of market regulations, direct payments, protection of the environment, food safety etc.), but a significant part of agricultural situations (such as the regulation of land ownership, land leasing, taxation) constitute a national competence. At the same time the results of social science (especially agronomy and sociology) can be relied upon, so the evaluation of the existing regulations and the justification of the necessary measures and legislative changes is possible from their perspective.

This study was completed as part of an interdisciplinary research project, however, it only examines PA from a legal perspective. By studying definitions known in the professional literature, I try to describe what can be considered as PA. In the course of the research, a questionnaire survey and several interviews were conducted (both in 2018) among Hungarian farmers. Based on the answers, the study shows what farmers consider important in the legal-political context for the spread of the PA, and it examines the circumstances behind the responses of the farmers. While seeking reasons it reflects on the problems of legal regulation and application.

## 1. Definition of precision agriculture

The first research task is to examine what precision farming means from a legal perspective. Clarifying the meaning of concepts in legal regulations is indispensable for the determination of the material scope of law. Currently there is no Hungarian legislation or binding EU legislation that would explicitly regulate and define PA. At the same time, there is a need from the direction of agricultural policy to promote the spread of PA,[4] that cannot be imagined without legal regulation. This can be solved by the legislator either by providing a generally applicable definition and introducing specific regulations on PA, or by indirectly regulating it without a definition, by promoting its main (favorable technical,

Precision agriculture: a potential tool to tackle drought and water scarcity in the EU. *Hungarian Yearbook of International Law and European Law 2018*, 371-388. E. Farkas deals with the issue of innovation. E. Farkas Csamangó, Gazdasági és jogi kérdések a környezetjog területéről: Az öko-innovációról. [Economic and Legal Issues in the Field of Environmental Law: Eco-innovation] – In K. Gellén (ed.): *Gazdasági tendenciák és jogi kihívások a 21. században*, Szeged, Iurisperitus Kiadó, 2019, pp.39-53.

[3] To review therelevant legal regulations (on data management, food safety, climate change mitigation etc.) of the EU *See:* M. Kritikos: *Precision agriculture in Europe: Legal, social and ethical considerations: Study*. Brussels, 2017, 80. http://www.europarl.europa.eu/RegData/etudes/STUD/2017/603207/EPRS_STU(2017)603207_EN.pdf (last access: 20.05.2019).

[4] Phil Hogan, the EU Commissioner for Agriculture said at the Forum for the Future of Agriculture 2018 that: "Member States would have to (…) explore the introduction of (…) incentives for precision agriculture." After 2020 "the role of new technologies and precision agriculture will be central" in the CAP in achieving the objectives of climate protection without reducing production volumes.

https://ec.europa.eu/commission/commissioners/2014-2019/hogan/announcements/speech-commissioner-phil-hogan-forum-future-agriculture-2018_en (last access: 19.05.2019)

management, environmental etc.) features separately.[5] It can be assumed that the former solution would be more accurate, more expedient in terms of PA, while the advantage of the other solution could be the its competitiveness and technological neutrality.

The question is, therefore, whether a generally acceptable definition could be given in the light of the professional literature and other non-legal sources, and, if so, in what category the precision farming could be classified according to its definition.

There are many definitions known of PA, almost all of which emphasize the linking of state-of-the-art agricultural machinery/technology with IT equipment, and the approach to economic, environmental and social sustainability. One way to do this is to differentiate within the areas of land: "precison farming is the term given to a method of crop management by which areas of land or crop within a field are managed with different levels of input in that field."[6]

According to the late British Home Grown Cereals Authority (merged into a new entity in 2008), PA is: "management of farm practices that uses computers, satellite positioning systems and remote sensing devices to provide information on which enhanced decisions can be made."[7] The United States Department of Agriculture calls this kind of agriculture "as needed" farming and define it as "a management system that is information and technology based, is site specific and uses one or more of the following sources of data: soils, crops, nutrients, pests, moisture or yield, for optimum profitability, sustainability and protection of the environment."[8]

In the Hungarian literature, PA is considered to be complete if a soil analysis based on a satellite navigation supported soil sampling, a differentiated nutrient replenishment, yield mapping, precision sowing, and differentiated plant protection are implemented on the given farm.[9]

There are a few who, opposite to us, makes a distinction between PA and PF. According to this view, PA is a sustainable use of agricultural resources which can be achieved by managing agricultural systems based on information and knowledge. Compared to this, PF is the use of available technologies to tailor soil and crop management to fit the specific conditions found within an agricultural field.[10]

PA is cost-intensive due to the high cost of special machines and the appropriate IT background, but it is eased by the fact that it is not necessary to introduce all its elements at the same time, thus it is possible to switch gradually between traditional farming and a system based fully on

[5] The main differences between conventional and precision farming are summarized by J. Tamás, *Precision agriculture*. University of Debrecen AGTC, Debrecen, 2011, 2.

[6] R.J. Godwin, G.A. Wood, J.C. Taylor, S.M. Knight, J.P. Welsh: Precision Farming of Cereal Crops: a Review of a Six Year Experiment to develop Management Guidelines. *Biosystems Engineering* 2003/4, p. 376. doi:10.1016/S1537-5110(03)00031-X. Spatial thinking has a long tradition in Hungary, both in practice and in scientific research, mutat rá Tamás, ibid. 1.

[7] H. J. S. Finch, A. M. Samuel, G. P. F. Lane: *Lockhart and Wiseman"s Crop Husbandry Including Grassland.* Elsevier, Woodhead, 2014,p. 236.

[8] Ibid.

[9] K. Takácsné György: *A precíziós növénytermelés közgazdasági összefüggései. [Economic contexts of precision plant production],* Szaktudás Kiadóház, Budapest, 2011.; J. Popp, E. Erdei, J. Oláh: A precíziós gazdálkodás kilátásai Magyarországon (Outlook of precision farming in Hungary). *International Journal of Engineering and Management Sciences* 2018/1, 138.

[10] J. Vieira Rocha: Precision farming and geographic systems. In C. Bauzer, M. Medeiros (Eds.), *Advanced Geographic Information Systems (Vol. 1.).* EOLSS, Oxford, 2009, pp. 151-168 (166).

precision solutions.[11] At the same time this also means that the use of some precision machines alone does not necessarily mean precision farming.

Based on the studied literature and the wide variety of documents available on the Internet (Commission and Parliament background studies, press releases, chamber statements, association documents),[12] at the very least, there is no uniform definition that can be used in legislation. Generally speaking, it is a form of farming, the conceptual elements of which can be adapted to the specific technical, economic, scientific approaches and policy objectives.

The limitations of the creation of a definition are also burdens for the legal regulations. If precision farming fails to formulate a definition that describes its essence to the legislator to distinguish it clearly from other types of farming methods/forms, then only the conceptual elements of precision agriculture can be captured by regulation. It may be a question of further research what conceptual elements (e.g. input and output characteristics, technical, information technological, soil usage, etc.) can be highlighted. This can be followed by the examination how the characteristics of precision farming fit into the current regulatory framework and – e.g. in line with the forthcoming reform of the Common Agricultural Policy – the changing regulations. Thus, what legal institutions, regulatory methods and elements are relevant within agricultural and environmental law as far as precision agriculture is concerned.

At the same time, it can also answer the question of which solutions with similar parameters can precision farming compete with. It is not a jurisprudence / research decision, but it can be examined how regulatory priorities can develop in this respect. From the prspective of legal policy, I would emphasize two aspects. On the one hand, I believe that there is a more favorable form of farming in terms of environmental sustainability (e.g. ecological farming), that at the same time has lower productivity. In this way, PA can represent a midway between, a transition to the promotion of ecological and economical interests. On the other hand, my opinion is that the spread of PA – for both farming and nature conservation reasons – should only be allowed in landscapes that are suitable for intensive farming (e.g. areas with lower quality of land, but rich wildlife, extensive cultivation and conservation of natural values should be encouraged).

In view of the above, the EU will, in the future, certainly expect the Member States to promote its spread by appropriate measures, in parallel with the pursuit to provide more opportunities for Member States to give input on agricultural policy for promoting agricultural innovation and for providing local answers for challenges (such as climate change).[13]

[11] G. Kemény, I. Lámfalusi, A. Molnár (Eds.): *A precíziós szántóföldi növénytermesztés összehasonlító vizsgálata.* [Comparative Study on Precision Farming in Crop Production.] Agrárgazdasági Kutató Intézet, Budapest, 2017, 16.

[12] Relevant policies and legal acts of the EU reviewed by: R. Schrijver: *Precision agriculture and the future of farming in Europe: Scientific Foresight Study.* European Parliamentary Research Service, Brussels, 2016, 42. IP/G/STOA/FWC/2013-1/Lot 7/SC5.

[13] According to the EU Commissioner for Agriculture, the future CAP will be more ambitious in terms of environmental objectives, and "greener" agriculture (among others) should be provided through the wider use of precision farming methods. In several of his speeches, he explained that the increasingly complex challenges facing the CAP need to be met with increasingly simple administration and the use of modern technologies; support for agricultural innovation will be left to the Member States after 2020. https://ec.europa.eu/commission/commissioners/2014-2019/hogan/announcements/speech-commissioner-phil-hogan-opening-wageningen-university-academic-year_en; https://www.euractiv.com/section/agriculture-

## 2) Issues of legal regulations

The research deals not only with the actual situation of PA in Hungary, but also with its perception by farmers and its possibilities for spreading. Interviews and questionnaires were conducted in order to get to know them. The problems raised by farmers are described below.

### 2.1. Problem map based on the opinion of farmers

Within the framework of the project 30 in-depth interviews were conducted with farmers in the Great Hungarian Plain[14] who are affected or may become involved in precision farming. Although the interviews do not explicitly approach the obstacles of the precision agriculture, the circumstances that stimulate it and the opinions about the PA from a legal perspective, [15] the interviewees have raised a number of questions that can be answered in whole or in part by means of legal regulation. Interviews – because of the relatively low number of respondents – serve as a basis for hypotheses rather than conclusions. Although the relevant issues that have arisen cannot be weighted based on the interviews, it is worth listing them.

a) It includes, in particular in smaller private farms, the lack of appropriate expertise as a barrier. The problem affecting the sector as a whole in Hungary is that the legislation does not expect any expertise from the farmers. So, anyone can farm without proper theoretical and practical knowledge. While since 2014, if buying or renting a land (if the land area reaches 1 hectare), certain knowledge shall be proven,[16] the requirements are only formal (can be accomplished easily, with participation in a course held only at four weekends). There is a more serious requirement, e.g. for large-scale use of plant protection products. However, precision farming would require more. This is confirmed by the literature.[17]

The organization of professional agricultural training is primarily a state task and the qualification requirements are defined also by legislation. In response to today"s expectations, state-accredited precision farming training is now taking place at some Hungarian universities, but for the time being there are thousands of professionals missing from the country who have the appropriate IT and management skills, that could also be passed on to others.

b) The issue connects with the expertise whether the farmers are provided someone to address their questions. While in several countries of Western Europe it is a tradition for decades, in Hungary, many

food/interview/hogan-eu-member-states-will-decide-on-agriculture-innovation-after-2020-not-brussels/ (last access: 20.05.2019).

[14] Today, PA is mainly spread in farms engaged in field crop production. A significant part of the Hungarian arable land utilized for field crop production (about 4/5 of the total irrigated area) is located in this region. Data of the Agricultural Research Institute, 2018. http://repo.aki.gov.hu/3168/1/2017öntözés kiadvány.pdf (last access: 20.05.2019).

[15] The interviews focused on the situation of the individual farms, opinions of the farmers, and primarily detected the problems of technology, labor, information flow and profitability. The interview questions changed from case to case according to the specifics of the given economy. We have not been specifically asked about the difficulties of legal regulation and bureaucracy, so they were only discussed when the interviewees themselves considered it important.

[16] In contrast, in many countries in Western Europe (eg Denmark, France, Germany), farming is conditional on the existence of expertise, that also affects inheritance. Ch. Grimm: Von der Landwirtschaft zur Wirtschaft auf dem Lande? Gedanken zum Begriff der Landwirtschaft. *Agrarrecht*, 2001/1, 3-4.

[17] The primary barrier to the spread of PA is the human factor, that highlights the importance of information and training. Popp et al, p 141. Special training courses have already been launched in Budapest, Debrecen, Eger, Győr and Keszthely.

complain about the lack of an appropriate system. This is not a coincidence, since the use of up-to-date, knowledge-based support for all farmers is an indispensable condition for the application of new technologies, but it is not considered as a priority by the current agricultural policy (along with training).[18]

c) Many also reported shortcomings, uncertainties and inconsistencies in the subsidy system. Predictability would be important as the expensive equipments and softwares are not necessarily procured at the same time. However, if it becomes available one day but the other day the special machine purchase support is not provided (currently not available), we cannot talk about predictability. There were also general problems related to subsidies such as inconsistencies in quantitative and qualitative criteria, market distorting effects of subsidies, slowness of decision making, different effects of support in field crop production and among large and small producers.

At the same time, as the literature points out, the negative experiences of domestic farmers are partly related to the fact that they have made inconsequent improvements. However, they are still currently receiving high income support, while interest rates are low, which are worth taking advantage of.[19]

d) The issue of the suitability of croplands and the need for differentiation have been raised by the more environmentally conscious farmers. This is not a coincidence, because one of the PA"s virtues may be to keep the conditions of the production area in mind, but this is not the case if the selection of the crop is not done properly. However, in a significant part of the Hungarian agricultural lands, plants that do not meet the natural conditions and the challenges of climate change are cultivated, non-soil-friendly farming technologies are used, [20] and the size of the land parcels has also been determined inappropriately.[21] First of all, changing the form of cultivation and a general land consolidation could help, but its social support is low and the government to this day has not undertaken its implementation.

e) A modern land evaluation system is required to know the characteristics of the croplands. Farmers are also facing problems in this area, as the main elements of the Hungarian land evaluation system were introduced – for taxation purposes – at the end of the 19th century. In the meantime, however, social and ownership conditions have changed, the role of ecological aspects has increased, and many ecosystem services in the land have been ignored, so it would be justified to complete the land reform that was left undone the 1980s.[22]

[18] Popp et al. p.143.

[19] Popp et al, 144.; I. Kapronczai: A műszaki fejlesztés beruházási háttere és az agrárpolitikai hatások [Investment background of technical development and agricultural policy effects]. *Gazdálkodás*, 2017/3, pp. 187-198.

[20] In 2005, a quarter of the arable land was considered to require a change in the cultivation and land use, and with that experts suggested to withdraw 1.5 million hectares of land from intensive crop production. In contrast, in the recent period (as a result of EU subsidies), the cereal sector has grown steadily. *See:* J. Ángyán, T. Szalai, Z. Fodor, R. Lőrinczi, G. Nagy: A földhasználat alakulása. [Land use trends] In P. Stefanovits, E. Michéli (Eds.): *A talajok jelentősége a 21. században.* MTA, 2005, Budapest, pp.55-57.

[21] E. Szabó, I. Pomázi (eds.): *Magyarország környezeti mutatói 2000 [Environmental Indicators of Hungary 2000]*. Környezetvédelmi Minisztérium, Budapest, 2000, p. 132.

[22] F. Máté, G. Tóth: A földértékelés tendenciái. *[Land Evaluation Trends]* In P. Stefanovits, E. Michéli (Eds.), *A talajok jelentősége a 21. században.* MTA, 2005, Budapest, 339.; I. Szűcs: A termőföld környezeti és gazdasági értéke a 21. században [The environmental and economic value of land in the 21st century]. In P. Stefanovits, E. Michéli (Eds.), *A talajok jelentősége a 21. században.* MTA, 2005, Budapest, p. 352.

f) Some indicated problems with the state-operated Soil Protection Information and Monitoring System (TIM). The details of the interview did not reveal, however, but the statement of the Ombudsman for Future Generations points out that the financial resources of the domestic monitoring systems are uncertain and the number of measurement points in the monitoring networks is constantly decreasing. The change of soil property due to various reasons (e.g. climate change, inadequate cultivation) requires the operation of a soil information system that reliably supports decisions on soil protection interventions, food safety, water protection, climate protection and land use planning.[23]

g) Strong concentration is an important feature of the structure of land use for the spread of precision farming. Despite the significant process of land concentration in recent decades[24] also fragmentation of the land structure (overdivision, large number of relatively small farms and parcels) appears to be a major barrier. There is a lack of regulations to kep farm areas together (e.g. special inheritance rules). The current law regulates the acquisition of land, not the acquisition of agricultural holdings as economic, organizational and technical units.[25]

h) The respondents consider it important to develop a system of agricultural services (e.g. machine rental, wage labor, consulting, etc.). This is related to the issues of farmer and producer organizations and co-operatives, that also have been mentioned by many. Organizations and co-operatives could provide appropriate frameworks for the joint organization, co-ordination of services and the joint procurement of machinery. In Hungary, however, there are lags in this area, that can be explained by the bad historical memory of the kolkhoz-type cooperatives that used to be established once based on the Soviet model and the lack of trust. [26]

i) The national rules and procedures for the operation of unmanned aircraft also give grounds for complaints, that hinder the spread of the technology, as they do not take into account the specificities of agriculture.[27] For example, flying larger drones suitable for spraying should be reported 30 days in advance. On the other hand, the meaning of drone use would be to intervene at the time of detection of agricultural pests, focusing on the affected area, as soon as possible.

j) Some of the legally relevant issues are related to irrigation, licenses required for water use, and other – rather excessive – administrative burdens. Due to the climate change in Hungary, there are longer periods of lack of rainfall, which affects many farmers, increasing production costs and drought damage. The Hungarian water management is not prepared to deal with the problem, therefore in the second half of 2018 the Government approved Government

[23] Statement on Soil of Ombudsman for Future Generations, Budapest, 29. 11. 2016, 15, 19.

[24] I. Kovách: Földek és emberek. Földhasználók és földhasználati módok Magyarországon.*[Soils and people. Land users and land use modes in Hungary.]* MTA Társadalomtudományi Kutatóközpont-Debrecen University Press, Budapest, 2016, pp. 39-45.

[25] Article P (2) of the Fundamental Law of Hungary; Act CXXII of 2013 on the transfer of lands used for agriculture and forestry.

[26] G. G. Szabó, I. Bartha: A mezőgazdasági termelői szervezetek - szövetkezetek jelentőségének és helyzetének változása az EU-csatlakozás után [Changes in the importance and position of cooperatives - agricultural producer organizations after EU accession]. *Gazdálkodás*, 2014/3, pp. 263-278. It should be noted that under the current Hungarian legislation, cooperatives still do not fully comply with Western European type cooperatives.

[27] Hungarian regulation does not take into account the appearance of new technologies and their economic impact, thus making it difficult for example to access national data assets for business purposes and to use drones for production purposes. Popp et al, p. 143.

Decree No. 1426/2018. (IX. 10.) on the development of domestic water management for irrigation purposes. (For the purpose of development, the irrigation infrastructure is being assessed, the regulatory environment is changing, an irrigation agency is being set up, etc.). Unfortunately, during the planning of the measures, the possibilities of precision farming were not taken into account and therefore a regulatory environment was created in where the ecological and competitive advantages of precision farming hardly prevail.

Changes to water legislation have already been made in some areas in 2019. So, for example, water license – under certain conditions for soil protection, environmental protection, water management – can be issued for water use for irrigation for up to 20 years instead of 5, which ease the administrative burden for the farmers concerned. The so-called permanent water shortage period in which farmers do not have to pay a water resources fee after the amount of water used for irrigation (pursuant to Section 15/C of Act LVII of 1995 on Water Management) has been extended. In addition, the State may derogate from the provision on the obligation to pay water resources levy for reasons of social, environmental and economic effects and geographical and climatic features in favour of the water user.[28] A separate law has been adopted on the framework for cooperation between farmers for irrigation (e.g. establishment of irrigation communities and districts, easements).[29] The fee requirements are debatable, as the principle of recovery of the costs of water services (see EU Water Framework Directive, Art. 9) may be undermined. Farmers are exempted if water resources are limited, while regulation does not encourage sustainable and efficient water use, that could be achieved, among other things, by precision farming.

### 2. 2. Some highlighted factors the according to the questionnaires

In the questionnaire survey, we received responses from 604 farmers, representing about 116,000 farms using 95% of the country"s cultivated areas. 7.2% of the respondents listed themselves as precision farmers. There were four issues that were more closely related to the legislation. We were asking about that as far as the spread of the PA is concerned how important the long-term land use legislation, the PA-specific tax policy, the PA"s political environment and the long-term predictable agricultural policy are considered. We asked to evaluate the significance of each factor on a five-grade scale. The results are summarized in Table 1. below.

Table 1.

The role of the legal, political environment in the motivation of farmers relating to PA

| Factors | mean | Standard Deviation | Factor Weights |
|---|---|---|---|
| Legislation that allows long-term land use safety | 4,12 | 0,83 | 0,54 |
| Fair tax rules adjusted to precision farms | 3,70 | 0,99 | 0,84 |

[28] It should be mentioned that a special fee has been introduced for agricultural water supplies.This fee was introduced in 2015 as due to the decision no. C-525/12 sz. European Court of Justice between the Commission v Germany (11.09.2014; ECLI:EU:C:2014:2202). J. E. Szilágyi: Aktualitások a mezőgazdasági vízjog köréből: A mezőgazdasági öntözés változó jogi szabályozása [Current Issues in the Field of Agricultural Water Law: The Changing Legal Regulation of Agricultural Irrigation.]. In K. Gellén (ed): *Honori et virtuti: Ünnepi tanulmányok Bobvos Pál 65. születésnapjára.* Iurisperitus Bt., Szeged, 2017, p. 433.

[29] Act CXIII of 2019 on irrigation agronomy.

| | | | |
|---|---|---|---|
| Precision farming friendly political environment | 3,66 | 0,98 | 0,86 |
| Long-term, predictable agricultural policy | 4,18 | 0,92 | 0,51 |

Source: self-created, based on survey results.[30]

It can be seen that the grade of laws that provide a long-term land use and long-term, predictable agricultural policies are significantly higher than the grade of the answers to questions specific to precision farming. (The reason why the ranking of the answers given to each question does not match the order of the factor weights of the questions, can be examined by modeling, but in any case, it indicates that the farmers do not necessarily make their decisions based on rational aspects.) If the precision farmers and the other farmer"s responses are considered separately, it is clear that there is the greatest consensus on the importance of long-term land use regulation.

Below are the individual factors. I am trying to highlight what can be the basis of these answers.

### 2.2.1. Significance of legislation that provide long-term land use

In Hungary, following the change of regime in 1989, there was an agricultural land structure in which land use had two decisive titles: ownership and lease.[31] The proportion of rent is the highest in the field crop production (55%). Ownership provides a stronger position for farmers, because (unlike some Western European countries) Hungarian agricultural law hardly applies so-called tenant protection measures. Although there is a pre-lease right, which gives an advantage to the previous lessee when entering into a new contract (under certain conditions, such as being registered in the "register of farmers", expertise, local residence), at the same time, for example the right to appoint the new tenant (the former tenant is not allowed to say who will continue the farming after her/him). The minimum lease period is 1 year, that does not guarantee the return on investment, but it takes the continuity of the work due in the given marketing year into account. A minimum or a specific period of lease has not been set by the law (as opposed to French law, for example).[32] The Act CXXII on the transfer of lands (Land Act)[33] sets the maximum lease period as a rule for 20 years (in case of forest area it can be significantly more, depending on the age of the forest). Within this time frame (1-20 years), the duration of the legal relationship is determined freely by the parties (owner, lessee). However, conclusiom of contracts with a duration of more than 5 years is motivated with an exemption from tax by the lessor. [34] If the contract has expired, the owner (whether or not he has the expertise or other profession) may decide to continue to cultivate the land himself, thus not to re-

[30] For complex statistical evaluation of the results of the survey and interviews *See*: A. Bai, P. Balogh, Á. Bujdos, I. Czibere, L. Fodor, Z. Gabnai, I. Kovách: Main motivational factors of farmers adopting precision farming in Hungary. *Agronomy* (submitted for publication, 2019).

[31] The asset management rights established in the case of state-owned lands (5-20 years) (the relevant rules are laid down in Sections 19/A – 22 of the Act LXXXVII of 2010 on the National Land Fund), or the land use and usufruct established for the relatives of close relatives (for free) has less importance.

[32] In Western Europe, the lease is generally considered to be long-term with a duration of more than 10-15 years, that is beneficial for both the owner and the tenant. A. Burgerné Gimes: Földhasználat és földbirtok-politika az Európai Unió országaiban. [Land Use and Land Tenure Policy in European Union Countries] *Statisztikai Szemle* 1998/4-5, 483-489.

[33] Section 44 of the Act CXXII of 2013 on the transfer of lands used for agriculture and forestry.

[34] Point 9.4 of the Exhibit #1 of the Act CXVII of 1995 on personal income tax.

lease it. [35] In case of inheritance, keeping the farm together is not ensured. This regulation result in contracts of varying duration depending on the strength, the size and fragmentation of the land (land), the EU subsidies and the land market conditions.

It increases the significance of the issue that the ownership structure and use conditions of Hungarian agricultural production areas are still characterized by extremes. In the case of fragmented parcels – that, in many cases, although makes up a single piece but is jointly owned by several people[36] – the tenant has to enter into a lease agreement with several owners, that becomes possible often with many difficulties. At the same time, small-sized parcels are difficult to carry out self-production (it is not typical of field crop production, but for example, it is feasible in grape production).[37] Fragmentation, therefore, favors capital-intensive farmers who have sufficient resources to rent land from small owners or the state and create a large economy. At this point, it should also be noted that companies in Hungary have not been able to acquire land since 1994, which means that the lease is the main legal basis of land use. At the same time, the farms with the largest area operate as companies (e.g. as a public or a private limited company, or a private limited liability company).

*There is no minimum land parcel size in Hungary, only the size of land that can be acquired by one person and the so-called land possession limit is declared by the Land Act. A person can acquire a maximum of 300 hectares of land (at the same time, if it is inherited, there is no upper limit), while the land possession maximum (that covers all areas used by the farmer) is currently 1200 ha, and in exceptional cases, 1800 hectares. (The latter applies, for example, to farmers engaged in animal husbandry.)[38] However, these rules are not suitable for characterizing the real forms of possessions or farm sizes. The latter period has been characterized by a significant concentration of property, that is not apparent in the registers (this is due to the phenomenon of company relations and cross-ownership).[39]*

*The importance of long-term land use rights lies first and foremost in the time needed for the return on the costs spent on developments and investments. The regulation providing long-term land use could get a high score also because the current regulation is relatively difficult to understand, it is over-bureaucratised,[40] and in addition, the regulations of land sales*

[35] Some Western European countries (e.g. France) restrict the owner"s right to dispose of the property (re-leasing can be denied only in cases specified by law at the end of the lease period). Burgerné Gimes, 483.

[36] One of the negative consequences of the change of regime is that lands were given into undivided joint ownership, and because of the small size and the location they cannot be distributed physically to individual lands. Currently approx. 1 million hectares of land and 4 million people are affected, that makes it impossible to predict long-term farming. According to press reports, the Ministry of Agriculture is currently preparing a draft law for resolution (in previous years there have been several attempts to eliminate undivided joint ownership, but with limited success)

https://www.portfolio.hu/vallalatok/nagy-valtozas-jon-az-osztatlan-kozos-tulajdonnal.313535.html (last access: 28.05.2019).

[37] From a statistical point of view, the farm threshold (the minimum area) is 500 m2 for grapes and orchards and 1500 m2 for other areas.

[38] In Hungary, although Article P) (2) of the Fundamental Law requires a qualified majority law (requires two-thirds of the votes) to regulate agricultural holdings, there is currently no legislation that would define the categories of holdings (e.g. small and large farms) on the basis of their size.

[39] Kovách, 67, 80-82. I note that, between 2002 and 2014, there was a limit specifically for all the lands owned by family members.

[40] In addition to the Act CXXII of 2013 on the transfer of lands used for agriculture and forestry the Act CCXII on certain measures and transitional regulations related to the Act CXII of 2013 on the on the transfer of lands used

*(acquisition, leasing)[41] have changed many times over the past decades. The fine-tuning of the land acquisition regulations introduced in 2014 has not yet been completed, and there is still a lot of uncertainty in judicial practice.[42] Several statutory provisions of the act had to be amended because of the decision no. 17/2015. (VI. 5.) AB of the Hungarian Constitutional Court, the other rules are being contested by the European Commission.[43] In the course of the operation of the National Land Fund, irregularities were also detected by courts and government control bodies.[44] Farmers, on the other hand, need to have a stable, clear regulatory environment to support their business decisions.*

### 2.2.2. Significance of the long-term, predictable agricultural policy

Today, agricultural policy is partly a competence of the EU and partly of the Member States, so its predictability depends partly both on the governance of Member States and on the EU. The CAP has undergone several reforms since 1991. A good part of these was made before Hungary"s accession, but since the accession has brought enormous changes in the national agricultural policy (e.g. within agriculture, the emphasis has shifted from animal husbandry to crop production). Today, the new CAP is being prepared in line with the new seven-year budget cycle (2021-2027).[45] The main directions of change (diversification, decoupling, greening, etc.) have been revealed for a long time, newer and newer corrections are preceded by several years of public negotiations, so the farmers are not facing the unexpected. Now in 2019 the changes after 2020 can be expected, e.g. reduction of

for agriculture and forestry shall also be highlighted. Special requirements apply to contracts concluded with the National Land Fund, the sale of vineyards in the wine-growing settlements, etc. At present, the notaries of local governments, the local bodies of the Chamber of Agriculture and government offices are involved in the execution and approval of land transactions.

[41] For example, the number and order of the right of pre-emption and the regulation of the acquisition of foreigners has changed several times (can it be obtained by them, and under what conditions). For the maximum duration of the lease, special regulations other than the general were applicable to forests, grapes and orchards. The maximum amount of rentable area was different for natural persons and companies (the former were 300 ha, the latter could rent 2,500 ha of land) and the area leased from the National Land Fund was not taken into account. It is completely new from 2014 to require the authority approval of contracts, and to prescribe the quality of "farmer" (and hence the existence of the aforementioned expertise) for Hungarian farmers and the obligation of personal utilization. Between 2014 and 2018, the Land Act was amended 9, the Supplementary Act was amended 26 times, to a greater or a lesser extent.

[42] T. Andréka, I. Olajos: A földforgalmi jogalkotás és jogalkalmazás végrehajtása kapcsán felmerült jogi problémák elemzése. [Analyzing the legal issues emerged in land-use legislation and application]. *Magyar Jog*, 2017 /7-8, 410-424.; I. Olajos: The acquisition and the right of use of agricultural lands, in particular the developing Hungarian court practice. *Journal of Agricultural and Environmental Law*, 23/2017, 91-116.

[43] J. E. Szilágyi: European legislation and Hungarian law regime of transfer of agricultural and forestry lands. *Journal of Agricultural and Environmental Law*, 2017/23, pp.158-161.

[44] In the most well-known case -No. Pfv.VI.21.775/2015 – the Curia declared the invalidity of the land lease contract on April 12, 2016 due to a collision in legislation and goodwill. (A company got land from the From the National Land Fund that did not perform any agricultural activities).

[45] J. Martinez, J. E. Szilágyi, A. di Lauro, L. Bodiguel, R. Norer, A. Reinl, E. Gregoire, Ch. Busse, M. List, I. Olajos et al: *CAP reform: Market Organisation and Rural Areas: Legal Framework and Implementation*. Baden-Baden, Nomos, 2017. For the Hungarian aspects of the 2013 reforms *See*: T. Andréka, K. Bányai, I. Olajos: The most changes of Hungarian Agricultural Market Policy after the 2013th CAP reform. *Journal of Agricultural and Environmental Law*, 19/2015, pp. 6-18.

subsidies, further greening.[46] It should be noted, however, that in connection with the unhealthy agricultural farming structure in Hungary, the proportion areas involved in field crop production is significant.[47] The vast majority of EU agricultural subsidies have also been spent on this in Hungary, and the participants of the sector are apprehensive of the reduction in subsidies. (In recent years, only the cereals sector has been able to grow within agriculture as a result of EU subsidies, while its growing share makes the whole agricultural sector vulnerable).[48]

In Hungary, land policy has always been a priority within the (national) agricultural policy.[49] Hence, the issues of predictable agricultural policy and regulation of secured long-term land use are connected. Over the last 100 years, several radical revolutions (land reforms, nationalization, reorganization, privatization, etc.) have taken place in this area. [50] During the decades of communist dictatorship, the fundamental rights of citizens, so as their rights to property was often violated. State interventions affecting the farm structure often neglected economic-management aspects, eg. it was not considered an issue to establish viable economic units (farms) after the regime change and the liquidation of Soviet-type cooperatives; economically related lands and economic equipment and machines were not in the hands of a single owner.[51]

There are several models of farm regulation in Europe.[52] Currently, Hungary occupies a transition between these, its agricultural legislation is fragmented (incomplete) and only partially capable of

[46] The Common Agricultural Policy – instruments and reforms. Fact Sheets on the European Union, European Parliament, 2018. http://www.europarl.europa.eu/factsheets/en/sheet/107/a-kozos-agrarpolitika-kap-eszkozei-es-ezek-reformjai (last access: 05.06.2019).

[47] According to the data of the Hungarian Central Statistical Office (HCSO/KSH) in 2017, almost 60% of the country"s agricultural land was arable land.

https://www.ksh.hu/docs/hun/agrar/html/tabl1_3_1.html (last access: 20.05.2019).

[48] Gazdaságkutató Intézet: *Az „elmúlt 8 év" és a „majdnem elmúlt 8 év." A mezőgazdaság teljesítménye.* [Institute for Economic Research: The "past 8 years" and the "almost past 8 years". The performance of agriculture] Budapest, 2017. https://www.gki.hu/wp-content/uploads/2017/11/GKI-Az-elmút-8év-Mezőgazdaság.pdf (last access: 20.05.2019).

[49] Kovách, p. 83.

[50] Kovách, pp. 14-15.

[51] For the legal problems of the agricultural policy measures of the regime change *See:* L. Fodor, *Agrárjog (fejezetek a mezőgazdasági életviszonyok sajátos szabályozása köréből) [Agricultural law (chapters on the specific regulation of agricultural life)]*, Kossuth Egyetemi Kiadó, Debrecen, 2005, 78-106.

[52] The differences between the models can be captured in the following areas: restriction of the acquisition of property, regulation on the size of the land, provision of official approvals, regulations for the farmer (e.g. expertise, local residence, the obligation to operate the farm, i.e. to cultivate the land). Some countries use additional instruments to protect small lands or tenants, while there are countries that have an liberal and institutionalized land policy. K. Bányai: A magyar mezőgazdasági föld tulajdoni és használati forgalmának jogi korlátai és azok kijátszása [Legal Limitations on the Ownership and Use of Hungarian Agricultural Land and its Circumvention] (PhD thesis), Miskolc, 2016.; T. Prugberger Tamás: Szempontok az új földtörvény vitaanyagának és a parlament által elfogadott szövegének értékeléséhez a nyugat-európai megoldások tükrében, [Considerations for the Evaluation of the Debate of the New Land Act and the Text Adopted by the Parliament in the Light of Western European Solutions] *Polgári Szemle*, 2014/3-6, 162-169.; A. Burgerné Gimes: Földhasználati és földbirtok-politika az Európai Unióban és néhány csatlakozó országban, [Land Use and Land Policies in the European Union and in Some Acceding Countries] Közgazdasági Szemle, 2003 szeptember, 819-832.; M. Kurucz: *Mezőgazdasági ingatlanok agrárjogi szabályozása.* ELTE Jogi Továbbképző Intézet, Budapest, 2001; T. Prugberger, J. E. Szilágyi: *Földbirtok-politika az EU-ban. [Land policy in the EU]* In Cs. Csák (Ed.), Agrárjog, Bíbor Kiadó, Miskolc, 2004, pp. 69-83.

fulfilling its task.[53] After the change of regime, the most important question was how large the size of the land owned or used by one person could be (at the same time, it was also a question whether companies could acquire land), but almost all governments had different ideas about it.[54] These changing ideas were also partly followed by legislation. The current regulations on Hungarian land policy (e.g. the Land Act, the National Land Fund Act)[55] focus on the objective of the spread of family farms. At the same time, fragmentation is not hampered by Hungarian law, nor is it able to prevent land property concentration. The operation of the National Land Fund is not fully in line with the agricultural policy goals[56] that have been declared because it promotes the industrial concentration of land.

### 2.2.3. Tax equity rules adjusted to precision agriculture

Precision farming is not subjected to specific regulations in tax law, so I examined the main agricultural features in the tax system.[57] Compared to the general income tax rules, several tax equity regulations apply to farmers (e.g. simplified declaration, exemption from tax liability under a certain level of income). It may be a question of how the farmers performing PA can benefit of these. The answer, however, does not depend on the use of precision tools, but on, for example, the amount of revenue, the type of farming (company, individual), etc. In addition, it is interesting to know what costs can be accounted (e.g. the purchase of the machine and the cost of the internet can be) and for how long (i.e. what rule of amortization / depreciation applies). There are also agricultural subsidies within the VAT rules, for example the so-called compensation surcharge (this, however, is related to the supply of goods or the provision of services - the latter may be interesting because machine rental is an agricultural service). The legal status of the producer is also important here, and whether there is any other activity / income beside

[53] Ultimately, in the absence of a long-term, coherent agricultural policy, Hungarian regulation is the framework for original capital accumulation that has taken place in the agricultural sector ever since the change of regime (this is reflected in the fact that since the change of regime there has been a significant reorganization - ownership concentration - regarding ownership and use conditions).Kovách, pp. 22-26.

[54] The point of one of the concepts is the development of small plants, the promotion of the spread of medium-sized farms, the point of the second is the provision of industrial farming and the position of companies. The acquisition of land by companies (that was one of the most controversial ideas) in the end was not made possible by the Hungarian law.

[55] According to the Preamble to the Act LXXXVII of 2010 on the National Land Fund, one of the objectives of the regulation is to promote the development of a modern farm structure based on family farms. The Preamble of the Act CXXII of 2013 on the transfer of lands used for agriculture and forestry defines the goal to organize rural family communities as a production community and to spread medium-sized agricultural enterprises and to ensure the stable operation and further development of small farms.

[56] Until 2014, the Land Fund could also help the establishment of farms with a higher than the maximum land, and could also enter into long-term lease contracts with tenants for up to 50 years. These solutions were criticized from an agricultural policy point of view by Gy. Domé: A földtörvény néhány elméleti és gyakorlati kérdése. [Some Theoretical and Practical Questions of the Land Act] *Gazdaság és Jog*, 2002/7-8, 39. Stability in land use rights has been compromised by the fact that in 2015, because of the changing law it has been made possible to terminate previously concluded lease contracts that have not expired, so that new owners could easily deprive those tenants their right to use the land, who have signed a contract with the state,. I note that in recent years the rules for utilizing land-based land have come closer to land policy, but the legality of the operation of the Land Fund has been questioned in many cases, which I have already referred to.

[57] Based on the 2019 detection and interpretation of the Hungarian national tax authority. https://www.nav.gov.hu/data/cms489589/06_Mez_gazdasagi__stermel__maganszemely_adozasanak_alapvet__szabalyai_20190125.pdf (last access: 20.05.2019).

agriculture. PA mostly means field crop production in Hungary, so it is interesting that in some cases the buyer pays the VAT instead of the producers (this is called reverse taxation, e.g. in case of corn, wheat, sunflower seed production).

It is important to see that the national regulation of taxation and the EU regulation of agricultural subsidies is linked (not only because of the financial situation of farmers, but also because there are subsidies in the tax system, and because some tax rules also apply to subsidies, e.g. when calculating income, or a t the cost accounting of assets purchased from the subsidy).

As I and most likely the farmers themselves view, additional benefits for PA (for the time being) are difficult to imagine.

#### 2.2.4. The role of PA-friendly political environment

From the statements made by the Hungarian Minister of Agriculture, [58] the EU Commissioner for Agriculture or the interest groups (National Agricultural Chamber, farmers" organizations, associations)[59] conclusions can be drawn on the future regulatory efforts on the field of agricultural policy. Farmers can formulate expectations regarding the institutional system and the legal framework (including the conditions of subsidies). It is difficult to research this sphere with legal science methods, but it is certain that the PA is an actual topic, and it is expected that both EU and national legislators will put the issue of regulation on the agenda to promote the spread of PA. Therefore, in the press news (at least recently) signs of a PA-friendly political environment has been shown, and farmers have also attached importance to it, even if not to the extent as to the institutionalized agricultural policy or to the predictability of land use. In addition to political statements, however, it is important that PA - together with all its advantages and potential disadvantages – to be more widely known by society (not only by farmers but also by consumers).

## 3. Conclusions

This Study reviewed the legal regulatory issues relevant to the spread of PA, based on an empirical research. Research questions were primarily determined by the opinion of the farmers. Other methods and considerations could definetly raise additional regulatory challenges (e.g. in the fields of the market regulation, labelling, nature protection, farm management, soil protection etc.). Other factors that are important to farmers – additional costs, availability of labor, farm size, land market development, etc. – are subject to further research.

The research focused on Hungarian law, but the experiences in Hungary (due to the similarities of economic and social environment, land ownership and use, CAP effects, common problems in the field of co-operations, etc.) seem to be exploitable in several respects regarding other countries in the Eastern European region.

In the light of the CAP and the Member States" agricultural policy margin including several elements of national agricultural regulation, it seems that solving issues relevant to PA is not possible only within the framework of national legislation, i.e. action at EU level is also necessary, especially as regards the subsidy system.

[58] According to the Hungarian Minister of Agriculture (2019), the precondition for competitiveness is the spread of PA. https://www.agrarszektor.hu/gepek/nagy-istvan-precizios-gazdalkodas-nelkul-nem-lesz-versenykepes-a-magyar-mezogazdasag.12821.html (last access: 20.05.2019).

[59] E.g. the Hungarian Chamber of Agriculture has successfully initiated legislation in many cases.

These problems are extremely diverse from a legal point of view, affecting most of the classic areas of agricultural legislation. In addition, constitutional law, EU law, environmental law, tax law, water law and other regulations have an important role to play. It can be concluded from this that the promotion of the spread of PA cannot be solved by a single intervention (e.g. with subsidies).

The legal and administrative barriers that the farmers have indicated does not only affect precision farmers but also other farms, in a more or less the same way. Concludingly, the requirement can be set to legislator to promote the spread of PA but not only directly (specifically) through PA measures.

If all of the above is considered by the regulations, it can have positive effects for the whole economy and society, and the risk of regulatory failures can be kept low, in addition to the costs of interventions.

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# RECENT CHANGES IN HUNGARIAN TAX PROCEDURES DUE TO DIGITALISATION[*]

**Zoltán VARGA**[**]

**Abstract**

*The digitalization has a great impact to the Hungarian tax procedures in the last years, so in this short article I will review these and present the major milestones. One of them was the Electronic Road Traffic Control System; and the other is the Online Account system, which can effectively help to ensure the highest possible level of tax revenues.*

**Keywords:** *digitalisation, tax procedure, Electronic Public Road Trade Control System, online account system*

## Introduction

In the past few years there were many changes in the taxation as an impact of the digitalisation. This article aims to overview about these innovations. One of them is the Hungarian Electronic Trade and Transport Control System - the so called "EKAER" System and the other is the online invoice system.

Because of the increased trade and the establishment of international chains the transporting of goods became more and more complex. That is the reason why the traceability of goods is emphasized nowadays. From 1 January 2015 the road transportation control system was introduced in order to prevent VAT fraud.[1]

The reporting obligation applies to acquisitions of goods from another EU Member State to the territory of Hungary or acquisitions for other purposes, supplies of goods from the territory of Hungary to another EU Member State or supplies for other purposes, and first supplies of goods subject to taxation in domestic trade, to other than end users, involving road transportation, if performed by using vehicles subject to road toll payment. The reasons of the introduction were the insurance of transparent goods"transportation, to filter foodstuffs containing ingredients unfit for humanconsumption and to reduce VAT fraud. Some products (sugar, oil) were succesfully filtered out by the road transportation system and as the results of the supervision it was obvious whether there was transportation between states or not. But it is important to mention that there are still remaining products like UHT milk and

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[1] Höflinger, Hajnalka: Az EKÁER mint egyedülálló megoldás [EKÁER as n unique solution] (Adó- és Pénzügyi Szaklap, XXIX. évfolyam, 2015/14. szám

popular IT-tools, where the fraudsters have chance to try to avoid taxes. According to the scientific literature the road transportation control system is a success. Since the setting of the system together with roadside checks and permanent investigation 100 thousands of controlls were carried out and an amount HUF 16 billion have been flown into the State budget. Good sign of success of the online cash register and EKÁR besides of the economic growth that last year an amount HUF 400 billion plus realised in the State budget. However there are some gaps in the system and the tax authority has to be up to date in order to prevent fraud. The scope of the notification has been increased. Not only does it have to announce the carriage of goods carrying a cargo of over 3.5 tons with a tolled vehicle, but the requirement for any vehicle, such as commercial vehicles, to reach 3.5 tons. This was necessary because the carriers shifted to the practice of overcharging the 3.5 tonnes of motor vehicles and thus delivering more goods, without the cargo would have been obligatory to EKÁER. It is also irregularity if they do not report a cargo and also reports more than they actually deliver.

Another problem is if the carrier carries a risky product with a weight of less than 500 kg or less than 1 million forints, it is not obliged to apply for an EKÁER number. A similar problem can be mentioned even among non-risky products that the vehicle does not cover vehicles up to 3.5 tons. So, whoever wants to avoid the system, it delivers the goods abroad by this method, because it does not count as illegal.

According to the opinion of the authors it would not be a good solution to wider the scope of the notification because of the burden of administration, it would be better to increase the number of roadside checks in the near of border crossing points. Significant changes have taken place with regard to official closure, and we may already find concerns before the implementation of the regulation. If the carrier fails to comply with its reporting obligation or other risk factors justify the application of the fiscal lock. Authority abolition was abusive; therefore decision-makers placed responsibility on the carriers to retain the official lock in an unharmed state from attachment to lock. If the carrier removes an official seal without the permission of the authority, the tax authority may fine it. Another major innovation is that the vehicle can now be held back by the inspectors until the payment of the fines imposed if the punished carrier does not have a Hungarian tax identification number and has his seat, residence, habitual residence in Hungary and no guarantee of payment of the fine. It follows that, the lock down is not cover equally all cases. Transport vehicles of the Hungarian carriers can not be hold back, but the transport vehicles of foreign carriers can.

It appears that the regulation benefits the domestic carriers, so the regulation is contrary to the principles of the EU.[2]

## The Hungarian electronic trade and transport control system - the "EKAER" system

Hungary introduced the EKAER[3] system to fight against tax fraud. The aim of

[2] Zoltán Nagy-Beáta Gergely- Balázs Katona: *Problems relating to tax avoidance and possible solutions in the European Union"s and Hungarian Regulation.* Curentul Juridic, The Juridical Current, Le Courant Juridique, Petru Maior University, Faculty of Economics Law and Administrative Sciences and Pro Iure Foundation, vol. 74, page 64, September 2018.

[3] Regulation No. 5/2015 (II. 27.) NGM of the minister of national economy on the operation of the electronic public road trade control system

the system is to track the actual route of goods and to ensure public revenues generated during the acquisition and sale of goods.

The objective of the system is to strengthen the market positions of compliant economic operators, to make circulation of goods more transparent, to eliminate fraud related to food products often endangering human health and; last but not least, to eliminate tax evaders.

The following taxpayers are required to register and report under EKAER[4]:

- who acquire or import goods from the European Union to Hungary by means of a vehicle that is subject to toll,
- who sell or export goods from Hungary to the European Union by means of a vehicle that is subject to toll,
- who is engaged in the first taxable sale of goods to an entity other than a consumer by means of a vehicle that is subject to toll.

Failure to register may lead to the seizure of the consignment and may give rise to a fine up to 40 percent of the value of the goods.

Firstly it is important to determine the definitions based on the Act CL of 2017 on the rules of taxation.[5]

EKAER shall mean the Electronic Public Road Transportation System operated by the state tax and customs authority, intended to monitor compliance with tax obligations arising in connection with the transportation of goods on public roads from any Member State of the European Union to the territory of Hungary, or from the territory of Hungary to any Member State of the European Union, or within the framework of internal trade inside the territory of Hungary.[6]

*EKAER number* shall mean an identification number assigned following notification of the public road transportation of a product by automated process in the Electronic Public Road Transportation Control System (EKAER) intended to identify a unit of a given product.[7]

*Motor vehicle* shall mean a motor vehicle subject to toll charges and any means of transport with less weight, covering trucks, lorries - including semi-trailers - and combinations of vehicles comprised of trailers and semi-trailer.[8]

*Goods of unverified origin* shall mean any merchandise and material for which the taxpayer is unable, at the time of audit, to produce an authentic document of origin or an instrument to substantiate such document.[9]

*Perishable foodstuff* shall mean products that have a shelf life and expiration date specified in compliance with the Act on the food chain and its authority supervision.[10]

*Motor vehicle subject to toll charges* shall mean a motor vehicle that is subject to toll charges under the Act on the fees charged for the use of tolled motorways,

[4] *Act CL of 2017 on the rules of taxation (Art.) Article 7 [Definitions] 14. EKAER shall mean the Electronic Public Road Transportation System operated by the state tax and customs authority, intended to monitor compliance with tax obligations arising in connection with the transportation of goods on public roads from any Member State of the European Union to the territory of Hungary, or from the territory of Hungary to any Member State of the European Union, or within the framework of internal trade inside the territory of Hungary.*

[5] Act CL of 2017 on the rules of taxation, in the following in Hungarian abbreviation: Art.

[6] Art. 7§ 14.

[7] Art. 7§ 15.

[8] Art. 7§ 21.

[9] Art. 7§ 23.

[10] Art. 7§ 41.

main highways and regular highways based on the distance travelled.[11]

## Obligations relating to the electronic public road transportation control system

For transporting goods on public roads via any motor vehicles subject to charge it will be required to apply for an EKAER number. Every number will be valid for 15 days and those organizing and executing the transit must have them as it must be presented during potential roadside checks by the authorities.

In Hungary only vehicles over 3,5 tons are subject to paying usage-proportional road toll when using highways and other and other roads and road sections defined by law. This toll is proportional to the distance travelled on tolled roads and is determined by the axle number and EURO class of the vehicle. Vehicles under 3,5 tons using tolled roads, e.g. highways have to pay toll in a vignette system, where the toll is not proportional to the distance travelled but a fixed price have to paid for a certain period of time.

Those who transport goods to Hungary using public roads from member states of the European Union, who transport goods from Hungary to member states of the European Union and everyone engaging in taxable product selling via public road transportation not targeting end users are obliged to apply for an EKAER number for every transport.[12]

By using EKÁER the actual route of the goods can be tracked because transport related data (name and quantity of goods, consignee, consignor, registration number of vehicle, etc.) have to be registered in a central electronic system before starting the transport. Some of these data (product weight, value, and registration number of vehicle) can be modified up until the arrival of the cargo and can be registered in the system on the first working day after the time of arrival to the address of receipt (unloading). Stating the registration number of the vehicle is not a precondition to determining the EKAER number but it has to be registered up until the start of transport.

The obligation for making data submissions mainly affects the domestic trading parties, the seller and the buyer.

A precondition for registration in EKAER is the access to the Client Gateway. Those already having access to the Client Gateway can create a right of access to the EKÁER electronic surface in two steps:

- First the legal representative, permanent trustee of the taxpayer (primary user) applies for username and password then
- after log-in to the EKAER electronic surface they apply for access rights for those persons (secondary users) who may submit or modify data.
- The obligation to submit data applies for each and every road transport of goods performed by using vehicles subject to road toll payment (i.e. vehicles exceeding 3.5 tons of maximum gross weight).

It is obligatory to report:

- for the consignee/recipient: intra-Community buying and import for other purposes,
- for the seller/consignor: sales to another EU Member State and export for other purposes;
- for the seller: first taxable domestic sale if it is not for and end-user.

Domestic products subject to reverse taxation are not exempt from the obligation to submit data.

[11] Art. 7§ 50.
[12] Art. 113. §

However, certain goods are exempt from the data submission obligation, e.g. relief supplies or vehicles participating in disaster relief, or road transport in the context of collecting freight if the quantity/value of the given product does not exceed the limit specified in the law, and in the case of transporting certain excise goods specified in the law. Non-risky goods with a net value not exceeding 2 million HUF and with a weight not exceeding 2.5 tons are exempt from the data submission obligation.

In the case of certain goods (risky food products and other risky products) the rules for submitting data in EKÁER cover also their transport by vehicles not subject to road toll payment (vehicles with lower than 3.5 tons of maximum gross weight), depending on the value and weight limits of those goods. This limit for risky food products is 200 kg or net 250000 HUF, for other types of risky products it is 500 kg or net 1 million HUF. The range of risky products can be found in the Annex to the Regulation of the minister of national economy.

All taxpayers engaged in activities involving transportation using public roads and transporting hazardous products has to pay a *security deposit*. Wage transport is exempt from this rule.

In the case of food products within the competence of the National Food Chain Safety Office a so-called FELIR identification number is also needed which requires the registration of the company and the first Hungarian place of storage.

In addition to submitting data, from 1 February 2015 a guarantee must be provided and maintained for risky food products and other risky products throughout the business operation. An exception from this is the export from Hungary to another EU Member State. The amount of security is 15 % of the net value of risky products registered in EKÁER in the course of 60 days prior to the submission of data (including the day of the submission); this may be reduced in some cases. The following entities may be exempted from the provision of a guarantee:

- taxpayers included in the database of qualified taxpayers or
- taxpayers that have been in business for at least 2 years, are included in the database for taxpayers free of public debt and the tax number of whom has not been suspended at the time of the data submission.

The system generates an EKÁER number[13] valid for 15 days when data is submitted which is connected to the transport. The transport operator or transport organizer has to be informed about the EKÁER number.

Unreported goods shall be deemed of unconfirmed origin, upon which a default penalty amounting up to 40% o[14]f the value of the unreported goods may be imposed. [15]The National Tax and Customs Administration may seize the goods to the extent of the amount of the default penalty or use an official seal.[16]

There are exemptions from submission of data.[17]

[13] Act CL of 2017 on the rules of taxation (Art.) Article 7 [Definitions] 15. EKAER number shall mean an identification number assigned following notification of the public road transportation of a product by automated process in the Electronic Public Road Transportation Control System intended to identify a unit of a given product.

[14] Article 226 [Supply of goods of unverified origin and the irregular fulfillment of the EKAER disclosure obligation](3)

[15] See detailed: http://ekaer.hu/en/ (30.09.2019.)

[16] Decree 5/2015 (Feb 27) of the Ministry for the National Economy on the operation of the Electronic Public Road Transportation Control System

[17] Exempt from the obligation to submit data:

*Information disclosure by the tax authority*

The state tax and customs authority shall disclose confidential tax information to the investigating arm of the state tax and customs authority in the interest of the prevention of criminal offences, and the investigation and detection of specific criminal offences, and for the prosecution of criminal cases.[18]

There are two types of the taxpayers in Hungary. These are the reliable taxpayers and the others are the risky taxpayers. The sanctions are different for these taxpayer groups, so I would like to introduce the rules that apply to them.

Since April of 2016 the classification of tax payers came into operation and it classifies the tax payers into 3 categories, like reliable, average and risky tay payers. The system has several advantages: the authority can supervise the risky companies and can warn the companies about the risky companies. This warning has a huge meaning, because in case of a tax audit, the company can not submit good faith if the audit of the tax authority reveals problems. The companies have to check the tax number of their business partners before and during the transaction and have to weight the factors because it can be serious consequences in case of business with a risky company. The tax authority classifies the business undertakings in every querter. The Companies with complience behaviour will be benefited and the risky companies will be sanctioned. The reliable companies have to meet strict condition. The reliable tax payers will be benefitted, for example in case of a tax penalty they will get payment in

vehicles of the Hungarian Defence Forces and the Military National Security Service, vehicles of law enforcement agencies according to the act on national defence, Hungarian Defence Forces and on measures applicable in special law, and vehicles of the Parliamentary Guard;

official or service vehicles of foreign armed forces stationing in or passing through Hungary, and of international military headquarters set up in Hungary for service purposes, and vehicles of other organisations exempted on the basis of international treaties, agreements and reciprocity;

vehicles participating in preventing or averting damages caused by a disaster defined in the act on disaster relief;

vehicles covered by international treaties or agreements (NATO, Schengen Agreement) and reciprocity;

vehicles transporting non-commercial (free of charge) humanitarian relief supplies;

vehicles exclusively transporting goods covered by the law on excise taxes and special regulations on the distribution of excise goods: alcoholic products, beer, wine, sparkling wine, intermediate alcoholic products, tobacco products, dried tobacco, controlled mineral oil products, bioethanol, biodiesel, E85 or several from these;

the taxpayer, if the weight of non-risky goods sent by him or addressed to him in one transport with the same vehicle subject to road toll payment does not exceed 2500 kg or if the non-taxed value of those goods does not exceed 2 million HUF;

the taxpayer, if goods sent by him or addressed to him in one transport with the same vehicle subject to road toll payment:

the weight of risky food products does not exceed 200 kg or its non-taxed value 250 000 HUF,

the weight of other risky products does not exceed 500 kg or its non-taxed value 1 million HUF.

Exemption from the obligation to provide a risk security

Security must be provided only if the taxpayer

imports risky products from another EU Member State to Hungary or imports for other purposes, including bringing own products to Hungary from another EU Member State;

sells risky products as a first taxable domestic sale for not an end-user.

The taxpayer is exempt from the obligation to provide a risk security if

– they are included in the database of qualified taxpayers or

– if they meet all of the following conditions:

– have been in business for at least 2 years and

– are included in the database for taxpayers with no public debt and

– their tax number has not been suspended at the time of the data submission.

[18] Article 131 (15) [Information disclosure by the tax authority]

instaltment. The average tax payers are regulated by the normal rules. From the regulationit is obvious that the risky companies have to expect continued audits in order to promote their legitim operation.[19]

*Sanctions for reliable taxpayers*

The upper limit of the *default penalty* that can be imposed by the state tax and customs authority shall correspond to fifty percent of the upper limit of the default penalty that can be imposed pursuant to the general rules provided that at the time of occurrence of the violation of the relevant legal regulations or the exploration of the violation of the relevant legal regulations (preparation of the report) the taxpayer is deemed as a reliable taxpayer.[20]

The upper limit of the default penalty that can be imposed by the state tax and customs authority shall correspond to fifty percent of the upper limit of the default penalty that can be imposed pursuant to Section (3)–(4) of Article 215 provided that throughout the tax assessment period under tax inspection or on the date of the report describing the findings of the tax inspection the taxpayer is deemed as a reliable taxpayer. [21]

These provisions shall not be applicable to defaults or cases of the assessment of any tax difference that result in the loss of the reliable taxpayer qualification.

*Tax fines, default penalties for risky taxpayers*

If at the time of occurrence of the violation of the relevant legal regulations or the exploration of the violation of the relevant legal regulations, or on the date of the report describing the findings of the follow-up tax inspection the taxpayer is deemed as a risky taxpayer, the state tax and customs authority may not decide to neglect the imposition of a tax fine and default penalty, and the minimum amount of the fine that can be imposed shall correspond to thirty percent of the upper limit of the default penalty that can be imposed pursuant to the general rules. [22]

The upper limit of the default penalty that can be imposed by the state tax and customs authority shall correspond to one hundred and fifty percent of the upper limit of the default fine that can be imposed pursuant to the general rules provided that at the time of occurrence of the violation of the relevant legal regulations or the exploration of the default (preparation of the report) the taxpayer is deemed as a risky taxpayer.[23]

It is important to overview the rules of the default penalty and the measures in bonnection with the EKÁER.

*DEFAULT PENALTY*[24]

*General rules of fines*

Unless it is otherwise required by the relevant legal regulations, the tax authority may impose a default penalty in an amount of two hundred and fifty thousand Hungarian Forints on natural person taxpayers and five hundred thousand Hungarian Forints on non-natural person taxpayers in the event of any violation of the

[19] Zoltán Nagy-Beáta Gergely- Balázs Katona: *Problems relating to tax avoidance and possible solutions in the European Union"s and Hungarian Regulation.* Curentul Juridic, The Juridical Current, Le Courant Juridique, Petru Maior University, Faculty of Economics Law and Administrative Sciences and Pro Iure Foundation, vol. 74, page 65, September 2018.

[20] Article 155§ (1)

[21] Article 155§ (2)

[22] Article 161 § (1)

[23] Article 161 § (2)

[24] CHAPTER XXX

obligations stipulated in this Act, other legislations prescribing tax-related obligations and other legal regulations based on the authorizations granted in these legislations.[25]

The fulfillment of the obligation with the provision of incorrect, incomplete or unreal information, as well as any delayed fulfillment or non-fulfillment of the obligation shall be deemed to be the violation of the obligation.[26]

In the case of any delays, no default penalty may be imposed provided that in addition to the fulfillment of the obligation the taxpayer justifies the delay by evidencing that he has acted as it can be generally expected in the given situation. [27]

*Supply of goods of unverified origin and the irregular fulfillment of the EKAER disclosure obligation*

Where the taxpayer supplies goods of unverified origin, the tax authority may impose a default penalty in the amount up to forty percent of the market value of the goods in question, or up to two hundred thousand Hungarian Forints in the case of natural person taxpayers and up to five hundred thousand Hungarian Forints for non-natural person taxpayers. [28]

If the taxpayer

a) failed to comply with the disclosure obligation with respect to the goods carried or a part thereof, or
b) the information supplied under such notification requirement is incorrect, false or incomplete, the state tax and customs authority may impose a default penalty on the taxpayer up to forty percent of the value of goods having remained undisclosed, or having been disclosed with incorrect, false or incomplete information.[29]

If the state tax and customs authority finds during an inspection that the taxpayer fulfilled its EKAER disclosure obligation with the supply of false information so that the quantity of the undisclosed products exceeds the actually carried quantity of products, then it may impose a default penalty on the taxpayer up to 40 percent of the value of disclosed goods that were not in fact carried.[30]

*MEASURES*[31]

*Seizure upon the irregular fulfillment of the disclosure obligation relating to the carriage of products on public roads*

If the state tax and customs authority imposed a default penalty for non-compliance with the EKAER disclosure obligation, or if the information supplied is incorrect, false or incomplete, it may seize the goods carried - with the exception of perishable goods and live animals - covering up to the amount of the penalty imposed, in security thereof, and shall so provide in the resolution imposing the penalty.[32]

*Common rules pertaining to seizure*

The state tax and customs authority shall draw up a report on the seizure, seal off the property seized or remove it from the premises for safeguarding at the expense of the taxpayer affected.[33]

[25] Article 220§ (1)
[26] Article 220§ (2)
[27] Article 220§ (3)
[28] Article 226§ (1)
[29] Article 226§ (2)
[30] Article 226§ (3)
[31] CHAPTER XXXI
[32] Article 240§
[33] Article 241 § (1)

The state tax and customs authority shall communicate the resolution it has adopted for imposing a default penalty to the attending taxpayer, his representative or proxy, or employee, whoever is available. The resolution shall be enforceable as of the date of communication notwithstanding any appeal.[34]

*Retention of the vehicle*

f the state tax and customs authority imposes any default penalty for the violation of the obligation to keep the official seal, the vehicle of transport – with the exception of the vehicles of transport carrying perishable goods and livestock – until the payment of the fine imposed during the inspection conducted by the authority or the provision of guarantee for the financial liabilities without the issuance of any specific resolution.[35]

The vehicle may not be retained in case

a) the registered seat, address or usual place of residence of the obligor(s) of the payment of the fine are in the territory of Hungary, and the obligor is in possession of a tax number or tax identifier having been issued by the state tax and customs authority, or
b) a financial institution assumes suretyship, guarantee for the fulfillment of the obligation to pay the fine, or the obligation is taken over by any domestically registered economic entity that has a tax number, and this fact is authentically evidenced by the obligor of the fine payment during the proceedings.[36]

If a foreign transport operator impedes the removal of the official seal that has been attached by the state tax and customs authority, with respect to the vehicle of transport owned or used by the transport operator the state tax and customs authority may apply the actions described in Section (1).[37]

For the purpose of this Article, the foreign transport operator shall be deemed as such a person involved in the movement of products in the territory of Hungary that

a) is not settled and otherwise does not pursue economic (production, service, operating, business) activities in Hungary as a legal person or other organization,
b) is a natural person driving the vehicle, but has no address or usual place of residence in Hungary, and
c) is the natural person driver of the vehicle involved in the movement of products that are owned by the legal person or other organization defined in Paragraph *a)*. [38]

***Practical questions in connection with the EKÁER System***[39]

*Recapitulative (VIES) report*

Taxpayers are required to file a consolidated statement regarding the products sold and the services rendered within the European Community and the products procured and services used from the European Community on a monthly or quarterly basis. The recapitulative report is to be filed with the same frequency as VAT returns.

*Recapitulative report*

From 1 July 2018, VAT-able persons will have to file a detailed declaration on the

[34] Article 241 § (2)
[35] Article 243 § (1)
[36] Article 243 § (2)
[37] Article 243 § (3)
[38] Article 243 § (4)
[39] https://doingbusinessinhungary.com/taxation (30.09. 2019.)

invoices accepted of acquisitions of goods and services in which the amount of VAT charged reaches or exceeds HUF 100,000. The taxpayer may fulfil the obligation of submitting recapitulative reports voluntarily, independently from a limit value.

*Real time online supply of data on invoices*

After 1 July 2018, all taxable persons registered in Hungary will have to supply data electronically on the invoices issued to domestic taxable persons on supplies of goods and services in which the amount of tax charged reaches or exceeds HUF 100,000.

*Invoicing software notification*

All taxpayers are obliged to notify the invoicing software used by them to the tax authority. The invoicing software is required to have an independent but integrated function titled "tax authority inspection data disclosure" that can export data concerning the invoices issued in the format prescribed by the tax authority ("NAV").

*Tax filing and payment deadlines*

Depending on the amount of their tax liability, taxpayers are required to file tax returns and pay the tax on a monthly, quarterly or annual basis until the 20th day of the month following the return period and, for annual filers, until 25 February of the year following the tax year. A liability to file a recapitulative statement or recapitulative report may also arise in relation to the filing obligation. In other words, there is no "preliminary" and final tax return in the Hungarian system but rather all tax returns filed are considered a final statement.

*VAT refund to foreign entities*

As of 1 January 2010, taxable entities seated in another EU member state are entitled to reclaim the Hungarian VAT by electronically submitting an application to the tax authority of the country where they are seated.

Taxpayers established in eligible third countries (Switzerland, Liechtenstein, Norway and Serbia) can submit their applications directly to the Hungarian tax authority either in paper format or electronically.

Taxpayers with a registered office or permanent site in Hungary have to apply to the National Tax and Customs Administration (NAV) for the reclaim of the value added tax paid in another member state of the European Community (foreign VAT). NAV only has a preliminary filtering role in the procedure if the applicants fulfil the requirements of the law. The office is required to forward applications to the foreign authorities within 15 days of their receipt. The deadline for receiving applications is 30 September of the year following the relevant year.[40]

## The system of online invoice

From the 1 January 2016. Every online billing programs had to have data service function. In case of an audit the billing program providees data about a defined period or defined invoices. It is important that in case of amount of 100.000. Ft VAT it was obligatory to report about the invoices to the tax authority. The system was under testing from 1 January 2017. The aim of the tax authority was to introduce the automatic data services. Similar systems are used in Turkish and Brazil with the exception that in those countries only the tax authorty is entitled to issue online invoices. From 1 January 2017 the invoice shall contain the tax number os the buyer if the amount of VAT is or over 100.000 Ft. After the testing period the system entered into force.

[40] See detailed the experiences: KÖCSKY Rudolf: EKÁER tapasztalatok az utólagos ellenőrzési szakterület szemével. [EKÁER experience in the field of ex post control.] ADÓVILÁG XXII. évfolyam 04. szám. 40-43. p.

Advantage of the system that the data service is full and clear. Together with the EKÁER it could be a great tool to filter out fictional invoicing and of course it contributes to environmental protection because it can decrease the amount of the paper invoicing. The disadvantage of the system is that cause huge administrative burdens and costs to the companies. In order to reduce the costs the government enhance to issue free billing programes to the companies.[41]

As of 1 July 2018 it is obligatory to provide date on the invoices containing charged value added tax at least of 100,000 HUF, issued of the transactions between domestic taxpayers.

As of 1 July 2018 the data disclosure regarding the data of the invoices issued (and documents to be regarded as equivalent to invoice) shall be fulfilled after the issuance, within a short period of time, by electronic means. In case of invoicing with the use of billing/accounting software the invoice data shall be transmitted to the NTCA without human intervention, via the public internet immediately, after the preparation of the invoice.

Data of the invoice shall be recorded on web interface in case of invoicing with the application of form, e.g. invoice pad (accordingly manual invoicing). The data report shall be fulfilled within five calendar days. This deadline is shortened if the invoice contains charged tax of 500,000 HUF or more than this amount. The data of the invoice containing of HUF 500,000 or more charged tax shall be recorded on web interface on the day after the day on which the invoice was issued.

The data disclosure liability in principle is covered by such an invoices issued on the transactions between domestic taxpayers in which there is HUF 100,000 or more charged tax.

The objective of the introduction of the online data report and of the establishment of the data management system is to further whiten the economy by discouraging tax frauds. This is complemented by the free online invoicing function, as a service of the NTCA. With this development a large amount of invoice turnover become visible and traceable for the NTCA consequently the risk management can be more effective and the VAT revenues can be significantly increased.

Within the system of online invoice

- real-time data on the issued invoices arrive to the NTCA,
- issued invoices can be queried by recipients of invoices and issuers of invoices as well,
- large amount of the invoice data is rapidly available for the purpose of effective risk analysis and audit which is assisting the detection of tax frauds,
- with the automation of the data report, the administrative burdens are reducing for users of billing/invoicing software,
- the new system substitutes the consolidated data report of issuers of invoices.

The basis of the solution is such a combined IT system which is able

- to receive and to control the invoice data that were sent in an electronic standard message as well as to confirm the sending, with the application of a system-system connection provided to taxpayers,
- to support manual recording of invoice data on a web portal,
- to trace economic activities and processes via the immediately available invoice data.

[41] Zoltán Nagy-Beáta Gergely- Balázs Katona: *Problems relating to tax avoidance and possible solutions in the European Union"s and Hungarian Regulation.* Curentul Juridic, The Juridical Current, Le Courant Juridique, Petru Maior University, Faculty of Economics Law and Administrative Sciences and Pro Iure Foundation, vol. 74, page 65, September 2018.

The online invoice assists the tax audit work of the NTCA, it makes the economic processes more transparent and broadens the group of the compliant taxpayers.[42]

*The registration procedure in the online invoice system*

Pursuant to point 9 of Schedule No. 10 of the Act CXXVII of 2007 on Value Added Tax[43] being in force as of 1st July 2018 the data disclosure within the meaning of points 5 to 8 of the Schedule referred to above shall be fulfilled on the electronic platform provided by our Administration (in the case of issued invoices containing input tax reaching the amount determined by the referred legal regulation, the taxpayer obliged to do so has to perform data disclosure in relation to the data of concerned invoice to the state tax and customs authority).

Registration is needed for the fulfilment of data disclosure obligation, which has to be accomplished either by the ones using invoicing program or by the ones using an invoice pad (invoice issued manually).[44]

*Taxpayer registration*

The precondition for the fulfilment of data disclosure is an existing so-called "client gateway" access (KÜNY storage) of the taxpayer, the legal representative of the taxpayer or rather the appointed agent of the taxpayer.

30 minutes are available for carrying out the registration, however, because of security reasons, which are the re-identification at the client gate, 5 minutes are granted for tax identification code to be provided.

In the possession of the Client Gateway access the single registration of the taxpayer, the legal representative of the taxpayer or the appointed agent of the taxpayer is necessary for the fulfilment of the data disclosure on the electronic platform of the Online Invoice System.

A person registered by the state tax and customs authority can be considered as *legal representative* of the taxpayer who is entitled to represent the taxpayer according to the legislation applicable to the taxpayer. In the case of legal representatives, the state tax and customs authority ex officio provides the procedural right of the legal representatives as of 2014 (the so-called automatic right creation).

*Appointed agent* of the taxpayer registered by the state tax and customs authority is entitled to perform the registration if

- s/he is entitled for full representation in all types of cases before the state tax and customs authority;
- s/he is entitled to administer all taxation cases;
- s/he is entitled to administer all declaration, data disclosures/-supplies related to taxation and all report, submission and application;
- s/he is entitled to administer all data disclosure;
- s/he is entitled to administer the data disclosures related to value added tax.

*Process of the registration of taxpayer"s representative, i.e. process of user"s registration*

As it was already mentioned before, the taxpayer liable to data disclosure must be registered in the *Online Invoice System* to secure the fulfilment of obligation a registration, which can be conducted by the legal representative or appointed agent entitled thereto on behalf of the taxpayer liable to data disclosure. The natural person

[42] Act CXXVII of 2007 on the Value Added Tax Chapter X INVOICING Rules on the Issue of Invoices

[43] Hereinafter referred to as VAT Act

[44] Honosi Krisztina Elvira: Az Online Számla felület használata kapcsán felmerült kérdések és válaszok. *[Questions and Answers related to using the Online Invoice interface]*.ADÓVILÁG 2019.április, p. 29-32.

registering the taxpayer is a so-called *"primary user"*.

In order for the person liable to data disclosure to be able to perform his / her obligation according to legal provisions and without any human intervention in connection with data from his / her invoices produced by his / her invoicing programme, registration of a so-called "*technical user*" is also necessary. After registration of the technical user, those data will be available that are necessary for the communication between the taxpayer"s invoicing programme and NTCA"s server.

In order to perform data disclosure obligation, a so-called "*secondary user*" can also be created. The secondary user is created by the primary user with access rights defined by him / her.

In the course of client registration, technical user and secondary user can be created in one step as well; however, a user can also be created later on after the successful registration, after logging in the Online Invoice portal.

## Conclusions

According to the opinion of the authors the Hungarian tax authority introduces more and more legal instruments in order to prevent tax fraud and in order to protect the sustainability of the highest VAT tax rate in Europe. The Hungarian tax authority is trying to step up with the development of the digital technology and introduced numerous different instruments like EKÁER or online invoce system.[45]

Otherwise there are another innovations. Hungary"s National Tax and Customs Authority (NAV) will become a paperless institution by 2021, Finance Minister Mihály Varga said last year.

NAV"s electronic services are becoming more and more widespread, indicating that taxpayers are on board with making the office completely paperless within a few years, the finance ministry quoted Varga as saying at a meeting.

The move to have NAV prepare all corporate tax returns by 2021 will halve the administrative burdens on businesses, the minister said, adding that the authority would offer a growing number of services over the coming years.

Finance minister noted that since 2017, NAV prepares personal income tax returns. Starting 2018, the authority also prepares corporate excise tax filings. The tax authority can have a key role in boosting the competitiveness of businesses.

The minister also said that over the next few weeks, NAV will be ready to assist companies in adapting to its new online invoicing system and with registering vending machines for mandatory electronic reporting.[46]

I hope that it will become reality.

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[46] https://www.xpatloop.com/channels/2018/06/finance-minister-tax-authority-to-go-paperless-by-2021.html (2019-05-14)

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# EFFECTS OF NEW EMPLOYMENT FORMS AND SOCIAL INNOVATION ON SOCIAL SECURITY IN HUNGARY[1]

**Gábor MÉLYPATAKI***

**Abstract:**

*The transformation of the labor market also brings with it changes in the forms of employment. Digitization will have an impact on employment relationships. Digitization is a multi-layered phenomenon that involves the use of gig economy and artificial intelligence as robots. They are all part of social innovation. In this study, I would like to focus on the impact of social innovation on employment. Following the general introduction, I would like to introduce the Hungarian rules and opportunities. Hungary is a typical Central and Eastern European country with problems similar to its neighbors, such as well-modeled problems, which can help us to think together and find solutions.*

**Keywords:** *social innovation, employment law, new forms of employment, Hungarian legal system, gig economy*

## 1. Introduction

The issue of social security has become more important recently. Primarily, social security means stability. It means such kind of stability in which a citizen of a certain state can count on the state"s support in the case of a crisis in the person"s life. This right also occurs in our prevailing regulation in Article XIX of the Hungarian Fundamental Law. According to the cited article, Hungary strives for providing social security in certain life situations for every citizen.

If we investigate this statement more precisely, the use of the term of "strives" for providing social security for the citizens is important from the viewpoint of social security. The question is what this governmental endeavour is enough for and what it will be enough for in the continuously changing social conditions. In connection with social security the endeavour of the state has become a weakened phrase. It is a weakened phrase in the sense that, according to the relating part of the earlier Constitution (Article 70/E), the state provides proper social security. Compared to the earlier version, this means a step back.[1] But it is necessary to add fast that numerous international commitments provide the persistency of the principle of social security. The protection level does not decrease drastically, however, it loosens the system of obligations binding the state. The

[1] The described study was carried out as part of the EFOP-3.6.1-16-2016-00011 "Younger and Renewing University – Innovative Knowledge City – institutional development of the University of Miskolc aiming at intelligent specialisation" project implemented in the framework of the Széchenyi 2020 program. The realization of this project is supported by the European Union, co-financed by the European Social Fund."

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[1] Téglási András : "Eroding" or rescuing the social state? – or social security in the new Fundamental Law, , "Law Theory Review" 4/2011, http://jesz.ajk.elte.hu/teglasi48.html, (Downloaded: 2018. 09. 15.)

state provides social security based on its measures and institutional system. The latter is called social care system. Social care system means all the activities organized within the framework of the society with the aim to support the members of the society who are unable to take care of their livelihood beyond their own fault or undertake additional burdens from the fund formed by withdrawing some of the financial goods produced by all the members of the society. . Different fields of the social care system are responsible for the support in different life situations. Social insurance, aid services, family allowances and the means of employment policy are the parts of the social care system.

The Fundamental Law lists the life situations in which, according to it, the social care system shall be activated. Pursuant to the text of the law, every Hungarian citizen is entitled to an aid defined by the law in cases of motherhood, illness, disability, widowhood, orphanage or unemployment happened beyond the person"s fault. These rights, that is which kind of social care is needed in a certain life situation, are described by the legislator in more details in the different social laws.. .

However, in my opinion, to understand social security, it is necessary to mention the right to work and free business. This right can be interpreted as an additional condition in this context. Article M of the Fundamental Law even states that the economy of Hungary is based on work creating value and the freedom of business. In my view, however, the interpretation of this right regarding the individual person is important. One of the bases of ensuring a certain person"s living is free work and the freedom of business. A citizen is free to choose his job to ensure his and his family"s financial welfare. Though, work as a factor should be understood indirectly, since in the Hungarian social care system allowances of insurance type are dominant. The primary condition of using these allowances is the prior insurance time which can originate from employment and other legal relationships of work. The amount of the allowances is based on the income acquired during the prior insurance time.

Based on these facts, creating social security is the task of the state, but to ensure his own welfare by acquiring the legitimacy for certain allowances within the state provided framework is the responsibility of the citizen . We must see, however, that the relations in this state framework are dynamic. In its present state only the framework system is constant. Change is the part of our every-day life, therefore the interpretation of social security is also changing continuously. In our present situation, creating social security is the citizen"s ability to ensure his own and his family"s living and acquire eligibility for certain allowances in the state"s framework system thus he is a member of the risk community. If we translate it all into everyday language, , it means that the citizen has a job which brings enough income and makes it possible for him to make use of a wide range of social benefits. From the viewpoint of employment, the citizen has an 8-hour employment relationship with indefinite duration. According to the common Hungarian social opinion, this is the only solution to guarantee secure livelihood in Hungary. This opinion is partly based on traditions, partly on the reluctance from new employment forms and partly on real experience. But the employment relationships and the changes of the labour market do not proceed to the same direction. New, more flexible employment relationships are coming into view. These are the so-called atypical work forms. Flexibility is only one characteristic of atypical work forms. It is also necessary to fulfil the requirements of security for these

forms to be an alternative for the employees. In the Hungarian context, , flexicurity means a particular, country-specific social and labour market model and strategy. One of the elements of this is the nature of the labour law regulation in which reaching the balance of flexibility and security is the most important issue. The balance is such an intensive legal guarantee in the relationship that is still motivating for the employer, who requires flexibility, to keep the certain legal relationship within the frames of labour law regulation.[2] This fragmentation strengthened when that legal institutions not regulated by the Labour Act started to play a more and more significant role.

The change of these contractual relations also influences the changes of the labour market. There is a tendency that the new working forms make their own ways without obstacles as a part of our everyday legal relations. The constant change forms those frame systems which are finally adopted. The changes of labour markets are also influenced by economic processes which are involved in social innovation. . In the following, I would like to examine the definition of social innovation in the context of new employment forms and I would like to show their common effect in the topic of social security.

The centre of the research is the changes of the labour market. Labour market is a continuously changing milieu, which always has to adjust its tools to some kind of new life situations. Two labour market changes were examined in the research. One of the examined phenomena was digitalization, the other was robotization. Both changes create such new situations when the traditional labour market and labour law tools will not be effective. Digitalization and robotization are the two newest challenges of the world of labour. However, these two challenges partly cohere. Digitalization primarily means work on on-line surfaces, platform work and work-on-demand via apps. Robotization means that some parts of the human work can be substituted by robots. We are talking about two different ways of labour law and employment, which can meet even where the employee who lost his job because of robots will or must occur as a character of gig economy. Both topics have a significant role regarding the future. These factors will determine the labour market of the present and the future, as well. These labour market changes will influence the financing and the use of supplies of the social care system.

## 2. Social innovation and labour market changes

The term innovation is usually interpreted primarily in economic, technical, technological, organizational, etc. fields. Innovation is primarily associated with its economic effects.[3] The characteristics determining innovation are also primarily connected to these fields:

- Novelty, relative novelty, original or originated solution, recognition, elaboration and formulation of new combination of factors,
- Utilization of recognitions,
- As a result of these, improving result, efficiency, welfare or other measurable,

[2] Jakab Nóra: Gondolatok a rugalmasság és biztonság egyensúlyáról Prugberger Tamás 80. születésnapja alkalmából, *"Miskolci Jogi Szemle"* 2017 2. special issue (különszám), 217; D. A. MÁTÉ : A munkaidő szervezése és a munkamorál összefüggései, *"Miskolc Jogtudó"* 1/2018, 3.;

Jakab Nóra – Tóth Hilda: *Flexicurity in Hungary from the more Vulnerable Party"s Point of View* In: 5th International Multidisciplinary Scientific Conference on Social Sciences and Arts SGEM 2018. STEF92 Technology Ltd., 2018 Issue 1.1., Modern Science, Political Sciences, Law, Finance, International Relations, 153-160.

[3] Angyal Ádám: Az innováció társadalmi kockázatai, in: *Mérleg és kihívások* 136.

evaluable and sustainable favourable effects, namely development.[4]

However, the definition of innovation can be expanded for those life situations which happen in the everyday society. Research for innovations or new and effective solutions is not only the characteristic of technical sciences, but it is also a demand on social levels. Social innovation does not have a unified definition. The differences among the interpretation frames can be found in the interpretation of welfare and the novel solutions given for social problems.[5] Most of the theories agree, however, that the aims are the reform of the operation and existence of the society and the improvement of the welfare of the affected people in certain social conditions.[6]

Based on the above, according to one of the most generally accepted definition, social innovation gives new or novel answers for a community"s problems with the aim of increasing the welfare of the community.[7] Therefore, social innovation can be approached from the side of individuals and groups to be supported. On the one hand, social innovation is searching solutions for people"s old and continuously upcoming problems, on the other hand, it tries to find solutions for the new life situations. New life situations never occur as lacking any basis, but they always develop from a classical life situation.

## 3. Effects of digitalization - employment forms of gig economy

The on-line space provides numerous opportunities for the users. It has become such a platform where a wide range of services changes hands. Labour force also belongs to these services. Changed social and consumer demands have created such working processes which can primarily be found in the digital world. For now, mainly classical employment forms are dominating across Europe, although, not as significantly as earlier. The reason is that these employment forms have not spread in the East-European states significantly.[8] Parallelly, it can be stated that a continuous increase can be experienced in those labour segments which are related to digitalization. Conditions of classic work cannot be enforced in this changed environment. The so-called "gig economy" differs from the classical labour market solutions in its most important characteristics. Differences can be recognized mostly in the applied tools, the working hours and the regularity. Based on these, labour relationships of gig economy mean several single (casual) jobs to maintain himself. Here we can primarily talk about self-employers and freelancers who make a contract for a certain task. In a lot of cases, specialists or people working in the creative sector accept jobs in these ways.[9] If we start from the definition of social innovation, the employment form created by gig economy can be considered to be such a solution

[4] idem

[5] Kocziszky György – Veresné Somos Mariann – Balaton Károly: A társadalmi innováció vizsgálatának tapasztalatai és fejlesztési lehetőségei, "*Vezetéstudomány"* 6-7/2017, 16.

[6] ANGYAL: Az innováció társadalmi kockázatai op. cit. 137.

[7] Kocziszky- Veresné- Balaton: A társadalmi innováció vizsgálatának tapasztalatai és fejlesztési lehetőségei op cit. 16.

[8] Tóth Hilda: A munkajog új kihívásai:A "GIG" gazdaság munkavállalói csoportjai, In: Szikora Veronika (editor), Török Éva (editor): *Ünnepi tanulmányok Csécsy György 65. születésnapja tiszteletére* II. kötet, Debreceni Egyetem Állam- és Jogtudományi Kar, Debrecen, 2017. 381.

[9] Malcoln Sargeant: The Gig Economy and the Future of Work, in: *E-Journal of International and Comparative Labour Studies* 2/2017, 2.

which gives novel answers for the challenges of the labour market. These employment forms can become (are becoming) quite popular primarily in the case of the Y generation, since they spend a significant part of their every-days on on-line surfaces. One key moment of gig economy is sharing.[10] The essence of this is that unutilized resources should be used in a new way. This new way materializes by providing services which are sold on the on-line market. One part of the services is the so-called crowd work, the other is the work-on-demand via apps.

### 3.1. Crowd work

Crowd work means work done in the framework of crowdsourcing. Crowdsourcing means the activity when a company or organization outsources a function having previously been done by its employees to a not precisely defined (usually big) group in the form of an open appeal.[11] Personal work is of course possible in this form, as well, , however, group work is more common. In this solution, working processes take place totally in the on-line space, including the transfer of the outcome, , too. In this case, sharing means dividing working processes among people with whom the costumer will never meet, though the established contact system does not require it, either.[12] The aim is to complete the jobs fast and effectively. Moreover, the parties leave their own local zone and enter the virtual space, thus the labour market becomes wider for them and it is necessary that they shall exceed the local level.

### 3.2. Work-on-demand via apps

Work-on-demand via apps is another significant employment platform of gig economy. Usually work in its traditional sense takes place in this case. The digital market has a significant role in transacting business between the costumer and the service provider. The interpretation of sharing mentioned above, which is based on the optimal utilization of the tools, comes into view in this regard. Numerous services can be ordered via applications, from taxi to food delivery. The innovation in this is that on-line platforms connect the demands with the offers via applications.. The market participants are brought closer to each other. A lot of big companies are built on this basis with thousands or millions of users.[13]

Work-on-demand via apps also means a significant amount of freedom for working people, since it helps connect people who could not be its members otherwise to the labour market . In addition to the fact that it is capable of involving inactive layers of workers, it is also necessary to highlight its flexibility. Contacting via applications supposes a new kind of communication practice, as well. Thus, work-on-demand via apps uses new solutions not only in the field of employment, but also in the field of communication. The new solutions have, of course, advantages and disadvantages, too.

One of the advantages is the flexibility which is excessively important in the present situation of the labour market. It should be added that flexibility itself is not enough. Innovation will only be complete in these legal relations if security also gets a role in them. Here, security primarily means the

[10] Rácz Ildikó: Munkavállaló vagy nem munkavállaló? A gig-economy főbb munkajogi dilemmái, "*Pécsi Munkajogi Közlemények"* 1/2017, 82.

[11] Tóth: A munkajog új kihívásai op cit. 386.

[12] Tóth Hilda: A változó munkajogi környezet hatása az innovációra. „*Miskolci Jogi Szemle"*, 2/2018

[13]The most famous global company is the group of UBER which deals with passenger transport in an organized way. All so that the offically registered activity of the company is IT service provider. The company tries to open this contradiction with the general argument that it only provides the surface for the parties to find each other.

security of the employee. Namely, the new solutions in labour law mean cases moved toward civil law. Hereby I am are just referring to it since it will be explained in detail later that all innovations have losers who are needed at least to be compensated. In the case of new flexible employment forms, it should always be considered in the background of the innovation that the employee should always be able to exercise his rights properly, so the person can enforce the security rules as well.[14] In certain cases, work like this can provide higher earnings opportunities for the service provider party. Although some fortune is also needed and it is the privilege of only a few. These working forms are characterised by very low wages.. Financially, the so-called digital nomads working in this field are extremely vulnerable.[15] Digital platforms often function as online candy shops since they keep the wages of workers so low that such wages do not reach the minimum wage in most cases, either. This latter is in connection with the fact that the operator can count on low costs.

Some negative effects have been examined in the context of advantages, but far not all of them. Another further issue is the examination of responsibility. Similarly to self-employed people, bearing damages remains totally on the side of the employee. The service provider will bear its damages itself.

### 3.3. The connection between social security and gig economy

Another important issue of our study is that the expenditures in connection with social security are borne exclusively by the employees when the employee is not able to work due to a disturbance or change in his life situation. This partly answers the question how the service provider will be entitled to certain social or social insurance benefits in the case of the new employment forms. This issue arises because employment in the framework of gig economy is not of labour law nature. The origin of this point of view is that according to the statements of the companies operating the applications, they just provide the platform where the two parties can meet, moreover, they are all registered as IT service provider companies. If we add the access to social benefits to the nature of the gig economy that typically only casual work takes place , it can raise concerns. Based on this concept, there may be numerous employees in the future whose social insurance status will be uncertain, and lots of people cannot become entitled to social benefits. Although the new employment form having been analysed so far means social innovation in the labour market, it will have negative effects regarding social security. The social insurance rules will be unable to follow the changes at the same pace as the changes of employment conditions occur. And besides , as it has already been mentioned, the service provider bears all the risks alone. The state will not give help in such a form as it would in the case of an employee.

There is another problem as far as casual work is concerned. Irregular income makes it hard to become a member of full value of the risk community from which the benefits and different health care benefits are given. When we analyse the situation of

[14] Jakab: op cit. 214.; Jakab Nóra: Systematic thinking on employee status, *Lex et Sciencia* 2/2018; a the changing of the protection level see more: Jakab Nóra – Szekeres Bernadett: A személyi és/vagy gazdasági függésben munkavégzőkre vonatkozó felelősségi szabályok a német és magyar jogban, "*Publicationes Universitatis Miskolciensis Series Juridica et Politica* " XXXV/2017. 266-284.

[15] See it in more details through case studies in: B. Y. THOMPSON: Digital Nomads: Employment in the online gig economy, in: *GLOCALISM – "Journal of the culture, politics and innovations"*, 1/2018/ 13.

these employees not only in the short, but also in the long run, it does not promise too much, either. It is because even life-end benefits are supply forms bound to prior insurance time. Although, as an entrepreneur or a self-employed person, the persons analysed belong to the category of the insured, due to the irregularity of the income and the sequential casual jobs it seems to be impossible to gain entitlement to such benefits as pension. It is more possible to become entitled to benefits bound to shorter prior term of insurance. If social security systems do not follow the changes of the labour market, it will cause enormous gaps between employees in the classical sense and workers choosing the new employment forms.

The problem is perceived, even if only indirectly, by the legislator, as well. Namely, the examined new employment forms raise several questions. One of these questions is whether work-on-demands via apps can only be imagined as being self-employed. Does the provider company really give only the platform? The answer for this is quite complex. On the one hand, it is worth examining the requirement system of service providers from the aspect that who they would like to work with. In her thorough study cited earlier, Hilda Toth introduces some companies operating such applications which define precisely (like an employer) their employing conditions.[16] In these cases the question may arise by rights that what kind of legal relationship is between the application operating company and the service provider employee. The answer for this question has serious effects on how the employee can exercise his right to social security. Namely, if the application provider company is considered to be an employer, the contact system between the employee and the operator of the on-line platform should be interpreted differently. To clear the situation, the case No C-434/15. of the Court of the European Union , named Asociación Profesional Elite Taxi kontra Uber Systems Spain SL helps us.[17] In the examined case the legal issue was that whether the services provided by the Uber can be regarded as transport services, services connected to the IT society or the combination of these two service types. "What is Uber in fact? A taxi company? Or an electronic platform that can make it possible to find, book and pay for a transport service provided by someone else?" According to the Court Uber is not just a simple mediator between drivers ready to provide casual transport services and passengers looking for such services. On the contrary, Uber is the real organizer and operator of urban transport services in those cities where it is present. So, the service of connecting passengers and drivers is neither independent nor of primary nature as compared to transport services, and therefore it cannot be considered as a "service in association with the IT society".[18] The decision"s effect on the labour law is that if the work relations of Uber drivers are regarded as employment, people employed in the form of work-on-demand via apps have more chances to reach a similar protection level as normal employees have. The decision may be a reference in all similar cases of course without the modification of labour law regulations.

[16] Tóth Hilda: A munkajog új kihívásai op cit 386.

[17] Az ügy teljes elemzését lásd: Gyulavári Tamás: Az Európai Bíróság és a gordiuszi csomó: az Uber applikáció vagy taxitársaság?, *"Munkajog"* 3/2018 8-12.; Jeremias Prassl: Uber: the Future of Work… Or Just Another Taxi Company?, in: https://www.law.ox.ac.uk/business-law-blog/blog/2017/05/uber-future-work…-or-just-another-taxi-company, (2018. 09. 23.)

[18] Opinion of the Advocate General 71.

## 4. Robotization as social innovation in employment

The idea of using robots for work is not a new thing. In the beginnings, it was common only in sci-fi novels, but it has become more and more real in practice. Mass use of robots is not far. Robot labour force has been working at the production lines of certain factories. The fact that it is a part of our every-days is well-shown by the news informing us that one of the restaurants in Győr has set a robot waiter about work. The owner invested in such a tool because of the lack of labour, though he is planning to set more robots into service.[19] Despite the fact that the idea of using robots is not new, it falls within the range of social innovation. It means a new phase in substituting manpower by machines. The aim of using robots is not just their suppor of human work or simply their function to take over humans" tasks. According to Jozsef Hajdu, the new element of using robotics is the substitution of labour shortage occurring in certain sectors.[20] Moreover, using robots means a cheaper alternative for the loss of workforces.[21] The question is not the use of robots in the future, but the extent of their use. According to surveys, robots could substitute for 12% of the Hungarian employees even at the moment.[22] Some news say that there is a Chinese company that has substituted for the workplaces of 650 employees by 60 robots.[23]

In the earlier chapter, in the case of gig economy, it was also necessary to examine the background of the social innovation. In the case of the analysis performed within the range of the social innovation, it was necessary to examine its negative effects and its connection with the right to social security, too. The advantage and disadvantage of robotization are the same: it liberates human manpower. It can be regarded as an advantage, because its aim is not only the general liberation of men, but also the substitution for labour shortage. Robotization, however, by becoming common, will affect the labour market. The costs of maintaining and operating robots are lower than the costs of an average worker. Robots can primarily take over the labour at the production lines.[24] The professional debate is not about whether the human labour force will be substituted for or not, but about its extent. This professional discussion is influenced by the recommendation of the European Parliament to the Committee concerning civil law regulations on robotics I, J and K points of the introduction to the recommendation deal with the effects on the labour market. Similarly to the above mentioned, the cited document also acknowledges that though robotics offers indisputable advantages, its use may transform the labour market and can make it necessary to think over the future of educational, employment and social policies appropriately. The advantages and disadvantages of the labour market, which will probably occur or have already occurred, are connected to this idea. According to the document, it is an

[19] Robotpincér viszi ki az ételt egy győri kínaiban, in: https://hvg.hu/kkv/20180912_Robotpincer_viszi_ki_az_etelt_egy_gyori_kinaiban, (2018. 09. 23.)

[20] Hajdu József: A munkavégzés jövője: A robotika forradalmának hatása a munkaerőpiacra, in: Gellén Klára (editor): Jog, innováció, versenyképesség, Wolters Kluwer, Budapest, 51.

[21] Kis Miklós: A jövő osztályharca, in: http://ujegyenloseg.hu/a-jovo-osztalyharca/, (2018. 09. 23.)

[22] Hajdu József: A munkavégzés jövője op. cit.52.

[23] Meixner Zoltán: Digitális hejehuja! És az állásunkkal mi lesz?, in: http://ujegyenloseg.hu/digitalis-hejehuja-es-az-allasunkkal-mi-lesz-2/, (2018. 09. 23.)

[24] Retteghetnek a szalag mellett dolgozó munkások az Epson új robotjától, in: https://sg.hu/cikkek/it-tech/131928/retteghetnek-a-szalag-mellett-dolgozo-munkasok-az-epson-uj-robotjatol, (2018. 09. 24.)

advantage that employees will even be able to work in more creative fields in the future instead of doing their monotone jobs. By the recommendation, the widely spread use of robots does not lead automatically to the substitution of manpower, but jobs requiring lower education in labour-intensive sectors will probably be more exposed to the danger of automation, since this trend can bring production processes back to the Union. Research has indicated that employment grows significantly faster in jobs using more computers, since the automation of work creates opportunities for people doing monotone work to change to more creative and meaningful tasks. The proper implementation of this can happen if the state invests in it in an appropriate way. Automation requires governmental investments in education and other reforms in order to foster the development of those capabilities which the employees of the future will need.

Of course, the recommendation has realized its dangers, as well. Since robotics and the development of artificial intelligence can result in robots" taking over the work presently performed by humans. Meanwhile lost workplaces are not substituted totally, which can raise concerns about the future of employment, the viability of social welfare and security systems and the continuous differences in pension contributions. If taxation continues to operate on the current basis and the inequality in the distribution of goods and influence may be increasing, in order to retain social cohesion and welfare, the possibility whether a tax shall be levied on work performed by robots or the use and maintenance of the robots shall be bound to payment should be examined in connection with the support and the funding of retraining the employees whose employment has decreased or been terminated.

### 4.1. The relationship between robotization and social security

As the text of the recommendation cited above shows, setting masses of robots about work will have significant effects on the maintenance of social security systems. According to the data cited earlier in this study, robots could substitute for 12% of the Hungarian labour force at the moment. Primarily, the work of employees of the assembly industry is in danger. If we look at this tendency in general, it can be said that the change of the labour market will be realized not only in the disappearing occupations and cessation of workplaces , but new occupations and jobs will also be created. The basic question is, however, that how the right to social security will be realized in the cases of the employees in the transitional periods. How will the worker be entitled to benefits whose legal relationship terminates because of setting a machine about work? The dismissed worker has to acquire new knowledge to become an active participant of the labour market again. In the possession of this new knowledge, he can be able to get a new job and participate in the state"s risk community system. Of course, working-out of the solution is not only the state"s, but also the concerned parties", that is the employer"s and the employee"s task. Such legal institutions and solutions as outplacement[25] and CSR[26] will be appreciated more at this point.

[25]Henczi Lajos: Outplacement, mint szociális gyakorlóterep, *„Munkaügyi Szemle"* 5/2002, pp. 21-25.; Hiezl Tamás: Az outplacement mint humánpolitikai eszköz, *„Munkaügyi Szemle"* 6/2000, pp. 14-17.

[26] Horváth Dóra Diána: The Connection Between Innovation and Corporate Social Responsibility

In: Gazdócziné Fekete Éva (editor) *Doktoranduszok Fóruma: Gazdaságtudományi Kar szekciókiadványa*. 2016., 18-23.;Szegedi Krisztina – Mélypataki Gábor: A vállalati társadalmi felelősségvállalás (CSR) és a jog kapcsolata, "*Miskolci Jogi"* 2016/1, pp. 51-70.

Social measures realizing in the framework of outplacement and CSR should be primarily done by the employers. But the state cannot stay passive, since it will be necessary to rethink its social care system. Simplifying the processes, in the current system one part of the social care system is financed by the employees and the employers and the state adds to this. Employees who lose their jobs because of robotization fall out of the financing of the system, since it is them who need support in some ways. The employer does not pay salary to the the worker dismissed, so these contributions will also fall out , and the state would remain the only funding party of the system. This would mean a significant decrease of the protection level. The demand of the employers" contribution to the maintenance of the system in case of employing robots is defined in the recommendation of the European Parliament cited earlier. The consequences cannot be defined clearly at this moment. One endpoint of the scale is that it will be better for everyone, the other is massive unemployment.[27] It will happen in any forms, it will affect the employee"s destiny. In connection with this, the idea of compensating[28] the negative social political effects of robotization by introducing basic income[29] has come up in scientific and business circles, too . Most generally, basic income occurs as a particular benefit form from which everybody can receive automatically. Basic income is the topic of continuous debates. Basic income means a regular income for individuals jointly and severally, without conditions, independently from other ones. It is such an income resource that seems to be a simple idea to create social security. It does not have a unified definition; certain definitions of it are usually collections of different ideas with contradictory goals. The sum (total or partial) of the basic income, the tax model established for its funding (budget neutral vs re-distributional) and the exchangeable social insurance regulations by the new social rules define its effects.[30] Supporters of the idea define the regular monthly sum received in the form of basic income not only as a simple wage, but also as a social benefit. This element of its makes it more attractive. This perception is well-illustrated by a Hungarian experiment in which the group called LÉT defined how basic income could be adapted to the Hungarian conditions. Creators of the conception started from the hypothesis that in the Hungarian system a significant part of aid items and social benefits would become unnecessary upon introducing basic income. In the study the authors explicitly state that family allowance, family tax benefit and several other child supports would be ceased because of the basic income, which would be higher than family allowance. Pregnant women would get an allowance which is one and a half times more than the basic income, and as a result benefits, which are lower than this amount would also be ceased. Just a few targeted financial benefits would remain in the system., The system would primarily keep the benefits which are for solving

[27] Ville Veilko Pulkka: A free lunch with robots – can a basic income stabilise the digital economy?, *"Transfer"* 3/2017, p. 296.

[28] Benjamin Kentish: Richard Branson calls for universal basic income because robots are taking people"s jobs, in: https://www.independent.co.uk/news/business/news/richard-branson-universal-basic-income-robots-taking-jobs-automation-threat-a7993006.html, (2018. 09. 24.)

[29] Basic income: "Basic income is such an income which is provided by a political community for all of its members on personal basis, indipendently from financial situation and without work obligations." See it in details: PARIJ"S: Alapjövedelem: egy egyszerű és erőteljes gondolat a huszonegyedik század számára, "Esély" 5/2010

[30] Pulkka: A free lunch with robots – can a basic income stabilise the digital economy?, op cit. p. 301.

crises or relieving unique problems.[31] In the latter cases , analysing tests would be introduced, which would bind payments above the basic income to conditions. If we relate these ideas to the topic of robotization, it can be seen that the formation of a new type of social protection net is planned by this income. Employees dismissed because of robots should not worry about their livelihood, since they would have income during the transitional periods, as well, until they can become active participants of the labour market again.

## 5. Summary in the mirror of life-long learning

It is sure that the meaning and the content of the right to social security will change. The way of it cannot be explained exactly since it will be the result of such a process the end of which cannot be seen yet. It is not sure whether basic income will be the future or not. There is some micro-researches in connection with basic income, but the results of them cannot be adapted to social conditions yet.[32] Social security is a complex legal institution, which is influenced by the changes of the society and particularly those of the labour market. Accordingly, social innovation occurring in the employment sector will also have an influence on the changes of the labour market. New employment forms set up different challenges for individuals and the society. Gig economy and robotization will affect the social care system and will force it to transform at the same time. Life-long learning means the continuity in the maintenance of the right to social security. The people who continuously adapt to the situation and own proper knowledge and competences will be able to remain active in the labour market and ensure social security for themselves continuously.[33] Highlighting this is important because besides the guidelines analysed above it should be mentioned that human capital gets a central role in today"s labour law thinking. Therefore it is worth paying attention to one of its main pillar, that is life-long learning. Supporting life-long learning is one of the key factors for employees to be able to keep their right to social security, while the definition of which is continuously changing. The employer and the state should be supporting as far as the support of learning is concerned, and the employee should be receptive. The continuous up-to-date knowledge is what - although will never solve the outlined problems - will ease to bridge over them and may have a significant role in minimalizing losses.

The aim of the study was to outline what kind of tendencies can be expected in the labour market and how they will influence social security. The right to social security is a right that we must protect in the changes of the labour market since it was not easy to acquire it. This helped the employees to act as independent participants against the employer and, if it is necessary, the state, as well. This right should be protected in the on-line space and against robots in the future. Continuous learning, development and the employees" adaptation to the new situation will have a significant role in this.

[31] "LÉT" 17. old.

[32] Pulkka: A free lunch with robots – can a basic income stabilise the digital economy?, op cit. p. 303.

[33] Kun Attila: Élethosszig tartó tanulást támogató nemzetközi munkajogi szabályozási tapasztalatok. A munkahelyi képzés szerepe az élethosszig tartó tanulásban, in: A. KUN (editor): *Az egész életen át tartó tanulás (lifelong learning) jogi keretei a munka világában, különös tekintettel a munkaviszonyra*, Károli Gáspár Református Egyetem Állam- és Jogtudományi Kar, Budapest, 2017, p. 17.

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# OLD PROBLEMS AND NEW SOLUTIONS? SOME CURRENT QUESTIONS OF LABOUR AND SOCIAL RIGHTS REGARDING THE EUROPEAN PILLAR OF SOCIAL RIGHTS AND THE ACTUAL CASE LAW OF THE COURT OF JUSTICE OF THE EUROPEAN UNION

**Márton Leó ZACCARIA***

**Abstract**

*The present paper analyses some current issues of the social policy of the European Union (EU). Employment policy is also present in the research but both aspects are focused around the labour and social rights that workers are entitled to. The methodology is both based on the hypothetical context and the relevant case law of the Court of Justice of the European Union (CJEU). The paper examines the relevant issues regarding the fundamental social rights in EU law and the latest steps of their development materialised in the European Pillar of Social Rights (EPSR). The relevant connection between the already existing labour and social rights and their regulation and the reforms of the EPSR is emphasised – among others – with the help of the Charter of Fundamental Rights of the European Union (CFREU). The analysis of some current judgments of the CJEU show the contradictions and questions regarding the social and the economic approach but both need to be considered regarding the changing environment in the labour market. That is the main reason the paper aims to conclude some ideas concerning the recent past and the future of these rights and regulations in EU law. The focus is on the EPSR and the practical approach of the CJEU"s case law in the context of labour and social rights in EU law.*

**Keywords:** *EU law, EU social policy, European Pillar of Social Rights, social protection, workers" rights.*

## 1. Introduction

The researcher who examines changes in labour law, which – according to a narrow interpretation – covers the rights of workers, the new directions of legal protection, and in general, the current stage of fundamental values, which traditionally ensure the essence of employment regulation within the framework of the social rule of law,[1] is in a difficult situation. Furthermore, the planned research definitely focuses on European Union (hereinafter: EU) law, its labour and social law acquis, and so we can expect to meet more questions than exact answers, since "EU labour law" itself has been experiencing an important transformation over a longer period of time.[2] As a result, we

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[1] György Kiss, *Munkajog*, Osiris Kiadó, Budapest, 2005, p. 211-213.

[2] Zane Rasnača, "*Bridging the gaps or falling short? The European Pillar of Social Rights and what it can bring to EU-level policymaking"*, published in *"European Trade Union Institute – Working Paper"*, Issue 5, (2017), p. 4, 8-9. and 19-20; this document is available online at: https://www.etui.org/Publications2/Working-Papers/Bridging-

can say with good reason that the EU social and employment policy is experiencing "interesting times"[3] heading towards the common social policy.[4] Taking into consideration all the above I think that with the method of research in such task we can examine the usual, generally used, even traditional values of labour law in order to put them into the context of the present or even future system. It is useful from the viewpoint of the level of both the regulation and the legal practice and can lead to further results for consideration.[5]

In the present paper I undertake this task: as an important component of a larger research topic[6] I sketch out some sore points on the basis of the present state of EU law which definitely influence and form the present and future of the protection of the employees; what is more, I am trying to give a general picture of the method of considering and reflecting on the raised issues. However, I have already referred to fundamental labour law rules being seriously changed in the following years,[7] and the already achieved results cannot be left without attention. However, I think that the main starting point of this study must be the norms in force now, but through a segment of the actual legal practice of the Court of Justice of the European Union (hereinafter: CJEU) the current content keystones of the above mentioned values that are general and transforming at the same time also can be observed. On the following pages the greater subjects of the chapters are linked to each other without exception, however, the relationship can be simplified to general questions of social policy and labour law, but I think that these current issues truly reflect the basic rights of the "worker" status and the level of their guarantee.[8]

The above mentioned difficulties and contradictions are proved by the subjects processed in detail below, since regarding the legal protection of the employees to discuss such questions of fundamental right, case law and questions of which one part exists only as proposals and concepts is very important. Naturally, to make a single system regarding the mainly different fields of labour law is difficult, but in my opinion this multi-layering issue represents the (potential) socio-political changes

the-gaps-or-falling-short-The-European-Pillar-of-Social-Rights-and-what-it-can-bring-to-EU-level-policymaking (last access: 02.09.2019).

[3] Frank Hendrickx, "*Editorial: The European pillar of social rights: Interesting times ahead"*, *European Labour Law Journal*, Vol. 8. Issue 3, (2017), p. 192.

[4] Rolf Birk, *Általános áttekintés*, in: György Kiss, *Az Európai Unió munkajoga*, Osiris Kiadó, Budapest, 2003, p. 19-22.

[5] Regarding this part of the research see in details: Márton Leó Zaccaria, "*A 91/533/EGK irányelv reformja – elméleti megfontolások és európai bírósági tanulságok"*, *Közjogi Szemle*, Vol. 12. Issue 1, (2019), p. 59-68.

[6] The aim of the indicated research is the thematic analysis of the actual state of the most significant areas of the legal (social) protection of the workers in Hungarian and EU law.

[7] The already accepted laws of the reform under the flag of the European Pillar of Social Rights are the following: Directive (EU) 2019/1158 of the European Parliament and of the Council of 20 June 2019 on work-life balance for parents and carers and repealing Council Directive 2010/18/EU, Directive (EU) 2019/1152 of the European Parliament and of the Council of 20 June 2019 on transparent and predictable working conditions in the European Union, Regulation (EU) 2019/1149 of the European Parliament and of the Council of 20 June 2019 establishing a European Labour Authority and Directive (EU) 2018/957 of the European Parliament and of the Council of 28 June 2018 amending Directive 96/71/EC concerning the posting of workers in the framework of the provision of services.

[8] Here I only refer to that clarification on the concept of "employee" requires another research, but in the present study I use the broadening interpretation made by the Court, refraining from mentioning the differences between basic dogmatism and the regulation of the Member States. See in: Martin Risak and Thomas Dullinger, *The concept of „worker" in EU law. Status quo and potential for change (Report 140)*, ETUI aisbl, Brussels, 2018, p. 18. and 40-41.; this document is available online at: https://www.etui.org/Publications2/Reports/The-concept-of-worker-in-EU-law-status-quo-and-potential-for-change (last access: 28.10.2019).

emphasizing such regulative questions of labour law which in given cases also can be on the agenda in the member states (e.g. issues of working time or social security). Altogether, the present, non-exhaustive research provides a snapshot of the above actual questions of labour law and looks to the future in order to make the particular legislative processes more transparent, and consequently, the questions raised are answered.

## 2. The role of ”solidarity” rights in the legal protection of workers

The function of the Charter of Fundamental Rights of the EU (hereinafter: CFREU) and its real legal strength is not a new question regarding the legal protection of employees,[9] that is, to the question whether the reference to the fundamental rights law laid down in the CFREU can ensure real and effective legal protection to the workers, is ”no”.[10] However, it is important to add that this negative answer on the one hand does not result in the rights laid down in Chapter IV of the CFREU being worthless, which cannot be used in practice, and on the other hand, it would not be correct to think that the changing case law of the CJEU could not lead to new directions of legal interpretation. Furthermore, the CFREU and the European Pillar of Social Rights (hereinafter: EPSR) do not have direct theoretical or legislative connection to each other, but it is possible that the protection of fundamental social rights laid down in the CFREU can get a new interpretation in relation to the constant development of the EPSR.[11]

In my opinion, the above-mentioned Chapter IV of the CFREU – entitled Solidarity – can be interpreted from two aspects regarding the legal protection of workers. Firstly, I mention the “material” legal side, that is, the rights summed up in the CFREU make such a new unconventional catalogue that is unprecedented regarding the protection of employees in the history of EU law,[12] and the importance of which cannot be questioned even referring to the limited applicability of the CFREU.[13] It is important to add that to elevate the most important rights of the employees – or at least the majority of them – to the level of fundamental rights was such an important step in developing social protection which has its effect on legislature even to this day,

[9] See: Sara Iglesias Sánchez, *“The Court and the Charter: The Impact of the Entry into Force of the Lisbon Treaty on the ECJ”s Approach to Fundamental Rights”, Common Market Law Review*, Vol. 49. Issue 5, (2012), p. 2565-2611.; Veronica Papa, *“The Dark Side of Fundamental Rights Adjudication? The Court, the Charter and the Asymmetric Interpretation of Fundamental Rights in the AMS Case and Beyond”, “European Labour Law Journal”*, Vol. 6. Issue 3, (2015), p. 190-199. and Massimiliano Delfino, *“The Court and the Charter – A “Consistent” Interpretation of Fundamental Social Rights and Principles”, European Labour Law Journal*, Vol. 6. Issue 1, (2015), pp. 86-99.

[10] Brian Bercusson, *“Horizontal” Provisions – Title VII General Provisions Governing the Interpretation and Application of the Charter (Articles 51-54)*, in: Brian Bercusson (ed.), *European Labour Law and the EU Charter of Fundamental Rights*, Nomos Verlag, Baden-Baden, 2006, pp. 404-414.

[11] See for example, article 30 of the CFREU that ensures protection for the workers against unjustified dismissal. In labour law, the question of the protection against unfair dismissal is such a typical and important field that it would be wise to emphasise its harmonization in the sphere of problems of labour market and social questions, which the EPSR attend to.

[12] It is necessary to mention the legal charter of the employees of 1989 (Community Charter of the Fundamental Social Rights of Workers) which is of high importance but it never entered into force, and regarding its legal nature and content it cannot be regarded equal to the CFREU in force, but it has become a proper theoretical ground for the legal protection of workers EU law.

[13] CFREU, articles pp.52-53.

since the comprehensive endeavours of the EPSR, which inspire real changes, also refer to them. According to my opinion, the rights of ”solidarity” try to compensate the deficiencies of EU law – even if on a theoretical level – that regards the employees as actors of the single market like providers of services but not people with social rights, there were possibilities for the protection of the rights of the employees between these extremities. Consequently, summing up these rights, elevating them to the level of the catalogue of fundamental rights, and clearing up their content have a great effect on the legal status of the employees, and I think, although this progress is complicated, that several solutions in the case law of the CJEU can be regarded consistent.

## 3. Fundamental labour and social rights in motion – recent examples from the case law of the CJEU

The other approach to the rights in the CFREU is the ”action” side, about which it is rather difficult to define in a definitely positive manner, [14] It is a recurring question in the practice of the CJEU – it will be discussed in detail below – that is, how it is possible to refer directly to the CFREU before regarding the fundamental rights included in it.

This question mainly emerges in connection to those fundamental rights that are not connected to secondary legislation, since referring only to the CFREU effectively is not possible. However, a part of the fundamental labour and social rights in Chapter IV are such rights,[15] consequently, direct enforcement of these rights for the employees is difficult, and unproductive in most of the cases. This consideration is a pure result of the legal protective mechanism of the CFREU,[16] but in many cases, this situation makes legal interpretation – which would strengthen the legal protection of the employees – more difficult. In my opinion concerning this question, the legal practice of the CFREU is mainly uniform; however, we can see some actual examples where the CJEU seems to move forward from the above-mentioned crystallised legal practice.[17]

In the lack of CJEU”s detailed analysis,[18] I only refer to judgment no. C-574/16.[19] in which the guarantees of equal treatment of the CFREU are referred to when examining the different working conditions of workers with fixed-term employment relationships. The national court wanted to know in connection to the CFREU if the fixed-term employment relationship can be terminated in an unjustified way under different conditions, and could the fundamental rights of the CFREU ensure legal protection to the employees in the lack of the concrete order of Directive

[14] Bob Hepple, “Fundamental Social Rights since the Lisbon Treaty”, European Labour Law Journal, Vol. 2. Issue 2, (2011), pp. 152-154.

[15] A typical example of it is the right to protection against unjustified dismissal declared in article 30 of the CFREU, but the following, article 31 on the right to fair and just working conditions is not an example of that.

[16] CFREU, article 52 paragraph (5).

[17] It is worth mentioning point 47, 49-50 and 76-77 of judgment no. C-414/16. Vera Egenberger v Evangelisches Werk für Diakonie und Entwicklung e.V. [ECLI:EU:C:2018:257] of the CJEU announced on 17.04.2018, in which the CJEU stresses the fundamental right character of article 21 of the CFREU.

[18] The CJEU did not examine the question referred by the national court regarding article 20 and 21 of the CFREU, because based on the earlier questions it was unnecessary.

[19] Judgment no. C-574/16. Grupo Norte Facility SA v Angel Manuel Moreira Gómez [ECLI:EU:C:2018:390] of the CJEU announced on 05.06.2018.

1990/70/EC.[20] Finally, the opinion of the advocate general answered to the hypothetical question that the regulations referred to equal employment do not conclude that the different situations should be handled the same way[21] that ensures the content of article 20 and 21 of the CFREU, similarly to the earlier points. Importantly, Advocate General Kokott refers to the problem of horizontal direct effect of the CFREU as a highly debated question, but she does not offer any legal solution. At the same time, she mentions that the CJEU has examined this question several times,[22] and regarding that articles 20 and 21 of the CFREU neither can lead to any other result in the concrete case than the above-mentioned rule of the Directive, judging this question is irrelevant.

Judgment no. C-472/16.[23] is also worth mentioning, though the case does not exclusively deal with labour law, but regarding the interpretation of article 47 of the CFREU it is interesting. This article of the CFREU contains the right to effective legal remedy, and in the present case, a legal dilemma has emerged in connection to it because of the transfer of the given undertaking. It is a question in the case of collective redundancies which was due to the transfer of the economic unit regarding that the subject of collective labour law took legal initiative, whether the resolution has binding force for individual employees. This questioning is justified since the collective labour law subjectivity is not equal with the joint subjectivity of the individual employees, however, the employees" private autonomy is not restricted,[24] even if its intention is to make it possible for the employees to act in order to protect their interests.[25]

In wider sense, it is another question whether in case of a standoff from the legal debates of the individual employees as consequence of the performance of the collective labour law subject the national court has the right – while respecting the fundamental rights of the CFREU – to decide on the merit of legal debates referring to individual employees, too. The workers necessarily referred to – besides the CFREU – their rights insured in the relevant directive[26] directly,[27] but it is a question whether we can speak about res iudicata in case of the performance of the organization representing the employees, and if the answer is "yes" , whether it is a violation of

[20] Council Directive 1999/70/EC of 28 June 1999 concerning the framework agreement on fixed-term work concluded by ETUC, UNICE and CEEP.

[21] Point 81-84 of opinion of Advocate General Kokott in judgment no. C-574/16.

[22] These problems were highlighted mostly by the following cases: judgment no. C-144/04. Werner Mangold v Rüdiger Helm [EU:C:2005:709] of the CJEU announced on 22.11.2005 and judgment no. C-555/07. Seda Kücükdeveci v Swedex GmbH & Co. KG. [EU:C:2010:21] of the CJEU announced on 19.01.2010. See further judgments from the recent past: judgment no. C-282/10. Maribel Dominguez v Centre informatique du Centre Ouest Atlantique és Préfet de la région Centre [EU:C:2012:33] of the CJEU announced on 24.01.2012; judgment no. C-176/12. Association de médiation sociale v Union locale des syndicats CGT and Others [EU:C:2014:2] of the CJEU announced on 24.01.2015 and judgment no. C-441/14. Dansk Industri (DI), agissant pour Ajos A/S v Sucession Karsten Eigil Rasmussen [EU:C:2016:278] of the CJEU announced on 19.04.2016.

[23] Judgment no. C-472/16. Jorge Luís Colino Sigüenza v Ayuntamiento de Valladolid and Others [ECLI:EU:C:2018:646] of the CJEU announced on 16.04.2014.

[24] Kiss (2005), op. cit., pp. 313-314. and 325-326.

[25] Tamás Prugberger and György Nádas, *Európai és magyar összehasonlító munka- és közszolgálati jog*, Wolters Kluwer Hungary Kft., Budapest, 2014, pp. 506-507.

[26] Council Directive 2001/23/EC of 12 March 2001 on the approximation of the laws of the Member States relating to the safeguarding of employees" rights in the event of transfers of undertakings, businesses or parts of undertakings or businesses.

[27] Point 101 of opinion of Advocate General Tanchev in judgment no. C-472/16.

the fundamental right in the sense that these employees de facto cannot practice their right to the possibility of the legal remedy according to the Directive.

According to Advocate General Tanchev, "Article 47 of the CFREU is to be interpreted as not precluding national legislation which prohibits a court from ruling on the substance of the claims of an employee who challenges in an individual action his dismissal, as part of a collective dismissal, in order to defend the rights deriving from Directive 2001/23 and Council Directive 98/59/EC of 20 July 1998 on the approximation of the laws of the Member States relating to collective redundancies, where final judgment has already been given on the collective dismissal in proceedings to which the employee was unable to be a party, although the unions established in the undertaking and all the collective statutory representatives were or were able to be parties, where under the national law, the binding force of that collective judgment does not exceed the boundaries of the subject matter of the proceedings and that subject matter differs from the one at issue in the individual proceedings."[28] Consequently, the possibility of the presence of the organization of the employees in the proceeding before the competent court deciding on the legal debate expresses the legality of the domestic regulation, but locus standi of the workers cannot be restricted even in such cases if the legal debates have different objects, this way ensuring the above mentioned directive guarantees. I regard this case as important, since the basic question of the guarantee of the rights of the employees is their enforcement, mainly, if the given legal dispute is linked to fundamental rights.

The decision in the joint cases no. C-680/15. and C-681/15.[29] contain important statements in relation to article 16 of the CFREU. Since the Alemo Herron judgment[30] it is regarded as clear what kind of means of fundamental rights are available for the enterprises in such cases when the organizations of the employees "abusing" their rights ensured in article 28 of the CFREU[31] make such contract referring to article 3 of Directive 2001/23/EC from which the receiving party is left out.[32]

However, it is still a question whether EU law protects the right to collective bargaining without abusing article 16 of the CFREU if all social partners take part in this process. The CJEU states if according to the national law the parties agree before the transfer the effect of the collective agreement after the transfer as well as its possibilities of correction, these legal issues are protected by article 3 of the Directive and do not restrict disproportionately article 16. Apparently, the interests of the new employer can be abused, seemingly restricting the freedom of contract, but the essentialia negotii of the original collective agreement is not affected supposing that otherwise the negotiations are carried out legally. It is clear that article 16 of the CFREU is not abused in this case if the new employer has real legal possibility a posteriori to enter the negotiation or it is

[28] Point 3 of conclusions of the opinion of Advocate General Tanchev in judgment no. C-472/16.

[29] Judgment no. C-680/15. and no. C-681/15. Asklepios Kliniken Langen-Seligenstadt GmbH and Asklepios Dienstleistungsgesellschaft mbH v Ivan Felja and Vittoria Graf [ECLI:EU:C:2017:317] of the CJEU announced on 27.04.2017.

[30] Judgment no. C-426/11. Mark Alemo-Herron and Others v Parkwood Leisure Ltd [ECLI:EU:C:2013:521] of the CJEU announced on 18.07.2013.

[31] Right of collective bargaining and action.

[32] Gyula Berke, "*Az Európai Unió Alapjogi Chartájának alkalmazása munkajogi (szociálpolitikai) ügyekben"*, *HR & Munkajog*, Vol. 5. Issue 11, (2014), pp. 10-14.

possible to correct the conditions of the contract by mutual consent (at least to initiate modification).

The CJEU confirms in judgment no. C-174/16.[33] relating articles 23 and 33 of the CFREU the fundamental right character of gender equality,[34] especially, in the field of employment, referring textually to the right to parental leave as one of the solidarity rights. Although several regulations of the CFREU did not have basic importance in the decision of the basic case, in my opinion this kind of focus on one of the most important rights of workers have high importance from the viewpoint of legal protection.

Finally, it is worth mentioning judgment no. C-306/16.[35] in which important statements can be found in connection to article 31 of the CFREU. The right to fair and just working conditions can be regarded as one of the most fundamental rights of the employees,[36] considering that rules of – among other important ones – working time and rest periods belong to this article, the legal disputes in connection to them are usual and what is more, the interpretation of the regulations of the directives[37] are not always unambiguous. However, in the judgment, it would be unnecessary to make a decision about it, but the CFREU is a kind of reference to strengthen the norms of the directive in the present case in relation with the issue of the compulsory weekly rest period for the employees. Namely, the CJEU decided on the basis of Directive 2003/88/EC stating that the requirement is not that the 24-hour minimal weekly rest period without break should be issued to the employee at the latest time on the day right after six workdays running, but it is stated that it should be issued within each period of seven days.

At the same time, the CJEU interprets shortly paragraph (2) of article 31 of the CFREU referring to the Community Charter of the Fundamental Social Rights of Workers of 1989 and the European Social Charter as well as to the relevant directives.[38] In my opinion, it is important regarding the protection of workers" fundamental rights, since this way the CJEU strongly emphasises the real content of the given fundamental right even if without the regulations of the directive it would not establish an argument to protect the employees effectively.

Regarding the legal status of workers it is advisable to mention judgment no. C-190/16.[39] from the latest case law in which the CJEU makes important statements regarding articles 20, 21, and 15. In connection to the prohibition of age discrimination, the judgment states that the fundamental right to equal employment is a primary principle of EU law[40] emphasising that the content of the CFREU should be interpreted together with the regulations stated in the relevant directions. Concerning the fundamental freedom of right to work the CJEU examined in merit how the regulation

[33] Judgment no. C-174/16. H. v Land Berlin [ECLI:EU:C:2017:637] of the CJEU announced on 07.09.2017.

[34] Point 31-32 of judgment no. C-174/16.

[35] Jugdgment no. C-306/16. António Fernando Maio Marques da Rosa v Varzim Sol – Turismo, Jogo e Animação, SA [ECLI:EU:C:2017:844] of the CJEU announced on 09.11.2017.

[36] György Kiss, *Alapjogok kollíziója a munkajogban*, Justis, Pécs, 2010, pp. 229-231.

[37] See typically: Directive 2003/88/EC of the European Parliament and of the Council of 4 November 2003 concerning certain aspects of the organisation of working time and Council Directive 89/391/EEC of 12 June 1989 on the introduction of measures to encourage improvements in the safety and health of workers at work.

[38] Point 50 of judgment no. C-306/16.

[39] Judgment no. C-190/16. Werner Fries v Lufthansa CityLine GmbH [ECLI:EU:C:2017:513] of the CJEU announced on 05.07.2017.

[40] Point 29 of judgment no. C-190/16.

of a member state constrains it when over a certain age employment of pilots referring to public safety is prohibited in civil air transport.[41] On examining, the above-mentioned fundamental rights the CJEU took into consideration the aspects of labour market and in relation to legal constraint, the CJEU considered every option and examined how the essence of the basic law would be influenced, as well as how it would restrict the chances/possibilities of the group(s) of the employees in the labour market.

It can be stated that the CJEU – mainly in relation to article 15 of the CFREU – abstains from a broadening interpretation which would enforce the social interests of the employees and prefers emphasising the economic side of work and states that reasonable, proportional and justified restriction of fundamental rights included in the CFREU in given cases can solve the interests of the labour market. Besides, the real, essential examination of the content and restrictions of article 15 are missing from the judgment.

Besides the above-mentioned aspects, I would like to mention in short judgment no. C-482/16. of the CJEU[42] in which the CJEU refers to the connection between article 21 of the CFREU and article 45 of the Treaty on the Functioning of the European Union (hereinafter: TFEU), which is an important statement concerning the fundamental rights interpretation of the principle of equal treatment, but since it is not explained in merit, we can only conclude its importance. According to the decision the regulation which takes into account in a professional carrier the periods of paid work performed only after the age of 18,[43] is not contradictory to either the prohibition of age discrimination or to the fundamental freedom of free movement, this way those employees who have periods of paid work under 18 should be treated differently based on age. The regulation with retroactive effect deleted this restriction referring to every employee, but referred only to the given economic sector, this way the basic right of the employees is not injured.

Finally, I would like to mention judgment no. C-89/16.[44] in which referring to article 34 of the CFREU guaranteeing the fundamental right to social security the CJEU stated since in that case the object of the legal dispute was the application and interpretation of the social coordination regulation,[45] consequently, the main question is whether the application of the article 34 of the CFREU would conclude the rejection and restriction of the edictal regulations. According to the CJEU the answer is ”no”,[46] since the function of the coordination, among others, is to ensure this fundamental right laid down in the CFREU. It is – on the one hand – an important guarantee referring the movement of the employees between the member states, but in this regard, article 34 practically did not have role in the decision of the legal dispute, consequently, its analysis failed.

[41] Point 72-77 of judgment no. C-190/16.

[42] Judgment no. C-482/16. Georg Stollwitzer v ÖBB Personenverkehr AG [ECLI:EU:C:2018:180] of the CJEU announced on 14.03.2018.

[43] Conclusions of judgment no. C-482/16.

[44] Judgment no. C-89/16. Radosław Szoja v Sociálna poisťovňa and WEBUNG, s.r.o. [ECLI:EU:C:2017:538] of the CJEU announced on 13.07.2017.

[45] Regulation (EC) No 883/2004 of the European Parliament and of the Council of 29 April 2004 on the coordination of social security systems, pp. 1-43.

[46] Point 43 of judgment no. C-89/16.

## 4. The European Pillar of Social Rights as a potential major opener to improve labour and social rights

As I referred to the CFREU several times, though the – mainly principal – importance of the EPSR cannot be contested, but the difficulties of the present means of the social protection of workers can emerge exponentially in the future on the old-new fields affected by the EPSR. Naturally, the EPSR cannot take a change of workers" legal protection, but the general expectations[47] and the EPSR"s seriousness and volume of the political decision in the EU let us come to the conclusion that regarding the labour market and social questions important changes in employees" fundamental rights are expected. At present, it is uncertain whether these changes will appear on the level of legislation effectively or rather on the level of soft law, but we will see later that practically, on the level of legislation we can speak now about effective changes.

At the same time, it is worth reviewing in short the spirit and the potential role of the EPSR in EU social policy,[48] since stripped off the context one can come to false conclusion regarding its role performed in the employees" rights. Although the EPSR would change the image of several areas of social policy,[49] I think that its most important idea can be that it would not try to take a complete turnabout regarding the protection of the interests and the rights of the employees respected and guaranteed so far. What is more, practically it develops the achievements of social policy until now in a way, which can be remedy for the social crises and crises of the labour market[50] on EU level nowadays.[51] It cannot be left without attention that the present main challenges of EU are only partly of an economic nature, since social factors which will be required by the member states to pay attention to for the further development and stabilisation of EU are as important.[52]

It can be stated that the EPSR does not intend to settle concrete disputed matters exclusively in order to achieve the balance of the labour market – even if such intention also can be seen – it rather tries to find remedies comprehensively to enable the lagging sectors of the society to catch up to ensure equal possibilities or to guarantee a higher level of social rights.[53] Although, it is clear from the above listed aims that this holistic approach can result in the slow development of the EPSR, or in worse case, inefficiency, but I think that workers do not need more spectacular possibilities in order for their rights and legal protection to gain great legislative focus and political interest. Three key areas of the EPSR, which should

[47] Hendrickx (2017), op. cit., pp. 191-192.

[48] Klaus Lörcher and Isabelle Schömann, *The European pillar of social rights: critical legal analysis and proposals (Report 139)*, ETUI aisbl, Brussels, 2018, p. 5-7.; this document is available online at https://www.etui.org/Publications2/Reports/The-European-pillar-of-social-rights-critical-legal-analysis-and-proposals (last access: 28.10.2019).

[49] Zane Rasnača and Sotiria Theodoropoulou, *"Strengthening the EU"s social dimension: using the EMU to make the most out of the Social Pillar"*, *ETUI Policy Brief – European Economic, Employment and Social Policy*, Issue 5, (2017), p. 2-3; this document is available online at: https://www.etui.org/News/Using-the-EMU-to-make-the-most-out-of-the-Social-Pillar 2018 (last access: 29.10.2019).

[50] Lörcher and Schömann, op. cit., pp. 21-22.

[51] Hendrickx (2017), op. cit., p. 191.

[52] Frank Hendrickx, *"The European Social Pillar: A first evaluation"*, *European Labour Law Journal*, Vol. 7. Issue 1, (2018), pp. 5-6.

[53] *Reflection Paper on the Social Dimension of Europe*, COM(2017) 206 (26.04.2017), pp. 6-7., 12. and 21.; available online at: https://ec.europa.eu/commission/sites/beta-political/files/reflection-paper-social-dimension-europe_hu.pdf (last access: 29.10.2019).

be improved by the EU decision-making bodies in the following years, are to establish equal possibilities in the labour market, to address the social problems, and to develop the availability of just working conditions for every worker.[54] The latter should be emphasised, though the right to fair and just working conditions is an already crystallised fundamental right in article 31 of the CFREU, but its real essence and practical enforcement is still dubious. It should be added that referring to equality in the labour market and just working conditions the EPSR specifically mentions several more modern, complex forms of work of the 21st century.[55] These working activities formally do not necessarily match with the present conceptual structure of labour law, but they may have real importance in the labour market in the near future (platform work,[56] sharing economy,[57] etc.).

Altogether, the real complex approach concentrates not necessarily on the current social and labour market problems, and those problems being on the agenda from time to time,[58] but definitely designates new directions for the reality of the labour market and for the legal protective stability of the employees as a new requirement. The new directions are only partly new;[59] they can rather be defined as new, modern versions.[60]At this point it is worth wondering whether the twenty rights of the three key areas of the EPSR[61] can be regarded as a kind of legal catalogue of the real interests and rights[62] of workers, in other words, can the listed and supported areas be traced back to direct, real interests, labour and social rights.

Posing this hypothetical question is justified because the EPSR seems to be a declaration regarding its text, structure, content of preamble, and general nature,[63] which – because of its importance – designates serious and definite aims and concrete rights that can be referred to. In case of a positive response to the above question, the main problem – clarification of the legal catalogue of the employees and its legal nature – can largely be solved. The circumstance, that though the legal nature of the EPSR can be debated,[64] the aim is that compulsory legal norms would come out in the mentioned areas[65] based on the EPSR should be taken into consideration. According to my standpoint, this duality has an effect on the legal nature of the EPSR even today, but the above-mentioned purpose can play an important role in the circle of the forecast reforms of social policy, and labour law. Furthermore, it is obvious that the EPSR is not realised as a

[54] Chapter I (Equal opportunities and access to the labour market), Chapter II (Fair working conditions) and Chapter III (Social protection and inclusion) of the EPSR.

[55] Preamble, point 9 and article 9 of the EPSR regarding the opportunities for real work-life balance.

[56] Erika Kovács, *"Regulatory Techniques for "Virtual Wokers"*, *Magyar Munkajog/Hungarian Labour Law Journal*, Vol. 4. Issue 2, (2017), pp. 1-2.

[57] Ildikó Rácz, *"Munkavállaló vagy nem munkavállaló?: A gig-economy főbb munkajogi dilemmái"*, *Pécsi Munkajogi Közlemények*, Vol. 10. Issue 1, (2017), pp. 82-85.

[58] See a typical example through the battle against poverty and social exclusion (preamble point 9, point b) of article 6 and article 12-14 of the EPSR).

[59] Hendrickx (2017) op. cit., p. 191.

[60] Hendrickx (2018) op. cit., pp. 3-4.

[61] Article 1-20 of the EPSR.

[62] Hendrickx (2018) op. cit., p. 5.

[63] Lörcher – Schömann, op. cit., pp. 5-8.

[64] Hendrickx (2018), op. cit., p. 5.

[65] Hendrickx (2018), op. cit., p. 5.

"pillar"[66] of "labour law" or "the workers"",[67] but mutatis mutandis – e.g. like the European Social Charter – the "social" nature mostly refers to the questions in relation to the employees, even if not exclusively. Otherwise, social focus truly reflects the concept of "solidarity" involved in Chapter 4 of the CFREU which also should be interpreted in all-social context, not exclusively as a special solidarity of labour market, and labour law.[68]

At the same time, the special situation in which the catalogue of social rights and interests naturally contains issues which are connected to the law of the labour market, or free movement as a fundamental freedom,[69] or issues which are closer to the participation of the employees in market activity than to the strictly interpreted relation between the employer and the employee,[70] should be mentioned. Firstly, regarding this quasi-social legal catalogue it should be examined that in social context – with extensive legal interpretation[71] – it really lists the rights of the employees, their families, further actors of the labour market – mostly unemployed people – without mentioning the side of the employer. This approach reflects the "solidarity" and "social" nature,[72] that is, it reflects the basic, original paradigm of labour law, even if its real starting point is a kind of necessity of the (labour) market.

Consequently, the social nature is given, and in the following I am going to analyse how the authorities in close connection to the status of the employee contain the so-called "typical" rights of the workers.[73] In my opinion in this regard the EPSR correctly reflects the real requirements of the labour market, since the EPSR contains the most important "labour laws", although, not in detail or broadly. Regarding the interpretation of the legal environment of the EPSR it will be important how the stated rights of the employees will be concrete and how they will be realised on the scene of legislation. Naturally, to connect legislative action to each authority is not possible, but it is true that the EPSR contains the most important social rights "like a charter"[74] regarding that their development can be enforced through legislation. Of course, it is difficult to forecast the issues of the following years regarding either the content concrete facts or the method of legislation, but on the level of secondary law certain changes can be taken

[66] In order to make clear the concepts, it should be added that the importance of using the term "pillar" itself is rather symbolic, than practical, so I think it is very special that in Union law we can speak about "pillar" in connection to social rights. See: Hendrickx (2017), op. cit., pp. 191-192.

[67] Contrary to the above mentioned socially motivated Charter of 1989 on the rights of the employees.

[68] In any case, "solidarity" reflects the original values and approach of labour law at least as faithfully as the attribute "social", mainly it appears as the protection of the human dignity of the employees. See: Bruno Veneziani, *11. Right of collective bargaining and action (Article 28)*, in: Bercusson (ed.), op. cit., pp. 293.

[69] Article 45 of the TFEU.

[70] For example: article 19 (Housing and assistance for the homeless) and 20 (Access to essential services) of the EPSR.

[71] Rasnača, op. cit., p. 5. and pp.10-15.

[72] György Kiss, "*Foglalkoztatás gazdasági válság idején – a munkajogban rejlő lehetőségek a munkaviszony tartalmának alakítására (jogdogmatikai alapok és jogpolitikai indokok)*", *Állam- és Jogtudomány*, Vol. 55. Issue 1, (2014), p. 50-51. and 58-59.

[73] In my opinion to compile such a catalogue is almost impossible, but the minimal rights in connection to the concept of employee in the traditional sense can be a starting point. See: Tamás Gyulavári, "*A gazdaságilag függő munkavégzés szabályozása. Kényszer vagy lehetőség?"*, *Magyar Munkajog/Hungarian Labour Law Journal*, Vol. 1. Issue 1, (2014), p. 10-12. Further base can be the above mentioned title of IV of the Charter on "solidarity"-like fundamental rights.

[74] Hendrickx (2018) op. cit., p. 5.

into account even according to the most pessimistic approach.[75]

The main cause of pessimism is that the EPSR cannot create new competences or areas for EU in the field of employment policy and social policy, but in my opinion, on the basis of Title IX and X of the TFEU then real legislative intervention is not impossible either. Especially, if the present labour and social regulations are assumed even with all their difficulties and criticism.[76] Altogether, though the EPSR cannot be regarded as an effective legal catalogue, but it is standard anyway, which typically, beyond concrete initiatives, can be conceptual background of the labour law environment in the future, which can be directive for both the side of the employer and the side employees (with the co-operation of the member states). It is worth examining the reform processes of the EPSR in the future, whether new inventions appear concerning the twenty rights, and altogether how the legislators will insist on the three key areas.

## 4. Conclusion

Altogether, it can be stated that the CJEU cannot find legal cause for the direct application of the fundamental rights declared in the CFREU (only under the general conditions), and typically, does not assume the advantages guaranteed for workers, but assumes their restriction based on the market. Naturally, there are fundamental rights – e.g. the right to social security – that indicate the direct application unnecessary because of the relevant secondary legislation, but we can still ask the question: can the CFREU guarantee the most fundamental workers" rights on a higher level or any other way than previously?

In my opinion the CFREU, in spite of the above mentioned contradictions, deals with this dilemma in more and more judgments, but has not constituted a precedent solution so far. Importantly – citing to the merit of judgment no. C-306/16. – referring to article 31 of the CFREU the given right eo ipso does not conclude from the text of the CFREU,[77] but at the same time because a directive exists connected with the article 31, we can come to the conclusion that the CJEU implies the greater importance of the factual regulations of the CFREU, so the cause of setting aside the independent application can be questioned. From another viewpoint, it is not excluded that in such cases the CJEU simply "includes" the directive to the relevant article of the CFREU. However, in this case it can cause an even greater legal dilemma in the future for example article 31 – there are no including rules – but in general we have to face the "deficiencies" of the fundamental rights guaranteed in the CFREU, which bears great risk in the labour market regarding the need for effective social protection.

In summary, the system of workers" rights EU law can be regarded as a structure, which, on the one hand, is in the period of development, mainly because of its relatively young fundamental law relevance, and on the other hand, which several institutions are out of time, consequently, some old deficiencies have to be corrected. At the same time, further improvement along the guidelines of modern labour law and employment is required.[78] In my opinion in

[75] Rasnača, op. cit., pp. 16-18. and pp.37-38.
[76] Rasnača, op. cit., pp. 6-7.
[77] Point 50 of judgment no. C-306/16.
[78] It is justified by the significant, actual endeavours which examine the possibilities of regulating the legal relations of the platform workers. See: Martin Risak, *Fair Working Conditions for Platform Workers. Possible*

this circle traditional interpretation and guarantee of the fundamental social rights is inevitable, but a priori it is a question as to what kind of legal catalogue and legal mechanism can solve the best the interests of the employees.

It also can be observed that there is a contradiction between the fundamental rights of the Charter – though in practice their efficiency is uncertain, but they represent serious legal protection value – and the ideas and the so far achieved results of the EPSR and the current trends of labour law, since the former assumes the strengthening social policy and the need of guarantee of the rights of the employee on high level. On the contrary, the structures of labour market and organisation of work, and consequently labour law, are not going into this direction. I think that the difficulties of labour market and social difficulties in EU are a special kind of coercion in the background of these phenomena, but it seems that the social ideas of the latest years (also) reacts to the European, international economic, and market mechanisms.

As a final remark, let me add that these old-new thoughts should assume the fundamental right of free movement of workers, but should be completed with such legal protective means, mainly with new directives, which more strongly concentrate on the social interests of workers than in the past. In my opinion, even the changes in the labour market, labour law, and society cannot override the essential paradigm of labour law regulation, and it is possible that the EU – partly differently from the old method – have to take more definite steps in order to define and guarantee these rights, or else we cannot speak about a really free labour market. Reflecting on the problems raised in the first part of the paper we can state that the legal protection of workers employees stagnates, changes, and develops at the same time, but the latest ideas of the reform definitely go into the direction of development, even if it often seems only to be a simple change or a very long road ahead.

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# THE FINANCIAL SETTLEMENT OF BREXIT

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## Abstract

*Brexit is a main problem in today"s Europe. The original two-year deadline of Article 50 has passed by and we have witnessed extensions of the exit deadline of the United Kingdom. During the negotiations one of the three mainstream issues that were taken into consideration as a must is the financial settlement between the United Kingdom and the European Union. No-deal Brexit as an United Kingdom exit from the European Union without a negotiated and signed agreement settling the terms after departing was a default situation from the start. Settlement we call the negotiated agreement regarding the financial issues may not be a part of the no-deal Brexit. Such settlement in case of a no-deal may only be slumbering and used as a guide and its content as principles when the parties wish to cooperate on such an area. As the financial settlement part was one of the easiest areas to be accepted by both parties should have as much highlight as areas the parties cannot reach an agreement even at the last minute.*

**Keywords:** *Brexit, Financial, Settlement, Agreement, No-deal*

## Introduction

23 June 2016 marks the latest crisis of the European integration. The United Kingdom European Union membership referendum took place, resulting the 51.9% of the voters favoring leaving the European Union.

Brexit, a linguistic blend of words, British and exit. What do we mean about it? Generally, it is the ongoing British withdrawal from the European Union. If we narrow it down, it could mean only the exact exit, which is now 29 March 2019 23:00 GMT. If we take a general look at the process, Brexit means the meant-to-be two years Article 50 period from 29 March 2017 until 29 March 2019, now extending to 31 October 2019. In a wider sense we could take Brexit from the referendum, or in an even wider viewpoint from the promise of David Cameron that a referendum will be held.

At the beginning of the negotiations between the European Union and the United Kingdom there were three mainstream issues regarding the Brexit: issues related to citizens" rights, the financial settlement, the Northern Irish border. We would like to take a look at the financial settlement in the paper.

To understand the relevance, significance and main aspects of the financial settlement, the following must be clear. As for an agreement regarding the financial settlement, we could easily say that it is one of the clearest areas of the Brexit issues. The financial settlement provisions

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got a green lit in the first, shorter draft of the Withdrawal Agreement.

Being considered as the easiest approvable part by both parties of the Withdrawal Agreement the financial settlement is not receiving as much emphasis as the other two mainstream issues. It should be covered, because the main slogan for the campaign was taking back control, meaning taking back also the control of the financial amounts payable towards the European Union budget.

The British withdrawal process could be seen as the greatest crisis in the European integration. As the Article 50 of the Treaty on European Union states the alternative for member states to leave, and the history of the United Kingdom itself and its relations with the European integration, still the decision came as a surprise.

The no-deal scenario is the main scenario of Article 50. A financial settlement is not the part of the no-deal, such settlement can only be achieved when the agreement has been negotiated and signed by the parties. No draft, document or agreement created of reached is wasted during the Brexit period, it created such ideas that are now essential and can be used in the future or in other areas of law, business and finance.

**Fractures during the European integration**

Before the Brexit we sadly witnessed downfalls during the course of the European integration. What were these? In a nutshell the failure of the Pleven-Plan (the European Defence Community)[1], the flaw of the Constitutional Treaty (the Treaty establishing a Constitution for Europe), the crisis of the Eurozone (the European debt crisis), Euroscepticism[2] itself too, maybe the small states leaving the European Union, and the question of supremacy[3].

Rene Pleven presented its plan of the European Defence Community[4] in 1950, which process resulted into the Treaty establishing the European Defence Community in 1952. The situation was undermined by France failing to ratify the treaty, still in 1954 when the last intentions were made resulting into a non-existing cooperation. The spirit of this kind of cooperation still lived on, and also we have to mention that such kind of idea is not fully off the table.

The Constitutional Treaty of 2004 failed mainly in 2005 because of its name, suggesting it to threaten the sovereignty of the member states by establishing an overruling constitutional entity. After its fail the provisions of this treaty mostly were able to make their way into the Lisbon Treaty which was accepted and ratified by the member states. A small change in the approach could nearly mean a world to someone. This situation showed that the time of the United States of Europe will have to wait.

The crisis we have witnessed from the end of 2009 in the Eurozone can be explained as the fragility of an Economic and Monetary Union. It highlights the need

[1] Klemm Dávid: An Attempt to Establish the European Army: The Pleven Plan, Journal on European History of Law, VOL. 7/2016 No. 1, STS Science Centre Ltd., EU, pp.105-110.

[2] Klemm Dávid: *The United Kingdom and the European Integration*, In: Doktoranduszok Fóruma: Miskolc 2013. november 7.: Állam- és Jogtudományi Kar szekciókiadványa, Miskolci Egyetem Tudományszervezési és Nemzetközi Osztály, Miskolc, 2013, pp. 153-157.

[3] Klemm Dávid: *Az elsőbbség elve az európai integrációban*, In: Studia Iurisprudentiae Doctorandorum Miskolciensium – Miskolci doktoranduszok jogtudományi tanulmányai 17, Bíbor Kiadó, Miskolc, 2017, 117-134.

[4] Klemm Dávid: *Az Európai Védelmi Közösség, mint az Európai Integráció katonai lépcsőfoka*, In: Tavaszi Szél 2016 = Spring Wind 2016 Tanulmánykötet I. kötet: Agrártudomáy, állam- és jogtudomány, föld- és fizikatudomány, had- és rendészettudomány, Doktoranduszok Országos Szövetsége, Budapest, 2016, pp. 219-225.

and necessity of cooperation and mutual understanding, also how the shifts in power may result into vulnerability in a cooperation based on an ever closing integration and most importantly on equality – even being formal. Also the Outright Monetary Transactions of the European Central Bank received[5] highlight[6] during the crisis.

There were three precedents when states have left the European integration, without reducing the number of the member states. French Algeria in 1962, Greenland in 1985 and Saint Barthélemy in 2012. First, French Algeria was the part of France – and also became the part of the European Communities via France – and in 1962 gained independence, resulting into its "withdrawal". The story of Greenland may be the biggest of the three, leaving in 1985. From 1953 until 1979 Greenland was the part of Denmark, as the County of Greenland. With Denmark joining in the first accession wave in 1973, Greenland also became a member. After independence intentions, the in 1979 Denmark in its Home Rule Act enabled Greenland to gain autonomy. So Greenland became an autonomous constituent country of the Kingdom of Denmark. In 1982 a referendum was held whether to remain a member of the integration or leave. The leave votes were in favour with 53%, as a results the Treaty establishing the European Communities to be amended with regard to Greenland in 1984. The last one is Saint Barthélemy was an outermost region of the European Union. Its relationship to France changed from overseas department to overseas collective – not effecting the outermost region status. But this change made possible for them to have a change in their status in the European Union from an outermost region to overseas country or territory. France requested[7] the change for them[8] from the European Union. From 2012 they have "left" the European Union and they function as requested.

And here we are in 2019 witnessing the procedure of Brexit which mainly started for the public with the 2016 referendum. Again the ever closer union is suffering again, not a scenario that Richard von Coudenhove-Kalergi[9] would be happy to see, dreaming about the United States of Europe.

### The Brexit

Brexit is the main phenomenon in the last 2-3 years regarding the issues of the European Union and also one of the biggest challenges in the law of the European Union as well as the law of the United Kingdom.

To take a different approach, a viewpoint regarding the United Kingdom"s specialties as a common law country and the main country for the parliamentary sovereignty could speak for itself. Also the European Union counts toward the future

[5] KLEMM Dávid: *Alkotmányos-e az uniós jog? Az EKB állampapír-vásárlási programja a német alkotmánybíróság és az EB szerint*, In: Via scientiae iuris: International Conference of PhD Students in Law, Gazdász Elasztik Kft., Miskolc, 2015, pp.191-202.

[6] THEIL, Stefan: *A union of states, constitutions, administrations and judiciaries: some initial thoughts on the OMT ruling of the German Constitutional Court*, U.K. Constitutional Law Blog, 20th July 2016

[7] 15224/10 Draft European Council Decision on amendment of the European status of the island of Saint-Barthélemy, Brussels, 20 October 2010, (3)

[8] France"s request reflects the desire expressed by the elected representatives of the island of Saint-Barthélemy, which is an overseas collectivity within the French Republic, governed by Article 74 of the French Constitution, with autonomy, to obtain a European status which would be better suited to its status under domestic law, particularly given its remoteness from the mainland, its small insular economy largely devoted to tourism and subject to difficulties in obtaining supplies which hamper the application of some European Union standards.

[9] KLEMM Dávid: *Kalergi Páneurópa mozgalma, mint az európai integráció előfutára*, In: Doktoranduszok fóruma: Miskolc, 2015. november 19.: Állam- és Jogtudományi Kar Szekciókiadvány, Miskolci Egyetem, Miskolc, 2016, pp. 161-164.

with its current member states but the United Kingdom.[10]

The first etap is until the voting day. Everything began with the draft renegotiating deal, where the European Union membership of the United Kingdom was put on the table, for a better set of rules for them, which would have been negotiated further after the 2016 referendum.[11] As in one of many member states, the United Kingdom also highlighted the sovereignty issue, this time during the renegotiation.[12] All this was before the referendum, everyone was waiting for it to pass by with a remain majority.[13] As an aspect of UK (constitutional) law, the question was in the air of the binding nature of the referendum. Furthermore there was an inclusion of voters, citizen who reside abroad, for example the Shindler case before the ECJ started with this issue.[14] Before the voting day some possible outcomes were foreshadowed in case of a leave majority (which many of them we face and are facing even right now).[15] Where we were at a point, no one thought many remain objective, and provided us with detailed milestones.[16]

From the leave majority at the referendum begins our next stage. The role of the Parliament after the referendum was beginning to gain highlight.[17] As in most matters it was unclear at the first, and even at the second sight what is the solution or the possibility regarding Article 50, it was not otherwise with the triggering it in the United Kingdom.[18] Also until the triggering there was period of uncertainty, everyone speculating in the unknown areas of Article 50.[19] Furthermore the devolution of the four nations came up.[20] What could happen, if the majority of the people awaits a different result than the result was voted for from the majority of voters? Questions could be thrown at the legitimacy[21] issue of the referendum.[22] It became clear in the first days that the Government and the Parliament will have to go hand in hand to achieve.[23] The fundamental constitutional principles

[10] Klemm Dávid: *A 27-ek Európai Uniója – az Európai Unió jövőjéről szóló fehér könyv*, In: Profectus in litteris IX.: Előadások a 14. debreceni állam- és jogtudományi doktorandusz-konferencián, Lícium Art, Debrecen, 2018, pp. 175-184.

[11] Peers, Steve: *The Draft Renegotiation Deal: EU Immigration Issues*, U.K. Constitutional Law Blog, 3rd February 2016

[12] Gordon, Mike: *The UK"s Sovereignty Uncertainty*, U.K. Constitutional Law Blog, 11th February 2016

[13] Eleftheriadis, Pavlos: *The Proposed New Legal Settlement of the UK with the EU*, U.K. Constitutional Law Blog, 13th February 2016

[14] Barczentewicz, Mikolai: *Does EU Law Bind Parliament as to Withdrawal from the EU? British Expats and Their Right to Vote (Shindler)*, U.K. Constitutional Law Blog, 16th June 2016

[15] Walker, Neil: *The Brexit Vote: The Wrong Question for Britain and Europe*, U.K. Constitutional Law Blog, 21st June 2016

[16] Renwick, Alan: *The Road to Brexit: 16 Things You Need to Know about What Will Happen If We Vote to Leave the EU*, U.K. Constitutional Law Blog, 22nd June 2016

[17] Barber, Nick - Hickman, Tom - King, Jeff: *Pulling the Article 50 "Trigger": Parliament"s Indispensable Role*, U.K. Constitutional Law Blog, 27th June 2016

[18] Armstrong, Kenneth: *Push Me, Pull You: Whose Hand on the Article 50 Trigger?*, U.K. Constitutional Law Blog, 27th June 2016

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[21] Ekins, Richard: *The Legitimacy of the Brexit Referendum*, U.K. Constitutional Law Blog, 29th June 2016

[22] Tierney, Stephen: *Was the Brexit Referendum Democratic?*, U.K. Constitutional Law Blog, 25th July 2016

[23] Tucker, Adam: *Triggering Brexit: A Decision for the Government, but under Parliamentary Scrutiny*, U.K. Constitutional Law Blog, 29th June 2016

set up a clear road[24], but as we see later, everything regarding Brexit needs a confirmation. Article 50 arose questions of its own rules and of rules regarding international law too.[25] The referendum shook up the still waters of the constitutional law in the United Kingdom[26] as well as the sleeping areas of European Union law too. It should become clear that the United Kingdom and its special legal system requires a more cautious approach.[27] Unwritten and flexible, the two main aspects[28] of the UK constitution[29] which could delay the processes and cause even more uncertain moments. Even more touches regarding the binding nature[30] of the referendums[31] came along the way[32], all slumbering issues waking up. The early general election[33] was already in the air a few days after the referendum.[34] Seeing the long-continued issues before the triggering[35] could warn us what a short two years we will have. Questions of the result following regarding the referendum even mention a second[36] possible referendum which will be targeted even more and more.[37] Before pulling the trigger, it already made sense to get clear about the one way scenario of the Brexit.[38] European Union citizenship also began to arise as an issue.[39] Triggering Article 50 brings further questions. The real questions began to rise what the triggering would mean.[40] What is being in the present days put behind the mainstream questions is the Fundamental Rights Charter of the European Union.[41] The Vienna Convention

[24] Smith, Ewan: *What Would Happen if the Government Unlawfully Issued an Article 50 Notification without Parliamentary Approval?*, U.K. Constitutional Law Blog, 30th June 2016

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[28] Reid, Paul: *Brexit: Some Thoughts on Scotland*, U.K. Constitutional Law Blog, 2nd July 2016

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[40] LIENEN, Christina: *Brexit and the Domestic Judiciary: Some Preliminary Thoughts on the Aftermath of Triggering Article 50*, U.K. Constitutional Law Blog, 21st July 2016

[41] Adenitire, John: *The Executive Cannot Abrogate Fundamental Rights without Specific Parliamentary Mandate – The Implications of the EU Charter of Fundamental Rights for Triggering Art 50*, U.K. Constitutional Law Blog, 21st July 2016

on the Law of Treaties will become a handy tool regarding the international law elements.[42] EEA and WTO, two magic words begun to circulate and get itself popularity.[43] The European Communities Act 1972 is of high significance during the debates before the trigger.[44] Also the House of Lords Constitutional Committee supplied us with a report on Article 50 as well.[45] The referendum was recalled as the lost gamble of David Cameron.[46] The idea of a Great Repeal Bill surfaced as a solution for removing the European Communities Act.[47] The decision for the execution of the triggering floating in the air whether the parliament or the government shall execute it.[48] Back in the days even the revoking surfaced before the triggering,[49] but only has been made clear in the not so distant past. We must take a moment to note that the parliamentary sovereignty is gradually eroding.[50] As time passed the Miller case started and was concluded[51] on the level of the High Court.[52] There shall be an Act of Parliament to trigger Article 50 by the government.[53] Brexit created a complex process under three legal systems.[54] An Act is required to ensure the constitutional requirements in Article 50.[55] Should the Miller case be the main highlight of that era before the trigger, the mainstream line was given in mediums regarding the Brexit.[56] We see now that on the European Union level also made its clear statements. The fear of irreversibility is a main factor of triggering Article 50.[57] The Miller case went before the Supreme Court, but really, during this period of time, there should have been more important issues behind the curtains in development and research. As the rules of

[42] Rylatt, Jake W.: *The Irrevocability of an Article 50 Notification: Lex Specialis and the Irrelevance of the Purported Customary Right to Unilaterally Revoke*, U.K. Constitutional Law Blog, 27th July 2016

[43] Bobić, Ana - van Zeben, Josephine: *Negotiating Brexit: Can the UK Have Its Cake and Eat It?*, U.K. Constitutional Law Blog, 2nd August 2016

[44] Creelman, Gavin: *The Relevance of Thoburn to the Article 50 "Trigger" Debate*, U.K. Constitutional Law Blog, 6th September 2016

[45] Elliott, Mark - TIERNEY, Stephen: *The House of Lords Constitution Committee Reports on Article 50*, U.K. Constitutional Law Blog, 13th September 2016

[46] Joseph, Philip: *Brexit: A View from Afar*, U.K. Constitutional Law Blog, 23rd September 2016

[47] Douglas-Scott, Sionaidh: *The "Great Repeal Bill": Constitutional Chaos and Constitutional Crisis?*, U.K. Constitutional Law Blog, 10th October 2016

[48] Eeckhout, Piet: *The UK Decision to Withdraw from the EU: Parliament or Government?*, U.K. Constitutional Law Blog, 15th October 2016

[49] Sari, Aurel: *Biting the Bullet: Why the UK Is Free to Revoke Its Withdrawal Notification under Article 50 TEU*, U.K. Constitutional Law Blog, 17th October 2016

[50] Campion, Elizabeth: *Pay No Attention to the Man Behind the Curtain: Parliamentary and Governmental Power in the Wake of the EU Referendum*, U.K. Constitutional Law Blog, 24th October 2016

[51] Barber, Nick - King, Jeff: *Responding to Miller*, U.K. Constitutional Law Blog, 7th November 2016

[52] Elliot, Mark - Hooper, Hayley J.: *Critical reflections on the High Court"s judgment in R (Miller) v Secretary of State for Exiting the European Union*, U.K. Constitutional Law Blog, 7th November 2016

[53] King, Jeff: *What Next? Legislative Authority for Triggering Article 50*, U.K. Constitutional Law Blog, 8th November 2016

[54] Allott, Philip: *Fundamental Legal Aspects of UK Withdrawal from the EU: Eight Stages on the Way to a New Relationship*, U.K. Constitutional Law Blog, 9th November 2016

[55] Adenitire, John: *Exiting the EU Constitutionally*, U.K. Constitutional Law Blog, 9th November 2016

[56] O"Connell, Paul - Sultany, Nimer: *Miller and the Politics of the Judiciary*, U.K. Constitutional Law Blog, 10th November 2016

[57] McCrea, Ronan: *Arguing that Article 50 Notification Is Reversible Involves Risks for the Government*, U.K. Constitutional Law Blog, 15th November 2016

the European Union law the Supreme Court could refer to the ECJ[58], but dealing with the revoke was not a practical question at that times.[59] The nature of European Union law in the United Kingdom"s special legal environment is also an interesting topic.[60] The essence and importance of the Miller judgement should not be lost[61], because of high significance.[62] Besides the revoke, also the interpretation issues began arising speaking of Article 50.[63] The Supreme[64] Court[65] was expected to approve the High Court.[66] As time passing by the Northern Ireland issue should surface.[67] The Miller case also highlighted some past aspects that could slumber forever without the Brexit, even in the case of a renegotiation.[68] The Supreme Court decision was a must after the appeal.[69] The government is accountable to the parliament in all cases.[70] Also that Miller could get us closer to the special nature of European Union law.[71] Notification of withdrawal, the named triggering of Article 50 generated even more disputes.[72] Brexit showed us how complex the British constitutional law is.[73] It became clear that the Parliament enables the triggering without knowing how the deal and the future relationship will be.[74] Could the taking back control be achieved after the approval was the main question.[75] The instructions regarding the European Union law will be changed from the European Communities Act to the Great Repeal Bill.[76] The latter will

[58] De Cecco, Francesco: *Miller, Article 50 Revocability and the Question of Control*, U.K. Constitutional Law Blog, 17th November 2016

[59] Georgopoulos, Aris: *(Un)Crossing the Rubicon: Why the Supreme Court Should Not Refer a Question Regarding the Revocability of Article 50 to the ECJ*, U.K. Constitutional Law Blog, 17th November 2016

[60] Barczentewicz, Mikolaj: *Consequences of the High Court"s Reasoning in the Article 50 Judgment: EU Law-making Unlawful*, U.K. Constitutional Law Blog, 18th November 2016

[61] King, Jeff - Barber, Nick: *In Defence of Miller*, U.K. Constitutional Law Blog, 22nd November 2016

[62] Phillipson, Gavin: *The Miller Case, Part 1: A Response to Some Criticisms*, U.K. Constitutional Law Blog, 25th November 2016

[63] Smismans, Stijn: About the Revocability of Withdrawal: Why the EU (Law) Interpretation of Article 50 Matters, U.K. Constitutional Law Blog, 29th November 2016

[64] Jones, Rachel: *The Importance of Silences in the "Brexit" Appeals*, U.K. Constitutional Law Blog, 7th December 2016

[65] Howarth, David: *On Parliamentary Silence*, U.K. Constitutional Law Blog, 13th December 2016

[66] Craig, Robert: Miller: *The Statutory Basis Argument: A Primer*, U.K. Constitutional Law Blog, 5th December 2016

[67] Harvey, Colin: *Northern Ireland"s Transition and the Constitution of the UK*, U.K. Constitutional Law Blog, 12th December 2016

[68] Renton, Simon: *Historical Perspectives and the Miller Case*, U.K. Constitutional Law Blog, 19th January 2017

[69] Craig, Robert: *Miller Supreme Court Case Summary*, U.K. Constitutional Law Blog, 26th January 2017

[70] Endicott, Timothy: *A Treaty of Paramount Importance*, U.K. Constitutional Law Blog, 26th January 2017

[71] O"Brien, Patrick: *All for Want of a Metaphor: Miller and the Nature of EU Law*, U.K. Constitutional Law Blog, 30th January 2017

[72] Allott, Philip: *Taking Stock of the Legal Fallout from the EU (Notification of Withdrawal) Act 2017*, U.K. Constitutional Law Blog, 2nd February 2017

[73] Lock, Tobias – DALY, Tom Gerald: *Brexit and the British Bill of Rights: Capturing Constitutional Complexity*, U.K. Constitutional Law Blog, 13rd February 2017

[74] Barczentewicz, Mikolaj: The *Principle of Legality in the EU-Withdrawal Statute*, U.K. Constitutional Law Blog, 21st February 2017

[75] Jancic, Davor: *A Very Parliamentary Brexit: Satire in Two Acts*, U.K. Constitutional Law Blog, 23rd February 2017

[76] Horsley, Thomas: *UK Courts and the Great Repeal Bill – Awaiting Fresh Instruction*, U.K. Constitutional Law Blog, 28th February 2017

also delegate powers of legislation.[77] Right before the trigger the dangers of Brexit began to surface, and the possible solutions also.[78] The Act on the notification is able to cause a constitutional ripple effect.[79]

The next stage can be seen when Theresa May triggered Article 50 on 29 March 2017. After the trigger of the notification, solutions and future relations began to emerge, like the WTO rules and the European Economic Area.[80] The Great Repeal Bill has a trio of tasks, repealing, converting and empowering.[81] The Good Friday Agreement has enormous significance and cannot become fragile.[82] After the notification that was the 9 months from the referendum, we could ask a question that would it still be on valid grounds?[83] The rights of the citizens also emerged.[84] The proper transition should be the aim, time is passing by, the clock is ticking.[85] There shall be both constitutional change and also legal continuity.[86] The Henry VIII clauses[87] received also numerous comments.[88] The House of Lords Constitutional Committee continued its work.[89] The European Union Directives[90] were likely paralled with the new Henry VIII provisions.[91] After half a year from the triggering there are thoughts whether Brexit can be stopped.[92] Revoking the trigger would also require the Parliament.[93] Two tools could have been used to avoid the no deal Brexit, one being the delayed exit the other the decreasing membership, but none

[77] Elliott, Mark – Tierney, Stephen: *The "Great Repeal Bill" and Delegated Powers*, U.K. Constitutional Law Blog, 7th March 2017

[78] Schwartz, Alex: *Mitigating the Hazards of Brexit: The EEA Option for Northern Ireland*, U.K. Constitutional Law Blog, 27th March 2017

[79] Campion, Elizabeth: *The Constitutional „Ripple Effect" of the European Union (Notification of Withdrawal) Act 2017*, U.K. Constitutional Law Blog, 27th March 2017

[80] Tomlinson, Joe: *UK Quo Vadis? The EEA as a Workable Framework*, U.K. Constitutional Law Blog, 6th April 2017

[81] Hayne, K M: *The "Great Repeal Bill"*, U.K. Constitutional Law Blog, 12th April 2017

[82] Harvey, Colin – Holder, Daniel: *The Great Repeal Bill and the Good Friday Agreement – Cementing a Stalemate or Constitutional Collision Course?*, U.K. Constitutional Law Blog, 6th June 2017

[83] Armstrong, Kenneth: *Has Article 50 Really Been Triggered?*, U.K. Constitutional Law Blog, 14th June 2017

[84] McCrudden, Christopher: *An early deal-breaker? EU citizens" right sin the UK after Brexit, and the future role of the European Court of Justice*, U.K. Constitutional Law Blog, 27th June 2017

[85] Gauci, Jean-Pierre – McCorquodale, Robert: *Brexit and Transitional Provisions: International Law Can Assist*, U.K. Constitutional Law Blog, 28th June 2017

[86] Caird, Jack Simson: *The European Union (Withdrawal) Bill: Constitutional Change and Legal Continuity*, U.K. Constitutional Law Blog, 18th July 2017

[87] Khaitan, Tarun: *A Constitution Proctection Clause for the Great Repeal Bill?*, U.K. Constitutional Law Blog, 19th July 2017

[88] Campbell, Kenneth QC: *Henry VIII Comes to Scotland, Wales and Northern Ireland, and Other Devolution Questions in the EU (Withdrawal) Bill*, U.K. Constitutional Law Blog, 20th July 2017

[89] Elliott, Mark – Tierney, Stephen: *House of Lords Constitutional Committee Issues Interim Report ont he EU (Withdrawal) Bill*, U.K. Constitutional Law Blog, 7th September 2017

[90] Lang, Richard: *The European Union (Withdrawal) Bill: Clause 4(2)(b), a Reply to Downie and Furhter Reflections*, U.K. Constitutional Law Blog, 15th November 2017

[91] Downie, Gordon: *Brexit: What to Make of Directives?*, U.K. Constitutional Law Blog, 8th September 2017

[92] Mac Amhlaigh, Cormac: *Can Brexit Be Stopped under EU Law?*, U.K. Constitutional Law Blog, 10th October 2017

[93] Craig, Robert: *Why an Act of Parliament Would Be Required to Revoke Notification under Artlicle 50*, U.K. Constitutional Law Blog, 16th October 2017

of these are likely to be.[94] Retained European Union law will be in the hands of domestic courts.[95] At the end of 2017 we can witness the mention of a transitional period.[96] The Withdrawal Agreement could cause problems regarding the parliamentary sovereignty[97] during its implementation.[98] Also the two clashing principles are still the sovereignty and the supremacy during the debates of the implementation of withdrawal into United Kingdom law.[99] Retained EU law[100] is an enormous question.[101] A second referendum is once again digging up questions regarding the referendums in general and its history.[102] Also what was split into two, that there shall be an agreement regarding the exit itself and also one separate for the future relationship.[103] There is a four sided interaction between national, EU, WTO and international law during the Brexit.[104] The implementation of withdrawal would "provide continuity and certainty" like behaving as a "legal rule book" in the United Kingdom.[105] The retained EU law term is generating[106] issues in the national law order in the United Kingdom.[107] The EU law status in the United Kingdom[108] from a legal[109] aspect could be more of importance than any other Brexit issues, but it is a national issue, not gaining any highlight in the mostly European Union aspect press releases. Wightman[110] also started as a could be milestone case[111] (with

[94] Cuyvers, Armin: *Two Legal Tools to Avoid Hard Brexit: Delayed Exit and Decreasing Membership under Article 50 TEU*, U.K. Constitutional Law Blog, 24th November 2017

[95] Horsley, Thomas: *In (Domestic) Courts We Trust: The European Union (Withdrawal) Bill and The Interpretation of Retained EU Law*, U.K. Constitutional Law Blog, 27th November 2017

[96] Daly, Paul: *EU Law in the UK after Brexit: EU Nationals" Rights and a Transitional Period*, U.K. Constitutional Law Blog, 15th December 2017

[97] Gordon, Mike: *Parliamentary Souvereignty and the Implementation of the EU Withdrawal Agreement (Part I)*, U.K. Constitutional Law Blog, 17th January 2018

[98] Gordon, Mike: *Parliamentary Souvereignty and the Implementation of the EU Withdrawal Agreement (Part II)*, U.K. Constitutional Law Blog, 18th January 2018

[99] Elliott, Mark - TIERNEY, Stephen: *Sovereignty or Supremacy? Lords Constitution Committee Reports on EU (Withdrawal) Bill*, U.K. Constitutional Law Blog, 29th January 2018

[100] Craig, Paul: *The Withdrawal Bill, Status and Supremacy*, U.K. Constitutional Law Blog, 19th February 2018

[101] Ford, Michael - Syrpis, Phil: *Retained EU law in the EU (Withdrawal) Bill: A Reaction to the House of Lords Constitution Committee Report*, U.K. Constitutional Law Blog, 14th February 2018

[102] Trueblood, Leah: *The Merits and Meaning of a "Second" Referendum*, U.K. Constitutional Law Blog, 5th February 2018

[103] Caird, Jack Simson: *Parliament and the Withdrawal Agreement: The "Meaningful Vote*, U.K. Constitutional Law Blog, 9th February 2018

[104] Allott, Philip: *The EU Legal System Is Not a Thing You Can Leave*, U.K. Constitutional Law Blog, 21st February 2018

[105] Craig, Paul: *European Union (Withdrawal) Bill: Legal Status of EU Retained Law*, U.K. Constitutional Law Blog, 26th February 2018

[106] Laws, Stephen: *Giving "Deemed" Domestic Law Status to Retained EU Law*, U.K. Constitutional Law Blog, 28th February 2018

[107] Craig, Paul: *European Union (Withdrawal) Bill: Legal Status and Effect of Retained Law*, U.K. Constitutional Law Blog, 8th March 2018

[108] Young, Alison: *Status of EU Law Post Brexit: Part One*, U.K. Constitutional Law Blog, 2nd May 2018

[109] Young, Alison: *Status of EU Law Post Brexit: Part Two*, U.K. Constitutional Law Blog, 4th May 2018

[110] Jones, Brian Christopher: *Wightman and How Not to Advance the Law*, U.K. Constitutional Law Blog, 11th April 2018

[111] Campbell, Kenneth: *Wightman v Secretary of State: Article 50 and Parliamentary Privilege*, U.K. Constitutional Law Blog, 22nd June 2018

another possible, but rejected one).[112] A dispute resolving mechanism is also a fundamental need to settle any issues.[113] We should not forget that besides the Commons, the Lords are there too in the Parliament.[114] Once again[115] there could be a feeling that the national, internal issues of the United Kingdom minimize the real upcoming threat of a no deal scenario. With the end drawing near implications of Article 50 began to be highlighted.[116] We can find the mainstream problems arising too in the national debates.[117] The possible models for the future like the EFTA are part of a complicated future picture.[118] Again half a year before the exit date and the possibilities and questions regarding the revoke surface again.[119] The acknowledged fact that before the exit day[120] all pending issues regarding the inner withdrawal issues have to be settled becomes questionable when the date could be moved. The political declaration besides the withdrawal agreement draft also brings us questions regarding the procedures[121] in the United Kingdom (regarding the meaningful vote.)[122] Like all things regarding the Brexit, we could speculate or draw possible plans and outcomes[123], but even in the last days or even hours a surprise can come up.

14 November 2018 marks the "final" version of the Withdrawal Agreement published. Also the Wightman[124] decision[125] of the ECJ has been delivered.[126]

"Article 50 TEU must be interpreted as meaning that, where a Member State has notified the European Council, in accordance with that article, of its intention to withdraw from the European Union, that article allows that Member State — for as

[112] Craig, Robert: *New Article 50 Case Resoundingly Rejected by the Divisional Court*, U.K. Constitutional Law Blog, 26th June 2018

[113] Horne, Alexander: *Dispute Resolution and Enforcement after Brexit*, U.K. Constitutional Law Blog, 3rd May 2018

[114] Young, Francis: *"Packing" the Lords: Some Legal Reflections*, U.K. Constitutional Law Blog, 16th May 2018

[115] Caird, Jack Simson: *Parliament"s Right to a "Meaningful Vote": Amendments to the EU (Withdrawal) Bill*, U.K. Constitutional Law Blog, 11th June 2018

[116] Young, Allison: *European Union (Withdrawal) Bill and the Meaningful Vote: Constititutional Inconsistency or Constitutional Inconvenience?*, U.K. Constitutional Law Blog, 20th June 2018

[117] Deb, Anurag: *The Unquiet Irish Border Problem: Implications in the Aftermath of the Withdrawal Act*, U.K. Constitutional Law Blog, 5th July 2018

[118] Solomon, Solon: *The Chequers Agreement: Brexit and the Infeasibility of Judicial and Legal Independence*, U.K. Constitutional Law Blog, 12th July 2018

[119] Taylor, Robert Brett - WILSON, Adelyn L. M.: *Seeking and Implementing a Referral on Revocability of Article 50 Following Wightman*, U.K. Constitutional Law Blog, 26th September 2018

[120] Caird, Jack Simson: *Taking Back Control: Brexit, Parliament and the Rule of Law*, U.K. Constitutional Law Blog, 10th October 2018

[121] Caird, Jack Simson: *Brexit and the Meaninful Vote: Down the Procedural Raab-it Hole?*, U.K. Constitutional Law Blog, 22nd October 2018

[122] Craig, Robert - Phillipson, Gavin: *Could the "Meaningful Vote" End up in Court?*, U.K. Constitutional Law Blog, 24th October 2018

[123] Allott, Philip: *UK/EU Withdrawal Agreement: A Legal Speculation*, U.K. Constitutional Law Blog, 7th November 2018

[124] Phillipson, Gavin - YOUNG, Alison L.: *Wightman: What Would Be the UK"s Constitutional Requirements to Revoke Article 50?*, U.K. Constitutional Law Blog, 10th December 2018

[125] Armstrong, Kenneth: *The Advent of Brexit – Can It Be Paused?*, U.K. Constitutional Law Blog, 12th December 2018

[126] Georgopoulos, Aris: *Revoking Article 50 TEU (C-621/18 Wightman and others): "Iphigenia Must Reach the Altar"*, U.K. Constitutional Law Blog, 17th December 2018

long as a withdrawal agreement concluded between that Member State and the European Union has not entered into force or, if no such agreement has been concluded, for as long as the two-year period laid down in Article 50(3) TEU, possibly extended in accordance with that paragraph, has not expired — to revoke that notification unilaterally, in an unequivocal and unconditional manner, by a notice addressed to the European Council in writing, after the Member State concerned has taken the revocation decision in accordance with its constitutional requirements. The purpose of that revocation is to confirm the EU membership of the Member State concerned under terms that are unchanged as regards its status as a Member State, and that revocation brings the withdrawal procedure to an end."[127]

Revoking is officially an option now.[128] The Backstop of the withdrawal agreement regarding Northern Ireland is named as one of the vote against factors.[129]

With the original exit date closing in, there was an extension period granted on 21 March 2019 until 12 April the same year. Thanks to this on 29 March 2019 the UK did not leave the EU but Theresa May asked for another extension of the exit date on 5 April. It was granted on 10 April until 31 October 2019. There was a special requirement that the UK had to hold the European Parliament Elections, failing this, the extension would have been only valid until 1 June.

Theresa May ended her little more than three year term as a Prime Minister on 24 July 2019 by resigning. Boris Johnson assumed his office as Prime Minister on 24 July. His plan to carry out the Brexit on the 31 October date stick to his mind. The prorogation of the UK Parliament that was carried out by Johnson was ruled unlawful by the Supreme Court on 24 September.

On 11 October, just weeks before the current deadline, there is again light at the end of the tunnel, there might be a solution as the negotiators from both sides are working on the agreement to avoid the hard Brexit, the no-deal scenario.

Brexit is now, as from the beginning, in a constant uncertainty.

### The mainstream issues of Brexit

After triggering Article 50, negotiations begun on 19 June 2017, naming the three mainstream issues, the Northern Irish border, the issues relating to citizens" rights, and the financial settlement.[130]

If we take a look at these mainstream issues, it is clear that these received the most significance, and mainly the issues related to the European Union have the highlights, the internal United Kingdom issues are not showcased outside the United Kingdom.

### The financial settlement

The financial settlement should be regarded as a mainstream Brexit issue, one of the three topics that occurred in the first place during the negotiations. But it is not an issue that should rob the importance of the other issues. Every single question that arose during the Brexit is a significant one. The whole picture shall be counted as a sum of the to be solved questions. This is an

[127] Judgment of the Court (Full Court) of 10 December 2018 Andy Wightman and Others v Secretary of State for Exiting the European Union – Case C-621/18

[128] Dixon, Dennis: *Wightman and the General Interpretation of Article 50*, U.K. Constitutional Law Blog, 7th January 2019

[129] Caird, J. Simson - Paterson, Ellis: *Could the UK Courts Disapply Domestic Legislation to Enforce the Protocol on Ireland and Northern Ireland?*, U.K. Constitutional Law Blog, 19th February 2019

[130] Speech by Michel Barnier, the European Commission"s Chief Negotiator, following the first round of Article 50 negotiations with the UK Brussels, 19 June 2017

Achilles heel of the Brexit, putting too much pressure on a few issues, and for a longer period of time, and by doing so ticking the precious time from other issues, resulting into jeopardizing the whole process.

What describes the financial settlement the best are the three words: mutual financial claims.[131] We are faced with a set of agreed terms from which there is no non-performance for the parties. It can end in two possible ends. The two scenarios are one for any agreement between the parties and one for the lack of such an agreement.

**In case of an agreement**

As in all matters of Brexit, the financial settlement is no exception, until the Withdrawal Agreement is not accepted, we have only a non-binding political declaration. First of all, the political agreement regarding the financial settlement was published on 8 December 2017, in the "Joint report from the negotiators of the European Union and the United Kingdom Government on progress during phase 1 of negotiations under Article 50 TEU on the United Kingdom"s orderly withdrawal from the European Union". The binding legal document should have been the Withdrawal Agreement, from which we have now an older, shorter, and an up-to-date longer version – being published on 19 March[132] and 14 November 2018. Our basic sources regarding the financial settlement are the Joint report and the draft Withdrawal Agreement.

Comparing the coloured March version and the new November version of the Withdrawal Agreement, in the financial provisions chapter we do not find any outstanding differences. What has to be pointed out, is the possibility of an extension of the transition period in the latest version, and the financial regulations of this possibility.

The Joint report starts its financial settlement part stating the agreement between the United Kingdom and the European Union on a methodology for the financial settlement. Consisting of four parts, a components list, a principles set regarding the value calculation and payment modalities, arrangements for the current Multiannual Financial Framework (for continued participation of the UK in the programmes of the current MFF until their closure), and also financial and related arrangements of the areas outside the EU budget (for the European Investment Bank, the European Central Bank, European Union trust funds, the Facility for Refugees in Turkey, Council agencies and also the European Development Fund).

There are three components of the settlement: United Kingdom participation in Union annual budgets to 2020, Outstanding commitments at the end of 2020, and Liabilities, contingent liabilities and corresponding assets. The annual union budgets of 2019 and 2020 will have the United Kingdom as a contributor and a participant during their implementation, in the form as the United Kingdom had remained in the Union. If there are any amendments after the date of the withdrawal and effecting the financial obligations of the United Kingdom, they will not apply on it. Also the annual revenue adjustment for 2020 will be calculated if it had remained in the Union regarding the amounts to be returned to or returned by it. The outstanding

[131] Sánchez-Barrueco, Maria-Luisa: *Leaving the EU budget: Brexit and mutual financial claims*, ERA Forum (2018) 18:453-468

[132] Draft Agreement on the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and the European Atomic Energy Community highlighting the progress made (coloured version) in the negotiation round with the UK of 16-19 March 2018

commitments financing share shall also be contributed by the United Kingdom at the end of 2020.

The situation clearly represents the rights and obligations arising from any contractual relationship. May the principle of pacta sunt servanda serve us during the initial detailing, and the understanding for the no deal scenario.

The United Kingdom shall fulfil the following obligations and have the following rights regarding the financial settlement in case of an agreement: contributing and participating in the European Union budgets of 2019 and 2020 being part of a transition or implementation period; the European Union funding towards the United Kingdom will be continued regarding European Union programmes being part of the 2014-2020 budget plan; contributing to the outstanding budget commitments on 31 December 2020 which commitments have been already undertaken but paid; contributing to before 31 December 2020 incurred European Union liabilities for example European Union staff pensions; liability for contingent liabilities of the European Union which mainly cover given financial guarantees and legal risks; the United Kingdom is entitled for its capital in the European Investment Bank which is 3.5 billion € and shall be paid back in twelve instalments beginning 2019; also the United Kingdom is entitled for its capital in the European Central Bank which is paid back at the time of withdrawal because of its rather small amount; United Kingdom liabilities remain regarding the European Investment Bank for its undertaken liabilities before the Withdrawal Agreement entering into force; also guarantee providing for the outstanding loans stock of the European Investment Bank; and lastly continuing the participation in the overseas programmes of the European Union until the end of the current round for example the European Development Fund.[133]

The main three principles of the settlement are: because of the withdrawal of the United Kingdom, there shall be no member state in the European Union to pay more or to receive less; during the membership the United Kingdom shall pay the share of its commitments; for the payments of the United Kingdom it shall not pay more or shall not pay earlier, as it remained in the European Union.

Regarding the participation of the United Kingdom in the Union annual budgets to 2020 it is clear that the contribution and the participation will continue in 2019 and in 2020. Only non-applying rules in this field of finances are the amendments to the budget itself or the financing of the budget after the date of withdrawal (likely 29 March 2019?). For the programmes participation the United Kingdom shall perform its obligations occurred during the current budget until these programmes close. The next milestone is the outstanding commitments of the European Union budget, shortly RAL after reste a liquider, where the United Kingdom shall make its contribution for the RAL financing at 31 December 2020. Liabilities is the next topic, where of those incurring before 31 December 2020 on the side of the European Union, the United Kingdom shall finance theme. One of the main liability are the pensions and other benefits of European Union employees. There are also contingent liabilities. These are a special kind of liabilities, being only potential, that may be occurring in the future. For example these are financial operations and legal cases. One additional but remarkable aspect of the

[133] Keep, Matthew: *Brexit: the exit bill, Briefing Paper Number 8039*, 21 January 2019, House of Commons Library, 3.

financial settlement, that the currency used shall be the euro.

Also there are areas outside the European Union budget. For the European Investment Bank the United Kingdom shall have its paid-in capital repaid. The amount we speak of is 3.5 billion euros. Starting the end of 2019 they shall have it back in twelve annual instalments. Also the 56 million € paid-in capital of the United Kingdom in the European Central bank is worth of mentioning. The aforementioned European Development Fund is also in play. So are the European Union Trust funds.

There is an estimate of the HM Treasury of the settlement and its components, giving us the United Kingdom participation in the European Union annual budgets to 2020 in 17-18 billion euros from 2019 to 2020, the RAL from 2021 to 2026 in 21-23 billion euros, the other net liabilities from 2021 to 2064 in 2-4 billion euros, coming to a total estimate of 40-45 billion euros from 2019 to 2064.

With the introduction of the possibility of transition period extension – in Article 132 of the Withdrawal Agreement draft – the financial settlement rules shall also comply with the new regulations. The extension means that the transition period will not end on 31 December 2020, but on the same day on 2021 or 2022. Regarding the next European Union budget for the years 2021-2027 the United Kingdom shall be treated in the European Union programmes as a third country. Moreover, the obligation of the United Kingdom to contribute towards the European Union budget will cease to exist. Also the Common Agricultural Policy will not have the United Kingdom as its part.[134]

**No deal scenario**

From the beginning, there was a chance for the no deal scenario and there still is. The Withdrawal Agreement is the only thing that could bear a legally binding character. The no deal scenario occurs when there is no accepted agreement between the United Kingdom and the European Union. So, the political agreement that has been reached last year is not of legally binding character, all of its provisions or agreed terms including the financial settlement could not be enforced. The reached status regarding all fields is all depending on the political approach and on how the relationship between the two parties shall be honoured looking at the future. The financial settlement as it is in case of a no deal could be looked at as a gentlemen"s agreement. After shaking hands it depends on you how you apply those rules for yourself. Before triggering Article 50, the House of Lords European Union Committee published a paper on Brexit and the EU Budget on 4 March 2017. In this document they state that "under EU law if there is no withdrawal agreement Article 50 allows the United Kingdom to leave the European Union without being liable for outstanding commitments, but the political and economic consequences of doing so are likely to be profound."[135] Under the rules of public international law, if making no payments regarding its non-binding financial commitments the United Kingdom could easily targeted by other member states in form of cases. Unreliability could be easily stamped on the head of the United Kingdom, caution is advised how the country will be seen on the whole international spectrum.

The words of Mr. Geoffrey Cox, the Attorney General should be taken also into

[134] Keep, Matthew: *Brexit: the exit bill, Briefing Paper Number 8039,* 22.
[135] Keep, Matthew: *Brexit: the exit bill, Briefing Paper Number 8039,* 25.

account: "The position on money is this. The view of the Government, and my view, is that we would have obligations to pay a certain amount of money were we to leave the European Union without a deal. The House of Lords European Union Committee concluded that there would be no obligation under EU law. That is a stronger argument—not necessarily an incontestable one—as to our obligations under EU law, but the Committee also concluded that we might have obligations under public international law, and with that I agree. There is an argument that we would not have an obligation under public international law, but it is an argument unlikely to be accepted by any international tribunal. My view is therefore that we would owe a presently unquantifiable sum were we to leave the European Union without a deal. It is impossible at this stage to say how much. It is true that the European Union is not a member state and is not a state, and therefore it is unable to take the case to the International Court of Justice. It might therefore be difficult to enforce the public international law obligation that existed. However, I ask the House to reflect on the fact that if this country, acknowledging that such obligations probably exist or do exist, did not pay them, it would be likely to cause the deepest resentment, just as it would to any of us who were unpaid a debt. If we leave a club, we pay the bar bill. If we do not pay the bill, we are not likely to get a lot of consideration from the other side."[136]

## Conclusions

Despite being a mainstream issue, we could easily mark the financial settlement as the most straight up Brexit issue. It is clear that the referendum campaign supporting the leave was based on at one side paying enormous amount toward the European Union, but the detailed, and thanks to its development, the well-based budgetary and financial system is transparent.

Being a mainstream issue does not always mark its complexity. As mentioned the highlighted areas are mostly important from the European Union side.

The question remains, whether the United Kingdom is to leave the European Union, or not, and in case of exiting will a withdrawal agreement to be reached or a no deal scenario will take place.

The questions arising from the financial settlement enable us to peek inside in a specific area of the Brexit. Also this makes it possible to review how the European Union finances work and which budgetary mechanism are in place.

Another possibility is the viewpoint of the possible withdrawal intentions is to draw up two groups, the net contributors and the net beneficiaries. The United Kingdom being part of the first group could stand on its own legs, but being part of the latter is a significant warning sign not to engage any withdrawal intentions.

A complex issue was detailed in a simplified way as it could be, for an easier understanding. As it suggests, any arising issues are subject to the international law too. Any member state withdrawing has to face an enormous amount of issues. Would Brexit be a perfect opportunity for the European Union to scare off any intending member state from a withdrawal? I do not think that any net beneficiaries would take risk, and there shall not be another net contributor to have such intentions.

[136] https://hansard.parliament.uk/commons/2018-12-03/debates/67B4BC40-0578-417D-9467-F737BDD5079C/WithdrawalAgreement LegalPosition (2 February 2018)

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# REGULATION OF JOINT-STOCK COMPANIES IN THE 19TH CENTURY HUNGARY

**Emőd VERESS***

**Abstract**

*The article traces the historical development of the regulation of the joint-stock company in Hungary, beginning with the early 19th century when this type of company was first attempted to be regulated and until the 1870s, when fully new norms in line with Western regulations of the period were adopted. We document the beginnings of regulation in the field of joint-stock companies, demonstrating that the first successful attempts at such regulation coincided with the start of the industrialization process of Hungary in the 1840s. The joint stock company was a necessary tool for economic development, especially after the Austro-Hungarian compromise in 1867. It is ascertained that the first Act dealing with joint-stock companies in 1840 already contained the basis for the successful functioning of such companies, by regulating public subscription, voting rights, how statutes were established and the payment of dividends. The modernization of the joint-stock company in the 1870s and through later norms paved the way for the general use of bearer shares and established how capital is concentrated for the creation of the company. It also ushered in the possibility for shares to be easily exchanged, thereby responding to the joint-stock boom which followed the Austro-Hungarian compromise in 1867. In conclusion, the regulation developed in the examined period withstood the test of time, being applied until the establishment of the Soviet-type dictatorship at the end of the Second World War.*

**Keywords:** *joint-stock companies in Hungary, 19th century legislative reforms, legislation as a tool for economic development, shares*

## 1. Introduction. The advent of joint-stock companies

The existence of the West-East *economic slope* is a historical fact in 19th century Europe: due to the complex factors of historical conditions, from the advanced West to the East of Europe, the economic development (especially high-scale trade and industrialization) was lower, which can even be evidenced by statistics.[1] This phase shift was even more pronounced as we moved gradually towards the East, also evident from the foundation of *joint-stock companies*, which were the great invention of corporate law in modern history. The joint-stock companies, as organizational

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[1] For the theoretical and empirical background of the economic backwardness, see: Alexander Gerschenkron, *Economic backwardness in historical perspective*, Cambridge, Massachusetts, 1962; Iván T. Berend, György Ránki, *Economic Development in East Central Europe in the Nineteenth and Twentieth Centuries*, New York, 1974; Iván T. Berend, György Ránki, *East Central Europe in the Nineteenth and Twentieth Centuries*, Budapest, 1977; Iván T. Berend, György Ránki, *The European Periphery and Industrialization, 1780-1914*, Cambridge, 1982; Ivan Berend, *An Economic History of Nineteenth-Century Europe: Diversity and Industrialization*, Cambridge, 2013; Tamás Szentes, *The Political Economy of Underdevelopment*, fourth, revised and enlarged edition, Budapest, 1983 etc.

structures based on the limited liability of the shareholders, freely transferable shares and on a gradually evolving separate legal personality, in Central and Eastern Europe emerged with a significant delay as compared to the establishment of the first British or Dutch companies of this kind (in 1600 and 1602, respectively). In Germany, the first joint-stock company was incorporated in 1750 (Frederick the Great"s Asiatic Company, with the full name *Königlich Preußische Asiatische Compagnie in Emden nach Canton und China*), while this happened in Austria only at the end of the 18th century. These dates are noteworthy because they show the correlation of the level of economic development and the appearance of joint-stock companies, confirming the hypothesis according to which further to East we go, later we will witness the emergence of this form of economic organization.[2] Hungary was no exception either; the West-East economic slope was present here as well, since the first joint stock companies were established in the first half of the 19th century. The East-Central European states, generally by this legislative modernization, did not follow the time-consuming path of organic development, but often adapted and developed the most advanced western models, therefore the essence of the processes was accelerated modernization. In the case of Hungary, in the last decades of the 19th century, joint-stock companies were frequently used for very different business purposes, as the process of economic caching up proved to be – with certain limits – successful, at least until the First World War interrupted these positive processes.

### 1.1. Codification attempt: Codex Cambio Mercantilis Pro Regno Hungariæ

Generally, in Hungary, companies were meant to be created by commercial law codification attempts. These efforts at regulation also indicate that the development of company law in Hungary is very different from that in Western Europe. In Western Europe, company law evolved and intensively developed as a result of an organic development that was required by the needs of the economy already at the end of the Middle Ages and in the modern era. In the regions whose development was belated due to the historical circumstances, including Hungary with a predominantly agricultural economy, the companies were meant to be created through legislative reform, in the context of a top-down modernization experiment.

In 1779, the Royal Curia was commissioned to elaborate an act on commerce and bills of exchange. The draft was prepared by 1786 and the second part also contained rules of company law. This proposal was submitted to the National Assembly that was convened after a long break as late as 1791 by Leopold II (Holy Roman Emperor and King of Hungary from 1790 to 1792). However, the National Assembly was not able to discuss the proposal and the topic was subjected to the effect of Act LXVII of 1790/91, which prescribed that "for the regular handling of those public policies and judicial matters and other topics which could not be accomplished by the National Assembly, committees will be set up and commissioners will be appointed."

The proposal (entitled *Codex Cambio Mercantilis Pro Regno Hungariæ Partibusque Eidem Adnexis In Tres Partes Divisus Per Regnicolarem Juridicam*

[2] See Sándor Tamás, *Jegyzetek a részvénytársaság új szabályozásához (Notes for the New Regulation of Joint-Stock Companies)*, Gazdaság és Jog, 2014/4, p. 17.

*Deputationem Articulo 67. 1791. ordinatam elaboratu*) of the commercial committee was submitted to the National Assembly in 1795. However, the proposals of the committee were not discussed and thus not accepted either. The reform processes halted for several decades because of the death of Leopold II, the inflexible absolutism of his successor Franz I (who reigned from 1792 to 1835) as a reaction to the French Revolution, which became more and more radical, and to the Jacobin movement led by Ignác Martinovics. The proposal was published in Pozsony (currently Bratislava, Slovakia) in 1802.[3]

### 1.2. Attempts at establishing joint-stock companies

Despite the difficulties of regulation, attempts were made at establishing joint-stock companies but these attempts either halted in the planning phase or in some later phase of the process of establishment, for some reason (for example, for the lack of capital), or perhaps the company whose establishment was started only pursued activities of local significance. The *Gács-based textile plant* (fine fabric manufacturer) established by the family of the Count Forgách, which tried to issue shares around 1800; the *plan for the Northern Wine Export Company* (1802); the *Révkomárom Ship Insurance Company* (1808); *the plan for the Hungarian National Joint-Stock Company* aimed at promoting tobacco trading (1826)[4] should be mentioned. The first joint-stock company that could be called successful or at least functional and which pursued its activities in Hungary, the *First Danube Steam Ship Joint-Stock Company* (1830) had its seat in Vienna.[5]

### 1.3. A new attempt at codification: Codex Cambio-Mercantilis eiusdemque Ordo Processualis

The codification efforts resumed in the first half of the 19th century. This is also the era of the development of romantic culture, which played a key role in building the nation. Through Act VIII of 1827, the title of which suggests that "further discussion of the regular efforts of the committees are postponed to the next session of the National Assembly," also relying on the results of the previous codification attempt,[6] a new draft commercial code entitled *Codex Cambio-Mercantilis eiusdemque Ordo Processualis* was prepared, which was not adopted either, but which was published in a printed form both in Pozsony and Buda in 1830. This was the last proposal for commercial regulation prepared in Latin. The national awakening also involved the strengthening of Hungarian as a legal language (the Curia adopted its decisions in Hungarian from 1830, and from 1834, the knowledge of Hungarian became the condition of holding public offices and pursuing legal practices).

To sum it up briefly, differently from how it happened in Western Europe, the advent of joint-stock companies in Hungary happened in the context of nation-building and the Reform Age, when the dissolution of feudalism, the bourgeois transformation and the emergence of capitalist production gave the context. The economic thinking of the Reform Age generation was defined by such tenets that were worded by Lajos Kossuth:

[3] Posonii, typis Franc. Jos. Patzko.

[4] See the details in Horváth Attila, *A részvénytársaságok és a részvénytársasági jog kialakulása Magyarországon (The Evolution of Joint-Stock Companies and Joint-Stock Company Law in Hungary)*, Budapest, 2005, p. 111-114.

[5] Horváth (2005), pp. 122–125 and Galgóczy Károly, *Cs. kir. szabadalmazott első dunagőzhajózási társaság (Imperial and Royal First Proprietary Danube Steam Boat Company)*, Statistikai Közlemények 1863/1, pp. 59–73.

[6] Papp Tekla, *Társasági jogalkotásunk rövid története, európai kitekintéssel (The Brief History of our Company Law Regulation, with a European Overview)*, in: Ünnepi tanulmányok Sárközy Tamás 70. születésnapjára (Festive Studies for Tamás Sárközy"s 70. Birthday), Szeged, p. 265.

"the contribution that a thriving industry makes to the greatness and happiness of the nation is bigger and more important than any conquests achieved with arms […] industry conquers misery with the grace of peace, to achieve public happiness."[7] It was written in the Hetilap newspaper in 1845 that "the economic facts are progressed further, politics only follows them; the cause lies in the economic facts, politics is only a consequence. The economic facts give orders, and politics is obliged to obey."[8]

## 2. Joint-stock companies as the key factors contributing to the economic development of the 19th century

### 2.1. The role and significance of István Széchenyi in introducing the idea of joint-stock companies in Hungary

Count István Széchenyi (1791-1860), a key political and economic thinker of the period, wrote the following in his book entitled *Hitel (Credit)*, published in 1830: "It is not true, or at least not believable that a foreign citizen would make huge sacrifice for Hungarian institutions without having a hidden and additional purpose; and thus, only Hungarians can be expected to make genuine contributions to such matters which bring moral rather than financial gains. So will a Persian, Spanish or Chinese investor be happy to see the progress of Hungary if he gets no returns from his sacrifice and the dividends that he receives from his shares will be nothing more than moral happiness? This would contradict nature and everybody who works for a higher purpose and with pure intentions will only do so for their homeland."[9] The national feeling may be the foundation for making a sacrifice. However, Széchenyi regarded gaining profits and dividends as a legitimate purpose as well, and he considered the national feeling and obtaining profits compatible. He acted in this spirit, playing an essential role in the establishment of several joint-stock companies. Széchenyi was the pioneer of the idea of joint-stock companies in Hungary.

István Széchenyi played a crucial role in the building of the *Chain Bridge*. According to Act XXVI of 1836 on the construction of a permanent bridge between Buda and Pest, "the construction of a permanent bridge between Buda and Pest will be the responsibility of a joint-stock company" (Section 1). In other words, the capital required for the building of the Chain Bridge was to be secured by the establishment of a joint-stock company. The consideration for the investment, the revenues of the joint-stock company distributable as dividends were planned to be covered from the tolls to be collected for the use of the bridge. The years of collecting tolls were defined by the contract entered into with this joint-stock company, while the law said that "after the terms and conditions of the contract to be entered into with the joint-stock company expires, the permanent bridge between Buda and Pest will immediately become the property of the Nation" (Section 7).[10] The law focused on the construction of the Chain Bridge rather than on the elaboration of the organizational and operational rules of the joint-stock

[7] Kossuth Lajos, *Zárszó az Iparegyesületi Ünnepély alkalmával (Closing Speech on the Ceremony of the Industrial Union)*, Életképek 1844/9, p. 295.

[8] Hetilap, 17.10.1845, issue 58, p. 914.

[9] Széchenyi István, *Hitel (Credit)*, in: Széchenyi István válogatott művei. Első kötet (Selected Works of István Széchenyi, Volume I), Budapest, 1991, p. 280.

[10] The right to collect tolls for the use of bridges was originally provided for 87 years, but it was exercised only for two decades, as the bridge was redeemed by the state under Act XXX of 1870.

company. The bridge was erected, and it was delivered to the public in 1849.[11]

The *Pest Roller Mill Company* (1838), which was founded by Széchenyi, was also one of the first joint-stock companies.[12] According to a historical synthesis published in 1890, the main problem was the difficulty, or rather, the impossibility of creating a broader market arising from the underdeveloped public transportation. The product of mills, i.e., flour cannot bear high transportation costs without losing its competitiveness. However, when the Pest roller mill was designed, there were no railways and public roads were in such a miserable condition that all traffic halted when the weather was unfavorable. In such circumstances, of course, no significant business transactions could be anticipated within the borders of the country and exports to other countries were out of the question. Other difficulties resulted from the lack of capital and entrepreneurs. Széchenyi was the person who managed to obtain both missing factors, although only partially from Hungarian resources. Half of the capital and the head of the company were provided from abroad, and what is more, experienced labor force had to be brought from abroad too. Also, the foundation of the first Pest steam mill also had a local obstacle. The millers, whose livelihood was threatened, managed to organize a rather strong party in the management of the city, which was able to prevent the mill from acquiring a suitable plot of land. Palatine Joseph [1776-1847] had to interfere with averting this obstacle and with ensuring that the new company received a plot of land, for a very high price.[13]

### 2.2. The Hungarian Commercial Bank of Pest

The *Hungarian Commercial Bank of Pest* was established explicitly on a contractual basis and based a royal charter of privileges. The granting of this privilege was requested as early as 1830. However, the charter was only issued as late as 1838. The bank, due to resistance from the imperial administration, could only be founded on October 14, 1840 (it was then that King Ferdinand signed the memorandum of association of the Bank) and it started its operation in 1841.[14]

According to the Latin language charter, the emperor ordered the following: "we strictly order to Hungary and its attached regions, to our faithful subjects of any rank or office, who became familiar of this letter in any way whatsoever, that they should not disturb or hinder the above-mentioned company in its financial institutions to be established and maintained, either publicly or privately."[15] It is evident that the first modern Hungarian bank and one of the first Hungarian joint-stock companies were established by applying the technique of royal charters, which was of medieval origins and which had been obsolete in Western Europe at that moment.

[11] See the details in Horváth (2005), pp. 125–132.

[12] Horváth (2005), pp. 133–137.

[13] *Emlékirat a Pesti hengermalom-társaság fennállásának félszázados évfordulója alkalmából, (Memoir on the 50th anniversary of the establishment of the Pest roller mill company)*, Nemzetgazdasági Szemle, 1890, p. 356.

[14] Cf. Pólya Jakab, *A Pesti Magyar Kereskedelmi Bank keletkezésének és ötvenéves fennállásának története (The History of the Evolution and Fifty Years of Operation of the Hungarian Commercial Bank of Pest)*, Budapest, 1892; Lamotte Károly, *A Pesti Magyar Kereskedelmi Bank 1841–1941 – Száz esztendő emlékei (The Hungarian Commercial Bank of Pest 1841–1941, Memories of a Hundred Years)*, Budapest, 1941; Botos János, *A Pesti Magyar Kereskedelmi Bank története (The History of the Hungarian Commercial Bank of Pest)*, Budapest, 1991; Holbesz Aladár, *A magyar hitelszervezet története (The History of the Hungarian Credit Organization)*, Budapest, 1939, p. 41-46; Horváth (2005), pp. 141–145.

[15] Lamotte (1941) (the book contains no page numbers).

## 3. The key provisions of Act XVIII of 1840

### 3.1. Commercial codification in 1840

The general rules regarding joint-stock companies were first laid down by Act XVIII of 1840 on the Legal Relations of General Partnerships.[16]

As a result of the intellectual movements of the Reform Age, and relying on the above-mentioned codification achievements, the complex legislation aimed at the catching up of the economy was completed by 1840. It was at that time that Act XV of 1840 on the Bills of Exchange was introduced,[17] as well as Act XVI of 1840 on Tradesmen, Act XVII of 1840 on the Legal Relations of Factories, Act XVIII of 1840 on the Legal Relations of General Partnerships, Act XIX of 1840 on Tradesmen"s Boards and Brokers, Act XX of 1840 on Haulers, as well as Act XXII of 1840 on Bankruptcy.[18] The majority of these acts are actually "simple translations of the relevant Austrian provisions."[19] It was Vienna-based lawyer *Ignaz Wildner* (1802–1854) who participated in the elaboration of these laws.[20]

During the National Assembly session of 1839/1840, Wildner attended a luncheon in Pozsony (currently Bratislava), which was held by György Andrássy. It was here that he said that he now has a completely different view of Hungarians than how they were described to him at the time of his departure from Vienna, and then he pictured the life of Hungarians based on the attacks of the paper Allgemeine Zeitung. This confession inspired the attending István Széchenyi to improvise and present a draft four-scene comedy, in the first scene of which Wildner receives instructions to beware of the leaders of the opposition from Prince Metternich and Police Prefect Count Sedlnitzky. In the second scene, Wildner finds the Hungarians loveable persons when attending a luncheon and when they introduce themselves to him, he realizes that these are the very persons (Deák, Beöthy, Bezerédi and Klauzál) who had been described to him as ignorant and man-eating beasts when he was prepared for the mission. In the third scene, Wildner is in a friendly relationship with the leaders of the opposition but he also betrays them. In the fourth scene, Wildner returns to Vienna after accomplishing his mission, where his friends are happy to see that he escaped from the land of robbers, maneaters and rebels, while others convict him and accompany him to prison because he made friendships with Hungarian liberal thinkers.[21] By the way, Ignaz Wildner was granted the title of a Hungarian nobleman for his codification activities.[22]

[16] Cf. Pókecz Kovács Attila, *Schaffung der Handelsgesetze von 1840 durch die ungarische Nationalversammlung und deren Anwendung bis 1849*, Jura 2011/1, pp. 117–127.

[17] See the details in Balogh Elemér. *Császár Ferenc szerepe a magyar váltójog kifejlődésében (The Role of Ferenc Császár in the Development of the Hungarian Law on Bills of Exchange)*, Jogtörténeti Szemle 2011/2, pp. 1–9.

[18] The effect of these rules did not extend to Transylvania.

[19] Holbesz (1939), p. 43.

[20] Sárközi Zoltán *A kereskedelmi jogalkotás kezdetei és a részvénytársasági törvény kialakulása Magyarországon (The Beginnings of Drafting Commercial Laws and the Evolution of Joint-Stock Company Law in Hungary)*, Jogtudományi Közlöny 1988/9, p. 525.

[21] Bártfai Szabó László, *Széchenyi ismeretlen első szatírája (Széchenyi"s First Unknown Satire)*, Magyar Bibliofil Szemle 1924/3–4, pp. 181–182.

[22] Act LII of 1840: »Taking into account the outstanding merits and services done in military and civil careers, the Estates of the Country have accepted (Section 1) the Austrian nobleman, legal scholar, Vienna-based Royal Court and Metropolitan Court lawyer Ignaz Wildner into the ranks of the naturalized noblemen of the Country, with his statutory descendants…«

**3.2. The concept of a joint-stock company**

Act XVIII of 1840 defines joint-stock companies as follows: "such companies in which neither member is specifically mentioned in the title and the total amount of corporate funds is divided to a certain number of shares of equivalent value, the shareholding members only risk the money that they have paid for the shares and they are not held liable with any other property of theirs in any case. These companies are called joint-stock companies (Actien–Geschellschaften)."

The law started out from the basic principle of the freedom of establishing joint-stock companies: everyone is free to acquire shares and join a joint-stock company without any restriction whatsoever (Section 54). This short act is by far not an exhaustive regulation of the joint-stock companies, it hardly indicates the main principles but it has the merit of wishing to promote the forming of joint-stock companies with its liberal measures, as a result of which it consistently disregards all kinds of unnecessary formalities and guardianship kind of supervision, it only wishes to protect the public from fraudulent company establishments.[23]

**3.2. The establishment of joint-stock companies**

Those who wish to establish a joint-stock company were obliged to submit the following written documents to the commercial tribunal (Section 55):

a) The purpose of the company to be established and those data on which the possibility of achieving the goal of the company rests – clearly distinguishing between the certain from the probable and the uncertain;
b) The approximate calculation of the necessary amount of capital;
c) The preliminary registration of the number of the shares, the date of their payment, the method of their distribution, i.e. the share plan, in which the following should also be indicated: "whether the founders intend to assign any part of the overall amount of shares to the public, and if so, what amount exactly, through public subscription."
d) The preliminary statutes of the company. "After having deposited these official deeds with the commercial tribunal, everyone shall have the right to review them." "The founders may not change the already submitted preliminary statutes in their own power" (Section 57). "Any and all – subsequent – changes to the statutes are to be registered with the commercial tribunal" (Section 65). "The accepted statutes shall be sent by the competent commercial tribunal to all the other commercial tribunals in copies and the free review thereof shall be allowed" (Section 62). Quoting István Széchenyi: "The guardian angel and bright ray of sunshine of a credit is publicity."[24]
e) If the joint-stock company to be established was not purely a trading company, or if the intention was to establish a (public interest) company subject to the Act XXV of 1836[25], it was required to present

[23] Vargha Gyula, *A magyar hitelügy és hitelintézetek története (The History of Hungarian Credits and Credit Institutions)*, Budapest, 1896, p. 79.
[24] Széchenyi (1991), p. 261.
[25] Act XXV of 1836 on the Private Companies that Increase the Public Assets and Trading of the Country.

the deeds to the Royal Council of Governor.

As long as there was a public subscription to shares (public offering), the law provided as follows: "shares are sold through subscription under public supervision, which subscription should remain open for at least three days, and the shareholders should be convened for a general meeting." (Section 58). In the statutory general meeting, the company "constitutes itself (constrituirt sich), the preliminary statutes are read out, the final statutes are determined, a board is assigned for the opening and management of the cash desk, if it is regarded necessary by the company, a company manager (Firmaführer) can be elected, and the board will be specifically authorized to get the statutes and the specimen signature registered. All these will be decided by the majority of votes cast by the attendants of the meeting" (Section 58). This means that the corporate governance structure of the company was based on the managing bodies of the company, the board and optionally the company manager, while the main company organ was the general meeting.

According to the law: "before such formation of the company, the founders may not require any preliminary payments for the shares in any case whatsoever. It is also forbidden to pay interests on the shares from the funds that are preliminarily paid by the shareholders for their shares" (Section 59). "The company shall pay the founders preliminary costs, and as long as these are sufficiently proven, these shall be paid immediately, unless it is otherwise provided by the statutes" (Section 63).

### 3.3. Protection of statutes and of minority shareholders and the prohibition of bearer shares

The board was forbidden by the law to diverge from the statutes: "the board shall not diverge from the statutes, or determine rules binding for the company without a specific authorization, which can only be done by achieving a majority vote in the general meeting of the company" (Section 64).

Similarly, the scope of the company could only be changed on the basis of a general meeting decision, with a three quarter majority, while the minority shareholders could exit the company, maintaining their claim for the payment of "the shares of the company at the time in question, and if there were any profits, the proportionate part of such profits."

The *issuance of bearer shares was prohibited* by law: "no such shares which are not for a certain name (au porteur) shall be issued" (Section 56).[26]

The law also used the method of maximizing votes and in consequence tried to exclude the "tyranny" of majority shareholders by legal tools: "in the general meeting of the company, each member will have one vote for each full share, however, they cannot have more than ten votes in any case whatsoever, however many shares they should possess" (Section 60).

It was mentioned as a deficiency of the law that it did not impose any sanctions for frauds, "although the legislators, or at least some of them should have known how complicated frauds had taken place abroad for a long time."[27]

[26] For the current prohibition of bearer shares in Hungary see Emőd Veress, *Report from Hungary: Is It Possible to Issue Bearer Shares in Hungary? Remarks on Mandatory and Default Rules in Hungarian Company Law*, European Company Law 2019/3, pp. 95-100.

[27] Rónay Károly, *Részvényjogunk vajúdása (The Labor Pains of our Shares Law)*, Királyi Közjegyzők Közlönye 1933/4, p. 112.

## 4. First Hungarian Savings Bank of Pest

It was on the basis of this regulation that the first Hungarian Savings Bank of Pest, which was founded in 1839, was transformed into a joint-stock company in 1845 at the initiative of the lawyer, writer and politican András Fáy (1786-1864). Its reorganization into a joint-stock company was proposed by Lajos Kossuth (1802-1894), later Governor-President of the Kingdom of Hungary during the revolution of 1848–49.

Saving banks were established before 1840 for philanthropic purposes, as associations, for example, for the reduction of usury. The *General Savings Bank of Brassó* that was established at the initiative of an official of the Vienna Chancellery, later the Councillor of the City of Brassó (currently Brașov, Romania, in German: Kronstadt), Peter Lange (1797-1875) was the first such savings bank. "This institution, which was founded on the basis of a German example and followed philanthropic principles, remained relatively small and isolated, also due to geographical reasons."[28] Despite this fact, the General Savings Bank of Brassó was Hungary"s first independent financial institution. "Brassó has been the first trading and industrial city of Transylvania for a long time. Its population exceeded 18 thousand as early as 1786 and its hardworking and well-to-do German inhabitants, who were always very open to the cultural impacts coming from their Western language relatives, were very willing to welcome the savings associations."[29] After 1840, the Hungarian savings banks were generally established in a joint-stock company form but such institutions of the Transylvanian Saxons in Brassó and Nagyszeben (currently Sibiu, Romania, in German: Hermanstadt) preserved their associative (non-commercial) form.[30]

It was this origin as an association that has led to that in the case of most of the savings associations organized as joint-stock companies, each shareholder, irrespective of the number of their shares, had only one vote at the general meeting. However, some savings associations used the opportunity that the number of votes was maximized in ten by Act XVIII of 1840, therefore they planned their statutes in such a way that they could ensure more than one votes for the shareholders. For example, at the Győr Savings Bank joint-stock company, those shareholders who held 1-4 shares had one vote, those who owned 5-9 shares had two votes, while those who had more than ten shares had three votes.[31] By this approach a specific tool of minority shareholders protection was created.

## 5. Joint-stock company foundation fever

The regulation created the legal frameworks for the foundation of joint-stock companies. In the press, news like the following appeared one after the other: "In Nagyszeben, Ferencz Czinege, who is famous for his knowledge of engineering techniques and chemistry, intends to set up a grandiose leather company through

[28] Tomka Béla, *A magyarországi pénzintézetek rövid története 1836–1947 (The Brief History of Hungarian Financial Institutions 1836–1947)*, Budapest, 2000, p. 9.

[29] Vargha (1896), p. 84.

[30] See the details on these saving banks in Egry Gábor, *A brassói és nagyszebeni Általános Takarékpénztár korai történetének néhány jellegzetessége - 1835–1848 (Some Characteristics of the Early History of the Brassó and Nagyszeben General Savings Banks - 1835–1848)*, Századok 2002/6, pp. 1261–1293.

[31] Vargha (1896), p. 111.

shares."[32] In 1864, based on the decree issued by Austrian emperor Franz Joseph I, the *Pest Commodities and Stock Exchange* was founded, whose purpose, according to its statutes, was the following: "the selling and buying of all kinds of commercial goods, bullion (gold and silver), currencies and bills of exchange, shares and bonds issued by Hungarian industrial companies based on high-level permits, aimed at facilitating pledge, insurance and shipping transactions." Its first president Frigyes Kochmeister (1816–1907) managed the institution for more than three decades.

However, the thriving of joint-stock companies genuinely began in Hungary only after the Austro-Hungarian Compromise of 1867, which closed the period of absolutism that followed the 1848-49 revolution with final effect. In 1868, the press wrote about a share fever, and the period that followed the Austro-Hungarian Compromise was named *Gründerzeit*, which can be translated as a fever to establish companies. As a pasquinade stated in 1868:

"Nulla dies sine linea! In Hungarian, this means that there is no day in Buda-Pest without the emergence of a new joint-stock company. What is more, sometimes the fertile mother of joint-stock companies, which is the desire to speculate and profiteer, gives birth to two born-alive infants on the very same day. We only have a few more weeks to go before we see joint-stock companies satisfy all kinds of needs from the cradle to the grave […] The birth of a new company is very easy. If two or three people drink a glass of wine or beer together, this company of people will immediately transform into a founding board […] Of course, a competitor for each joint-stock company appears right away. The founders become directors and management councilors, their relatives and other protégées are given well-paying positions. The first general meetings will probably promise high dividends, which can be expected in the future. In the meantime, the shares continue circling around and they end up in the hands of ordinary people, where they will stay. The whole world, even the simplest cartman hopes for bright dividends, dreams of millions of Forints, which will just flow to their wallets without anything to be done by the shareholder, during his sleep […] Imagination runs wild; the desire to become rich quickly without any effort is spreading like a stain on a fabric; whole classes of the society suffer from the share fever […]"[33]

However, it should be stated that the legislation has produced such results due to the favorable political and economic circumstances created by the Austro-Hungarian Compromise in the setting of a general economic development.

## 6. Legal modernization: Industry Act and Commercial Act in the 1870s

The Industry Act VIII of 1872 terminated the operation of *guilds*, while the Commercial Act XXXVII of 1875 modernized the regulation of joint-stock companies based on the German example.[34] The model for the Hungarian Commercial Act was provided by the General Commercial Code of the German States of 1861, the *Allgemeines Deutsches Handelsgesetzbuch (ADHGB)*, which was also taken over by Austria as the member of

[32] Hetilap, 15.07.1845, issue 31, p. 494.

[33] Vasárnapi Újság, year 15, issue 27, July 5, 1868.

[34] On the circumstances of the adoption of the Commercial Act, see Horváth Attila, *A kereskedelmi törvény - 1875. évi. XXXVII. tc. (The Commercial Act no. XXXVII of 1875)*, in: A kettős monarchia (The Dual Monarchy), Budapest, 2018, pp. 203–245.

the German Confederation (Deutscher Bund) in 1862-63. Professor István Apáthy (1829–1889) played a vital role in the elaboration of the draft. However, the Commercial Act was not a servile copy but a flexible adaptation of the ADHGB. This was also visible in the regulation of the joint-stock companies:

Regarding the definition of the organizational structure of joint-stock companies, there is a striking difference between the ADHGB and its Austrian version on one hand, and the Hungarian legislation on other hand. This first shows in the size of legislation. The ADHGB contains a total of 43 sections in Part 3 norms regarding the joint stock company, while there are 63 sections in the tenth part of the Hungarian version on the same subject. The differences in content are even more conspicuous. Between the emergence of the two commercial regulations, between 1861 and 1875, significant changes took place in the development of European capitalism. It is a rather well-known fact that after the Austro-Hungarian Compromise of 1867, then the Franco-Prussian War of 1870-71, a large-scale company establishment fever began in Hungary on the one hand, and in the territory of the German Empire, on the other hand. The operational frameworks defined in the ADHGB of 1861, which reflected conditions that were outdated by that time, proved to be too narrow in several aspects, by taking into account the lessons learned from the 1873 over-production crisis. This is why the statutorily regulated organizational structure of joint-stock companies in Hungary is much more complex and many-sided compared to the requirements of the ADHGB.[35]

### 6.1. The concept of a joint-stock company

Pursuant to the Hungarian Commercial Act (hereinafter referred to as: CA), "those companies are regarded as joint-stock companies which are established with a capital that consists of predefined and equivalent value shares of a certain number (complete or part) and where the holders of the share are only held liable up to the value of their shares" (Section 147 of CA).

This statutory definition was criticized with reason, as it is not sufficiently accurate: the holders of the shares are liable to the company for the complete payment of the consideration of their shares. However, they are not held liable for the debts of the company. In the legal literature of the time, it was emphasized that Act XVIII of 1840 also worded its text more accurately when it stated that in the joint-stock companies, the shareholding members only risk the money that they have paid for their shares and they are not liable with any of their other property in any case whatsoever.[36]

The nominal value of the shares could not be increased during the existence of the company. Such increase was regarded invalid.

### 6.2. The foundation of a joint-stock company

According to the CA, a joint-stock company can be regarded as established if 1. its capital is provided; 2. the company"s statutes have been elaborated, and 3. the company was incorporated in the trade register (Section 149).

During subscription, if no higher amount of payment was stipulated in the draft, 10% of the nominal value of each subscribed share is to be paid in cash in the

[35] Sárközi (1988), p. 526.

[36] Mutschenbacher Viktor, *A kereskedelmi jogtudomány elemei a magyar kereskedelmi törvénykönyv szabályaihoz alkalmazva (The Elements of Commercial Law adjusted to the Rules of the Hungarian Commercial Code)*, Pécs, 1884, p. 238.

value defined in the draft. The subscribers or their legal successors cannot be obliged to make any higher payments than the value that is stipulated in the law or in the draft before the statutory general meeting is held. Any contrary share subscription shall be deemed invalid. For incorporating the company, at least 30 percent of the nominal value of the shares had to be actually paid. What is equally important, the joint-stock company was not allowed to issue new shares before the full payment of the originally issued shares. The new shares issued prior to full payment were invalid and their issuers had joint responsibility with all their property for any and all damage arising from the issuance of the shares. Otherwise, they were not obliged to make any other contribution to the purpose and the obligations of the company but the payment of the nominal value of the shares defined by the statutes (Section 168). Those shareholders who failed to realize the payments for their shares in due time were obliged to pay late interests based on the law.

The company was free to stipulate a certain amount of penalty in the statutes in the case of missed payments, irrespective of the other statutory consequences, or to declare that the defaulting shareholders will lose their rights arising from the subscription to the shares and the effected payments (Section 169). If the share was annulled due to the missed payment, the subscriber to the share was still held liable up to 50% of the nominal value of the subscribed shares (Section 171).[37]

The initial subscribers remained liable for a value up to 50% of the subscribed shares even if the shares were passed on by observing the law and the statutes.

The statutory general meeting had to be held within two months from the closing time of the subscription to the shares. If the general meeting was not convened in these two months, or the subscription to the shares remained unsuccessful, the subscribers could claim back their contributions without any deductions. It was the joint and several obligation of the founders to refund these contributions. Otherwise, the shareholders could not reclaim the amount that had been paid and during the existence of the company, the shareholders could only claim the amount of the pure profits which were distributed among the shareholders based on the statutes.

At the statutory general meeting, each subscribed share was worth one vote, but no one may have more than ten votes. The statutory general meeting had quorum if at least seven subscribers who represented at one-quarter of the capital were present at the meeting either in erson, or through a representative.

### 6.3. The transferability of shares

The transferability (negotiability) of the securities, i.e., of the shares that were issued as the consideration for the contribution to the formation of the company"s capital is a key characteristic feature of a joint-stock company.

The holder of the share made his funds available to the joint-stock company with final effect by having bought the shares, funds which cannot be redeemed, only the shares can be sold to someone else. The economic advantage of the shares is in their very marketability. The share as a tool for capital placement may have attractive power for the public in two ways. On the one hand, if the company fulfills the hopes attached to

[37] However, the shareholder was protected by the rule that the claims of a shareholder could only be declared terminated if the announcement on payment was displayed by the closing deadline indicated in the statutes, and announced at least three times in a determined gazette and the last time that there was such announcement, it was displayed at least four weeks prior to the final deadline for payment (Section 170).

it, then it will bring profits through the paid dividends. On the other hand, the changes in the prices of the shares also mean a significant attractive power for speculation.[38]

### 6.4. The number of shares

The number of issued shares had to be indicated in the statutes of the joint-stock company. The number of shares was not defined by the CA, but at least seven subscribers were required by the law. Therefore, the company had to issue a minimum of seven shares. Also, the CA *did not set a minimum capital requirement*, nor did it provide on a minimum nominal value.

### 6.5. Registered and bearer shares

It was allowed by the CA to define in the statutes whether the shares were *registered or bearer* shares. The CA it made possible to issue bearer shares, differently from the earlier regulation. The assignment of bearer shares was realized by handing over them (Section 172). In the Hungarian law, the issuance of bearer shares was prohibited by Act XVIII of 1840 but the rules set out in the CA still did not count as a novelty: after 1869 several laws made it possible for railway joint-stock companies to issue bearer shares.[39] A company under the regime of CA could have both registered and bearer shares at the same time.

In the case of registered shares, the assignment had to be entered in the share register by indicating the names and residential addresses of the shareholder. The shares could also be assigned with a blank endorsement, but the shareholder could be deemed certified with the company only in case that the assignment was entered in the share register by the presentation of the share, unless it was otherwise provided by the statutes. The ancient shareholder remained liable up to the amount of the outstanding nominal value of the registered share, despite the assignment, until the new shareholder was entered in the company register (Section 173).

It was established in the judicial practice that a provision in the statutes which excludes the assignment of registered shares, or one that would make sales practically impossible, or excessively burdensome, was invalid. The requirements regarding a transfer fee had to be defined in the statutes preliminarily, which could not be replaced by a simple decision of the general meeting. For example, it was invalid if the transfer fee was defined by the board of directors pursuant to the statutes. In another court decision, it was stated that the transfer fee should not exceed 20% of the nominal value of the share. These restraints had to be indicated in the share deed as well.[40] "However, those restrictions which only extended to a short time and which were imposed for a rational purpose were not made invalid. Such requirements often guaranteed the success of the company foundation. There were many such enterprises where the identity of the shareholders seemed to be an important aspect at the time of establishing the company, to ensure that in this critical moment, the company should have no malignant, bad-intentioned members. The validity of this restriction was defined in a maximum of five years."[41]

### 6.6. Capital protection requirements

The joint-stock companies were not allowed to acquire or pledge their own shares. In this respect, exceptions were

[38] Horváth (2005), p. 217.
[39] Horváth (2005), p. 219.
[40] Horváth (2005), p. 219.
[41] Horváth (2005), p. 220. See Curia decisions No. 45/1904, 1068/1903 and 1039/1904.

possible if the shares were acquired for the purpose of capital decrease (Section 161). If the members of the board of directors violated this rule of capital protection, they had joint liability towards the creditors of the company.

The shares could be issued for a particular person or to a bearer, but they could always be issued for a definite amount of money and were indivisible with regard to their holders. In those temporary shares or share vouchers which were issued before the full payment of the nominal value *the actually paid amount had to be clearly indicated* (Section 164).

It was prohibited by law that any interests or dividends be provided or paid to the shareholders from the capital. Only the pure profits that remained according to the annual balance sheet could be distributed to the shareholders. Despite of this, interest-bearing shares were acknowledged by the CA with a limitation. The law stipulated that it was possible to determine interests to the benefit of the shareholders for the period defined in the statutes as necessary for the preparation for the activity of the company, exclusively for the before starting the full-fledged operations (Section 165). The shareholders could not claim any dividends until supplementing the capital reduced by the losses.

## 7. Conclusion

A high number of joint-stock companies were established on the basis of the CA: for example, Ganz és Társa Villamossági-, Gép-, Vagon- és Hajógyár Rt (Ganz and Partner Electric Machinery, Wag on and Shipyard Joint-Stock Company), Hofherr-Schrantz-Clayton-Shuttleworth Magyar Gépgyári Művek Rt (Hofherr-Schrantz-Clayton-Shutthlewort Hungarian Machine Factory Joint-Stock Company), Gschwindt-féle Szesz-, Élesztő-, Likőr és Rumgyár Rt. (Gschwindt Spirit, Yeast, Liquor and Rum Factory Joint-Stock Company), Weiss Manfréd Acél- és Fémművek Rt (Weiss Manfréd Steel and Metal Works Joint-Stock Company), Wolfner Gyula és Társa Rt (Wolfner Gyula and Partner Joint-Stock Company), Goldberger Sám. F. és Fiai Rt (Goldberger Sám.F. and Sons Joint-Stock Company), Salgótarjáni Kőszénbánya Rt (Salgótarján Coal Mining Joint-Stock Company), Rimamurány-Salgótarjáni Vasmű Rt (Rimamurány-Salgótarján Steel Works Joint-Stock Company), Magyar Kerámiagyár Rt (Hungarian Ceramics Factory Joint-Stock Company), Révai Testvérek Irodalmi Intézet Rt (Révai Brothers" Literary Institute Joint-Stock Company) etc. The joint-stock companies constituted critical components of the Hungarian industry and economy in general. In 1909, the first Hungarian automobile factory was also established based on the CA, which was the Arad-based (currently Arad, Romania) Magyar Automobil Részvénytársaság Westinghouse Rendszer (which later, from 1912, came to be called Marta – Magyar Automobil Részvénytársaság). The municipality of Arad provided a plot of 16 acres to the factory and subscribed an amount of 30,000 crowns for the capital of the company.

The CA and the joint-stock company regulation remained in effect in the period between the two world wars, not only in the present-day Hungary but also in Transylvania, which became part of Romania under the 1920 Trianon Peace Treaty, under the name Transylvanian Commercial Code (Codul Comercial din Transilvania). The history of the CA was closed by the Second World War and the Soviet-type dictatorship. In the years of Soviet-type dictatorship, joint-stock companies were not needed, therefore they were not regulated either, the central players

of the economy were the state enterprises integrated into the state administration, subordinated to line ministries and having public law features.[42]

In the course of and following the change of the economic and political regimes, Hungary saw the elaboration of several company laws, which indicated, among others, the adjustment of the law of joint-stock companies to the economic needs, as well as the development thereof: Act VI of 1988, Act CXLIV of 1997 and Act IV of 2006. Currently, company law and the regulation of joint-stock companies are integrated by the legislator into the Hungarian Civil Code (Act V of 2013), but this is the law in force, which is not the subject of an analysis of legal history.[43]

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[42] Professor Tamás Sárközy gave a scientifically exciting overview of the period. See Sárközy Tamás, *A szocializmus, a rendszerváltás és az újkapitalizmus gazdasági civiljoga 1945–2005 (Economic Civil Law of Socialism, the Change of the Regime and New Capitalism 1945–2005)*, Budapest, 2007.

[43] For the current regulation, see Veress Emőd, *A részvény mint értékpapír (The Shares as Securities)*, Budapest, 2019.

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# MINORITIES PROTECTION AFTER THE RESOLUTION OF EUROPEAN PARLIAMENT OF 13 NOVEMBER 2018

**Dimitris LIAKOPOULOS***

**Abstract**

*This paper intends to analyze EU law evolution on minorities protection, highlighting its particularities through a summary but unavoidable incursion into the system of Society of Nations, United Nations, Council of Europe and OSCE (formerly CSCE).*

**Keywords:** *protection of minorities, Resolution of 13 November 2018, OSCE, EU law.*

## 1. European Parliament"s role in the protection of "right to difference": From the "Arfè" Resolution to the Resolution of 13 November 2018

With regard to minorities protection in EU law, the doctrinal contributions[1] are relatively recent as they date back to the early 1980s of the last century. Referring to the first resolutions of the European Parliament in this area[2], they focus mainly on the evolution that the protection of minorities has recorded since the aforementioned resolutions until reaching the (partial) innovations introduced by the Lisbon Treaty[3]. Although these studies converge with regard to the importance to be given to acts adopted in progress by European institutions starting from the fundamental resolution "Arfè" of 16 October 1981[4], it is rare to find within them the clear distinction, of an internationalistic nature, between the principle of "non-assimilation" aimed at safeguarding, through the assumption of international obligations by states, the cultural identity of the minority group and the principle of "non-discrimination" to be recognized to persons

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[1] A. Van Bossuyt, L"Union européenne et la protection des minorités: une question de volonté politique, in Cahiers de Droit Europèen, 46, 2010, pp. 425ss.

[2] P. Thornberry, International law and the rights of minorities, Oxford University Press, Oxford, 1991, pp. 25ss. F. ERMACORA, The protection of minorities before the United Nations, in Recueil des Cours, 1983, IV, ed. Brill, The Hague, pp. 247ss. F. MIHANDOOST, B. BADAJANIAN, The rights of minorities in international law, in Journal of Politics and Law, 9 (6), 2016, pp. 16ss.

[3] See the Resolution of the European Parliament of 11 February 1983 on measures in favor of minority languages and cultures, in OJ, C 68 of 14 March 1983, and the Resolution of the European Parliament of 30 October 1987 on minority languages and cultures ethnic and regional communities in the European Community, in OJ C 318 of 30 November 1987

[4] Signed on 13 December 2007 and entered into force on 1 December 2009.

belonging to said group[5]. Part of the doctrine[6], after having limited itself to emphasizing the non-obligatory effectiveness of these resolutions, however, has neglected the fundamental logic to which they are inspired, i.e. the recognition, of a "right to difference" of the overall minority group understood. In fact, in-depth information on the role to be recognized to the principle of non-assimilation, understood not in a broad and generic sense (including, therefore, also of the principle of equality and non-discrimination), but focused on the diversification between majority and minority of population and on minority"s group fundamental right to avoid its dispersion within the majority, with consequent loss of identity.

The concept of "discrimination" against minorities and their languages, in fact, is inspired not by the need to ensure respect for the principle of substantial equality towards individuals, as could be considered to a superficial examination of such acts, but rather to the opportunity to safeguard, with a view to non-assimilation, the "historical identity" of minorities themselves, understood as a collectivity.

In assessing this evolution, we will dwell in particular on the recent Resolution of the European Parliament on minimum standards for minorities in EU[7] with which this institution intended to send a warning to the other European institutions and in particular to the Commission, hoping for the adoption of a series of "special protection measures" in favor of minorities, as if to reaffirm the insufficient level of protection currently granted to minority groups in the European juridical space.

## 2. The distinction between the principle of "non-assimilation" and "non-discrimination" in the international minority regime

First of all, it is necessary to highlight the distinction between two principles which, although deeply connected, present substantial differences: the principle of "equality and non-discrimination" and of "protection of minorities" in the strict sense, concerning the necessity to adopt special measures of protection in favor of minorities. The rationale behind these-which can justify a differentiated treatment with respect to the majority-is represented by the non-assimilation of the minority group, understood as "conservation of characteristics, traditions and values proper to each minority" and is aimed at safeguarding the minority group from the risk of losing its cultural identity and the consequent danger of absorption by the majority of population[8].

The prohibition of assimilation, therefore, sets itself as the primary objective not to promote an undifferentiated treatment, but to protect the "diversity" of the minority group. Hence the clear distinction with the principle of formal and substantive

[5] Resolution of the European Parliament of 16 October 1981 on a Community Charter of regional languages and cultures and a Charter of the rights of ethnic minorities, Rapporteur Gaetano Arfè, in OJ, C 287 of 9 November 1981.

[6] J. Burgers, The Right to Cultural Identity, in J. BERTING (eds.), Human rights in a pluralist world, ed. Praeger, Wesport-London, 1990, pp. 251 ss.

[7] European Parliament resolution of 13 November 2018 on minimum standards for minorities in the EU (2018/2036 (INI)),

[8] With the opinion of 6 April 1935 on minority schools in Albania (Publications de la CPJI, Series A/B n. 64, p. 4 et seq.) It was stated that the application of the principle of equality of treatment cannot lead to make a minority group lose its identity towards the majority of the population

equality[9], under which different situations cannot be treated identically and whose purpose is to remove the causes that generate a similar inequality in order to create the conditions for an undifferentiated treatment with no exceptions[10]. While, therefore, the use of "differentiated protection measures" is addressed to minority rights as such[11], or as a community. The implementation of the principle of non-discrimination is based on the recognition of rights of persons (individuals) belonging to a minority.

Another crucial aspect concerns the old question of whether the protection of minority group identity, in application of the principle of non-assimilation, materializes in the recognition of collective rights proper to the minority or if-equal to what happened in the system of the Society of Nations with the Minority Treaties - this protection is pursued through the provision of precise guarantee obligations imposed on states. Some authors have brought the question back to the problem of the existence or non of a collective right recognized to minority groups[12] by solving it in various ways without, however, asking oneself before whether there can be a protection of minorities identity that is independent of the existence or otherwise of collective rights.

It is therefore necessary to ask whether minority groups can receive adequate protection of their identity when an international obligation is imposed on states where these groups exist and, therefore, also independently of the existence of recognition in their favor of a specific right[13]. It will be on these aspects that, starting from the evolution that the protection of minorities has registered at a global level and at a regional level during the twentieth century.

## 3. Minorities protection and cultural diversity in the system of the League of Nations, United Nations, the Council of Europe and OSCE

In the knowledge that it is not possible to exhaust the complex question of means by which international law ensures the protection of human person, we have chosen to recall only the principles and the most important provisions which, within the framework of the law of the Society of Nations, in that of the United Nations, Council of Europe and, more recently, the Organization for Security and Cooperation in Europe (OSCE), note in the field of minorities protection and cultural identity. Indeed, it is quite easy to understand whether EU law is inspired by the principles that inform the aforementioned systems or if, on the other hand, it deviates from them.

At a global level, in relation to the international minority regime at the time of the League of Nations, it should be remembered that the period 1919-1939 was characterized by the absence of international norms for the protection of human rights. The only exception was represented by the

[9] N. Feinberg, La juridiction et la jurisprudence de la Cour Permanente de Justice Internationale en matière de mandats et de minorités, in Recueil des Cours, 1937, I, ed. Brill, The Hague, pp. 660ss.

[10] D.H. Miller, The drafting of the Covenant, New York, 1928, II, pp. 130ss.

[11] Among the particular hypotheses in which minorities are considered "comme des entités collectives" we recall the art. 9 and the art. 10 of the Treaty with Poland, concerning "financial contributions for carrying out educational, religious or charitable activities" and "financial contributions to Jewish schools".

[12] In positive sense see: K. Vanderwal, Collective human rights: a western view, in J. BERTING et al (edited by), Human rights in a pluralist world, ed. Praeger, Wesport-London, 1990, pp. 96ss, which is affirmed that: "can be regarded as human rights, albeit a special sub-category of human rights".

[13] J. Donnelly, Human rights, individual rights and collective rights, in J. BERTING (eds.), Human rights in a pluralist world, ed. Praeger, Wesport-London, 1990, pp. 56ss.

treaties on minorities of which, however, only a small number of beneficiaries could be worth. The rules contained in them were aimed not only at prohibiting any discrimination of individuals, but also above all at protecting certain minority groups from the risk of being assimilated to the majority of the population with consequent loss of their identity.

The subsequent United Nations system did not take into consideration the aspect of collective entities protection as such; said omission was justified by the alleged (especially by the United States) superfluity of a reformulation of art. 1 of the UN Statute and the provisions of the Universal Declaration of Human Rights that already recognized the right of every person (including members of minority groups) not to be discriminated against for reasons of race, language and religion. In this regard, it must be observed that the classification, starting from 1945, of the rights of minorities within the genus of person rights, has implicitly led to a clear *deminutio capitis* connected to the non-consideration of the principle of non-assimilation; situation that will last for about twenty years.

It was only after several years, moreover often on the basis of soft law acts, that at world level even the protection of minority groups as such, or with respect for their identity, would be the subject of a dedicated discipline[14].

The principle according to which persons belonging to a specific minority are recognized as "cultural" rights is found for the first time in the well-known art. 27 of the International Covenant of Civil and Political Rights of 1966. It represents the first legally binding norm of the post-World War II period, which recognizes rights to the generality of minorities and no longer only to certain minority groups. The aforementioned provision, extending the assumption already contained in art. 27 of the Universal Declaration of Human Rights according to which every individual has the right to take part freely in the life of the community, states that persons belonging to ethnic, religious and linguistic minorities cannot be deprived of the right to have their own cultural life, profess and practice one"s religion, use one"s own language, in common with the other members of one"s group[15], which would give the contracting states the obligation to take all the necessary positive measures to protect minorities identity[16].

A particularly significant stage in the process of affirming the obligation to protect minorities identity is represented by the Declaration of the rights of persons belonging to national or ethnic, religious and linguistic minorities, adopted by the General Assembly of the United Nations on December 18, 1992 with Res. 47/135 that in art. 1 highlights the existence and identity of these minorities. States favor the creation of suitable conditions to promote these identities and adopt the necessary legislative provisions for this purpose[17]. On closer inspection, the choice to maintain a specific international discipline on minorities

[14] A. Liebich, A la recherche d"une solution introuvée, in A. LIEBICH, A. RESZLER (a cura di), L"Europe centrale et ses minorités: vers une solution européenne?, Graduate Institute, Geneve, 1993, pp. 198ss.

[15] R. Ben Achour, Souveraineté étatique et protection internationale des minorités, in Recueil des Cours, 1994, I, ed. Brill, The Hague, pp. 424ss

[16] General Comment No. 23 on minority rights, formulated in 1994 by the Office of the High Commissioner for Human Rights.

[17] On the contrary, the subsequent articles (in particular those from 2 to 7 of the Declaration) focus on the principle of non-discrimination but, in obvious analogy with the aforementioned art. 27 of the 1966 Pact, specify that the rights recognized by the Declaration can be exercised "individually as well as a community with other members of their group" (Article 3).

protection following the consolidation of a supranational protection system for human rights, should favor the identification of the ratio in the desire to specifically protect the identity cultural group of the minority group, with simultaneous provision of protection obligations for states, aimed at preventing its dispersion within the majority of population.

Lastly, with reference to other important acts that, at a global level, are relevant for the protection of minorities while not expressly dedicated to this matter, it is necessary to recall the UNESCO Convention on the protection and promotion of diversity of cultural expressions concluded at Paris 20 October 2005 which, highlighting the "importance of cultural diversity" for the progressive realization of human rights, in art. 2 reaffirms the principle under which "the protection and promotion of cultural diversity presupposes respect for human rights, fundamental freedoms such as freedom of expression, information and communication as well as the ability of individuals to choose their own cultural expressions". As opposed to EU law in which the appreciation of "cultural diversity" is left to Member States will, in this act an exhaustive definition of this concept is provided and, on the other hand, it is given to emphasize the principle of respect and appreciation of the diversity of cultures, by virtue of which the culture of each community (and therefore also of a minority group) has a value and a dignity that must be respected and preserved. It basically implies the recognition to groups of that right "to diversity", to "non-assimilation" that permeates the system minorities protection as collective entities and that differs from the system of protection dictated in favor of individuals who, as already pointed out, is based on the principles of equality and non-discrimination.

On a European scale, with reference to the acts adopted in the Council of Europe, there are several similarities with the system of minority protection adopted worldwide by the United Nations. The European Convention on Human Rights (ECHR) in fact, is entirely inspired by the principle of equality and non-discrimination. In particular, art. 14 provides that: "the recognition of the rights and freedoms recognized in the present Convention must be guaranteed without any distinction based above all on sex, race, color, language, religion (...), belonging to a national minority"[18]. It is clear that the question of minorities is confined exclusively to the right of persons belonging to a national minority[19] not to be discriminated.

In ECHR, as in the Universal Declaration of Human Rights, an individualistic approach prevails which only in the early 1990s will present significant openings in the direction of recognizing minorities protection as such and of defending and enhancing the cultural identity of the community. Both the Framework Convention for the Protection of

[18] Clearly inspired by both art. 14 of the European Convention on Human Rights, both in art. 27 of the International Covenant on Civil and Political Rights, is the Final Act of the Conference on Security and Cooperation in Europe, signed in Helsinki on 1 August 1975, which contains some elements of novelty regarding the protection of minorities, between whose goal is to develop cultural cooperation aimed at enriching the respective cultures in the awareness "of the merits and value of each".

[19] It is recalled that the only definition of "national minority" is that contained in recommendation 1201 of the Parliamentary Assembly of the Council of Europe (1993) concerning an additional protocol on minority rights to the European Convention on Human Rights, according to which they fall under this concept "groups of people in a State residing in the territory of the State in question, of which they are citizens; they maintain ancient, solid and lasting ties with the State; they have specific ethnic, cultural, religious or linguistic characteristics; they are sufficiently representative, albeit numerically lower than the rest of the population (...); they are motivated by the desire to preserve what constitutes their common identity, including culture, traditions, religion or language (...)".

National Minorities of 1 February 1995, and he European Charter for Regional and Minority Languages opened for signature in Strasbourg on 5 November 1992, move in this direction, as they are not confined to sanctioning the applicability of the principle of non-discrimination in favor of all those who belong to the aforementioned minorities, but contain provisions specifically set to protect minorities values of ethnic and cultural identities considered as a whole[20].

In fact, among the inspiring principles of the aforementioned Charter, the "right to be different" is expressly described, defined as "inalienable and unavoidable" due to all those, "individuals and groups", who use a language distinct from the official language of the state[21]. The Framework Convention on the value of the cultural heritage of human society was opened for signature in Faro on 27 October 2005 the Council of Ministers with which all states party to the Council of Europe were invited to take measures suitable to support and promote cultural and linguistic diversity in the new global context, respecting (in addition to its own) the cultural heritage of others, as a common European cultural heritage.

With regard to CSCE documents (OSCE since 1994), it should be pointed out that in them we find different references to the principles of equality and non-discrimination aimed at protecting people. Among these, one of the most important is the document adopted at the end of the Copenhagen summit of 29 June 1990 in which the states in paragraph 30 stated that "questions relating to national minorities can only be satisfactorily resolved in a democratic political framework based on the rule of law" which guarantees full respect for human rights and fundamental freedoms, equal rights and conditions for all citizens.

Having said this, the most important fact is that, in the system under consideration, it is above all at the principle of non-assimilation that states finally pay particular attention, stating in paragraph 32 that persons belonging to national minorities have the right (exercisable as an individual or in association with other members of their group) to freely express, preserve and develop their own ethnic, cultural, linguistic or religious identity and to maintain and develop their own culture. In the next paragraph, the aforementioned states are committed to protect minorities identity on their territory, in order to create the conditions for the promotion of this identity.

## 4. The resolutions adopted by the European Parliament and the inertia of other Community institutions

Within EU, as previously pointed out, it is from the 1980s that the first significant acts on the subject of minorities are detected. The aforementioned European Parliament”s 1981 Resolution on a Community Charter of regional languages and cultures and a Charter of rights of ethnic minorities, although lacking in mandatory effectiveness, is clearly inspired by the recognition of a "right to difference" by the minority group and, therefore, to the principle of non-assimilation. From a careful reading it emerges, in fact, that the reference to the prohibition of "discrimination" contained in it is aimed at safeguarding "the historical identity" of minorities and not already ensuring the respect of the principle of equality towards individuals. It is

[20] Art. 7 n. 1, lett. e) and art. 7 n. 4 of the Charter of Regional and Minority Languages of 1992.

[21] See the Preliminary Report prepared by Lluis de Puig for the Permanent Conference of Local and Regional Authorities of 30 January 1986. On this point in doctrine see: S. PETSCHEN VERDAGUER, Las minorias linguisticas de Europa occidental: documentos (1492-1989), Parlamento Vasco, Vitoria, 1990, pp. 582ss.

precisely in order to pursue this purpose that, by means of this act, the European Parliament already from then on wished the adoption of special measures in favor of "minority language and cultures"[22]. These requests, which we regret to note, have also remained unexplained in the 1990s due to the continuing inertia of the Commission and the Council which, both in terms of primary[23] and secondary law, have not introduced any regulatory reference at international level to minorities rights[24].

## 5. A bitter confirmation: the "not received" principle of non-assimilation in the EU Charter of Fundamental Rights, Directive 2000/43/EC and EU Court of Justice jurisdiction

Unlike the Treaty of Nice of 26 February 2001 in which it was decided not to make any changes in the matter of principles applicable to minorities (so much so that this term does not even appear in it), the Charter of Fundamental Rights of the European Union, always proclaimed in Nice on 18 December 2000, contemplates art. 21 the provision of prohibition of "any form of discrimination based, in particular" on membership of a national minority"[25]; thereby confirming the tendency to "confine" the issue of minority protection solely within the scope of application of the right of persons belonging to them not to be discriminated against[26].

Even the immediately following directives 2000/43/CE[27] and 2000/78/CE respond to the purpose of making the principle of equal treatment effective, forbidding both in art. 2, any form of direct or indirect discrimination. In this regard, it is worth pointing out that the statements contained in the just-referred secondary legislation have for a long time remained unexpected since, after almost ten years, the European Parliament, with Resolution of 20 May 2008 on equal opportunities and non-discrimination in EU, still urged member states "to promote citizens" rights more

[22] See also the subsequent Resolution of 30 October 1987, Rapporteur Willy Kuijpers,

[23] this regard it must be observed as well as the change made by the Treaty of Amsterdam to art. 1, par. 1 TEU, it is limited to establishing that: "The Union is founded on the principles of liberty, democracy, respect for human rights and fundamental freedoms, principles which are common to the Member States", without, however, having a explicit reference to minorities.

[24] With regard to the external level, by contrast, some association agreements are clearly more oriented towards the protection of minority groups outside the Union, including, by way of example, it is sufficient to recall here the one with the States of the Central and Eastern Europe and those of Hungary, Estonia and Poland. On the subject of the double standard adopted minorities as such. All the acts adopted in application of the then art. 7 par. 1 TCEE are, in fact, focused exclusively on the principle of non-discrimination of persons and not also of the community and pursue the sole objective of respecting the principle of equality, without saying anything about the enhancement of the diversity of the collective entities considered in themselves. In terms of deeds without binding efficacy, the only one worthy of note is probably the Laeken Declaration on the future of the European Union where Europe is described as "the continent of freedom, solidarity and above all diversity, which implies respect for the languages, culture and traditions of others ". Minorities, albeit with reference exclusively to those outside the EU borders, are expressly referred to when the idea of a Union open only to those countries that respect fundamental values such as respect for minorities and minorities is outlined. of the rule of law.

[25] F. Van Den Berghe, The European Union and the protection of minorities: how real is the alleged double standard?, in Yearbook of European Law, 22, 2003, pp. 162ss.

[26] F. Van Den Berghe, The European Union and the protection of minorities: how real is the alleged double standard?, op. cit.

[27] Council Directive 2000/43/EC of 29 June 2000 implementing the principle of equal treatment between persons irrespective of racial or ethnic origin, OJ L 180, 19.7.2000, pp. 22-26.

effectively in accordance with directives 2000/43/EC and 2000/78/EC"[28].

It should also be noted that the Court of Justice of the European Union (CJEU) jurisdiction, prior to the stipulation of the Lisbon Treaty, appears rather misleading. With reference to the ruling made in the Grand Section on 22 November 2005 in the Mangold case[29], in fact, the reference to the legitimacy of "specific provisions" could mislead recalling the concept of "special protection measures" and favoring recognition in the field of EU principle of non-assimilation. However, a careful examination of the sentence shows that the aforementioned provisions that admit "unequal treatment" in favor of individuals are aimed at promoting the principle of substantial equality and certainly not at enhancing the differences that characterize minority groups, thus substantially confirming the previous orientation focused on the recognition of the principle of non-discrimination only.

## 6. The limited changes regarding minorities protection introduced by the Lisbon Treaty

Unlike what some authors have claimed, we believe we can say that not even the Lisbon Treaty has introduced appreciable changes in the field of minority protection. If there is no doubt that either art. 2 TEU or art. 21 of the Charter of Fundamental Rights mention, for the first time at the level of primary law, minorities. It is also true that the aforementioned norms emphasize exclusively the principle of non-discrimination, without adding anything in terms of protection of the minority group as such. The reference made by art. 2 TEU to the "rights of persons belonging to minorities", falling within the broader category of human rights, is nothing more than a mere clarification of what could already be inferred from the previous art. 6 par. 1 (in the version defined in Nice) in which human rights and fundamental freedoms were mentioned. Although in art. 2 TEU make reference to "pluralism" as the first character that distinguishes European society, in no way this concept is subsequently developed in TEU, neither in TFEU nor in the Charter of Fundamental Rights of EU. This gap is particularly indicative of a "regression with respect to the topic of advantageous situations in favor of spontaneously born collective subjects"[30].

The current European legislation is, in fact, strongly focused on a concept of minority protection limited to the recognition of individual rights and "indifferent to the protection of social pluralism, if not as a reflection of the protection of individual freedoms", without any specific form of protection be reserved for collective subjects. Likewise, even the prohibition of "any form of discrimination based on belonging to a national minority" clearly recognizes the right not to be discriminated against by individuals alone, thus reducing the innovations introduced by the Lisbon Treaty.

Not even in art. 22 of the Charter of Nice seems to be able to recognize any innovative element since it merely states that "the Union respects cultural, religious and linguistic diversity", where the choice to use

[28] Council Directive 2000/78/EC of 27 November 2000 establishing a general framework for equal treatment in employment and occupation, OJ L 303, 2.12.2000, pp. 16-22.

[29] CJEU, C-144/04, Mangold v. Rüdiger Helm of 22 November 2005, ECLI:EU:C:2005:709, I-09981. In the same spirit see also: C-64/16, Associação dos Juizes portugueses of 7 February 2018, ECLI:EU:C:2018:117, published in the electronic Reports of the cases.

[30] M. Decheva, Recht der europäischen Union, ed. Nomos, Baden-Baden, 2018. C. BARNARD, S. PEERS, European Union law, Oxford University Press, Oxford, 2017.

the term "respects" seems emblematic of a "passive" will that, while not confining itself to sanctioning the principle of non-discrimination, it says nothing about the provision of positive behavior by states. The system of protection of minorities in EU law must be completed with reference to the provisions dictated in terms of cultural diversity, including art. 167 TFEU (formerly art. 151 TEC) which completes (with the part shown in italics) the previous version and states that the Union (previously the Community) "takes into account the cultural aspects of the action it performs (...), in particular in order to respect and promote the diversity of its cultures"[31]; and art. 3 par. 3 TEU which concerns the respect of cultural and linguistic diversity (with reference only to the internal dimension) and the development and safeguarding of European heritage.

## 7. The European Parliament Resolution of 13 November 2018 on minimum standards for minorities in EU

In response to the "persistent discrimination" against those belonging to national minorities, the European Parliament, on 13 November 2018, adopted, with 489 votes in favor, 112 votes against and 73 abstentions, the aforementioned resolution to ask for common standards to protect the rights of all national minorities in EU[32]. In particular, after an extensive reconstruction of international and community legislation and an explicit reference to case T-646/13[33], Parliament has asked the European Commission to draft a legislative proposal concerning a directive that introduces minimum standards for minorities protection in EU, provide specific parameters and rules to prevent member states from discriminating against minorities and include a common legal definition of "minority", recommending to this end the adoption of the definition contained in the European Convention on Human Rights.

At point Q - referring almost exclusively to the principle of non-discrimination – the Parliament has critically observed that at present, the Union only has "limited effectiveness tools" to respond to the systematic and institutional manifestations of discrimination, racism and xenophobia and that, despite multiple appeals to the Commission, so far "limited measures" have been adopted to ensure the effective protection of "persons belonging to minorities" (point R).

Through the adoption of the aforementioned resolution, the Parliament highlighted the need for member countries to guarantee equal cultural, linguistic and educational rights to 8% of citizens belonging to national minorities in EU and emphasized importance to protect and promote regional and minority languages in education systems and media. It was also highlighted that the Community system for minorities protection should be accompanied by an evaluation of member states policies in this field. This is because minorities throughout EU are still subject to institutionalized discrimination and are subject to derogatory stereotypes and even their acquired rights are often limited or applied selectively (point X).

[31] M. Decheva, Recht der europäischen Union, op. cit.

[32] European Parliament resolution of 13 November 2018 on minimum standards for minorities in the EU (2018/2036(INI)).

[33] See the next case: T-646/13, Minority SafePack of 3 February 2017, ECLI:EU:T:2017:59, published in the electronic Reports of the cases, which the Court upheld the appeal brought by the Citizens" Committee against the Commission, annulling the latter"s decision not to register the petition by which the Union to improve the protection of persons belonging to national and linguistic minorities and to strengthen cultural and linguistic diversity.

Certainly the most significant part with reference to the subject under examination is contained in point Y where, confirming the importance in the Community context of the recognition of the principle of non-assimilation, the Euro-Parliament states textually that: "there is a difference between protection of national minorities and anti-discrimination policies, that non-discrimination is not enough to stop assimilation, that effective equality is not limited to avoiding discrimination, but means guaranteeing minorities the enjoyment of their rights, including the right to identity, use of language and education, cultural and citizenship rights on an equal footing with the majority". It also notes in point V that "member states" national legislative systems show significant gaps with regard to minorities and indicate a low level of harmonization and symmetry".

However, in the conclusions, contradicting what was said about the need to protect minority groups as such, the European Parliament merely encourages the Commission and member states to safeguard EU citizens right belonging to minorities-who they are placed in a special category as far as the right to the means of appeal is concerned and have specific needs that must be met if they are to guarantee their full and effective equality - to "preserve, protect and develop their own identity, and to adopt the measures necessary to promote the effective participation of minorities in social, economic and cultural life and in public affairs". With the reference to the rights of individuals and not of the minority in itself considered, the European Parliament, assuming an attitude of excessive prudence, has substantially caused its resolution to lose its content, marking a regression with respect to what was more incisively supported in the past.

## 8. Concluding remarks

Wanting to draw the strings of the survey carried out, it is possible to affirm that while the principle of non-discrimination of persons belonging to minorities-both at the world level and in Europe-has been given an adequate regulatory recognition in time, the same thing cannot hold to the principle of non-assimilation of the minority group. And indeed, the protection of minorities (cultural) identity at United Nations, Council of Europe and OSCE has gone from an initial tendency to conceive minorities protection as a matter of human rights, to the progressive awareness of the need for special protection measures for the minority group as it has been almost completely neglected by EU law.

The actions of the European Parliament, the only European institution really active in wanting to outline a system of minorities protection based on the enhancement of the identity of the minority group and the opportunity to preserve their differences were in vain. Even the "vaunted" innovations introduced by the Lisbon Treaty in articles 2 TEU, 21 and 22 of the Charter of Fundamental Rights of the European Union[34] constitute, in the opinion of the writer, mere specifications of the principle of

[34] For further details see: X. GROUSSOT, G.T. PETURSSON, The EU Charter of the Fundamental Rights five years on. The emergence of a new constitutional framework?, in S. DE VRIES, U. BERNITS, S. WEATHERILL, The EU Charter of Fundamental Rights as a binding instrument. Five years old and growing, Oxford University Press, Oxford, 2015. S.I. SÁNCHEZ, The Court and the Charter: The impact of the entry into force of the Lisbon Treaty on the ECJ"s approach to fundamental Right, in Common Market Law Review, 49 (5), 2012, pp. 1566ss. T. TRIDIMAS, Fundamental rights, general principles of EU law and the Charter, in Cambridge Yearbook of European Legal Studies, 16 (3), 2014, pp. 364ss. H. VON DER GROEBEN, J. SCHWARZE, A. HATJE, Europäisches Unionsrecht, ed. Nomos, Baden-Baden, 2015, pp. 820ss.

equality and non-discrimination, but they add nothing in terms of specific protection of minority groups, which are at a time producers and users of the European intangible heritage. In fact, in them there is no express (or even implicit) reference to differentiated protection instruments, or ad hoc treatments aimed at avoiding a dispersion of the minority within the majority group[35].

As regards the causes that led to the absence of an effective regulation of this matter, it must be pointed out that these are not attributable principally or exclusively to, although certainly influential, resistance shown by some member states towards the provision of one specific system for protecting minorities within EU[36]. A prominent responsibility, on the other hand, is believed to be attributed to the European institutions themselves (with the exception of the Parliament) for which, with a view to balancing interests, minorities protection as such through the provision of differentiated treatment in them favor, cannot be reached, as stated by the same Community jurisprudence[37],to the point of hindering the functioning of the common market, if at all possible pushing only to the recognition of the right of persons belonging to a not discriminated minority.

If on the one hand, therefore, no impediment is in principle interposed at Community level to the possible policies of minority group protection and of the enhancement and defense of its cultural identity undertaken by member states, on the other hand-as on many occasions reiterated by CJEU jurisprudence[38]-they must "give way" when they could represent a clear obstacle to the free movement of people, goods, services and capital[39], thus coming to collide with the mandatory principles laid down by the Treaties. To date, this seems to be the direction followed by EU law which, in order to avoid endangering "the autonomy of one"s own legal system in pursuing its own purposes", excludes the applicability within it. This, although in principle worthy of protection, can irreversibly entail an "alteration of essential elements of the community structure".

In a period like the present one, characterized by strong anti-European and nationalist impulses, the delay towards full legal recognition of the status of minorities could inevitably find a concrete and unshakable justification in the fear of some member states to see their national unity threatened. Therefore, it seems difficult for the European Parliament to ensure that the other European institutions, together with EU states, become aware that the protection of minorities, so that it can be considered effective, cannot be limited only to recognition in favor of individuals they belong to the right not to be discriminated against, but must instead, also through the provision of conduct obligations for states and a sanctioning system, safeguard minority groups, preserving their identity against the risk of a progressive as well as inevitable assimilation.

[35] T. Kerikmäe, Protecting human rights in the EU. Controversies and challenges of the Charter of Fundamental Rights, ed. Springer, Berlin/Heidelberg, 2014.

[36] K. Lenaerts, Fundamental rights in the European Union, in European Law Review, 6, 2000, pp. 598ss.

[37] CJEU, C-15/81, Gaston Schul Douane Expediteur BV v. Ispettore dei tributi d"importazione e delle imposte di consumo di Roosendaal of 5 May 1982, ECLI:EU:C:1982:135: I-01409, par. 33.

[38] CJEU, C-49/89, Corsica Ferries France of 13 December 1989, ECLI:EU:C:1989:649, I-04441 in point 8 it was specified that "any obstacle, even minor, to the freedoms themselves is forbidden". See also: J. RAITIO, The principle of legal certainty in EU law, ed. Springer, Berlin, 2013.

[39] F. Palermo, The use of minority languages: Recent developments in EC law and judgments of the ECJ, in Maastricht Journal of European and Comparative Law, 8, 2001, pp. 300ss.

In line with the wishes set out in the recent resolution of the European Parliament, it is hoped that in the immediate future the Euro-unitary order will not be limited, in a merely abstaining view, to prohibit discriminatory behavior towards minorities, but yes openly active in bringing about positive behaviors that can give greater substance to the spirit of EU, truly "united in diversity". What the European Parliament wished to reaffirm with the examined resolution is, in fact, that "EU is a mosaic of cultures, languages, religions, traditions and history, which forms a heterogeneous community of citizens united by their common fundamental values; that this wealth of Europe cannot be taken for granted and should be protected and nourished"[40].

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[40]CJEU, Opinion 1/9 of 14 December 1991, ECLI:EU:C:1991:490, I-01137. See also in argument: T. LOCK, The European Court of Justice and international courts, Oxford University Press, Oxford, 2015, pp. 86ss.

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# THE LEGAL CONSEQUENCES OF THE CONSTITUTIONAL COURT"S DECISIONS IN THE CONTEXT OF THE LEGALITY PRINCIPLE OF THE CRIMINAL PROCEDURE

**Liliana-Dorina RĂDUCU**[*]

**Abstract**

*The principle of legality of the criminal procedure is the established general rule according to which the criminal trial is carried out under the provisions stipulated by the law. In order to fully understand the application of the fundamental principle of legality of the criminal proceeding, it is necessary to clarify, on the one hand, the notion of "criminal procedural law" - a term that does not have a legal definition and, on the other hand, it is necessary to analyze the evolution of the concept referring to the source of criminal procedural law, in the current conventional context, as well as in the context of the Constitutional Court"s jurisprudence. Ensuring the application of the criminal process" lawfulness is firstly achieved by the legislator"s fulfillment of the obligation to clearly regulate the rules of conducting the criminal proceedings and other judicial proceedings in connection with a criminal case. However, the actual reality proves the existence of numerous legal provisions declared unconstitutional, the Constitutional Court"s decisions being binding for both the legislator and the judicial bodies. Thus, the purpose of the research is to identify the consequence of the legislator"s lack of intervention so that the stipulations declared unconstitutional would agree with the Constitution"s provisions if it grants valences of some sources of law to the decisions of the Constitutional Court, if it transforms the Constitutional Court into a positive lawmaker or it just assigns the entire task of guaranteeing of the criminal process" lawfulness to the judicial bodies. In fact, although the nullity is the main procedural guarantee of the legality of the criminal trial, the consequences of the Constitutional Court"s decisions raise many problems of unitary interpretation and application of the law even in this area, thus questioning the legality of the criminal process.*

**Keywords:** *the legality of the criminal trial, criminal procedural law, the effects of the Constitutional Court"s decisions, sources of criminal procedural law, absolute and relative nullity*

## 1. Introduction

The legality of the criminal process is the fundamental principle governing the conduct of the entire criminal process, its incidence sights all phases of the criminal process: prosecution, preliminary chamber, judgment and enforcement of judgments.

The fundamental principle of legality is generally enshrined in the Romanian Constitution, in art. 1 para. (5) showing that, in Romania, the observance of the Constitution, its supremacy and the laws is compulsory, and in particular, as regards the criminal proceedings, in art. 2 of the Code of Criminal Procedure, according to which the criminal proceedings are carried out in accordance with the provisions prescribed by the law.

Starting from the general framework of the principle of legality of the criminal process, although the existence of a clear and predictable law-as a source of law,

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constitutes an imperative in this area, the notion of criminal procedural law does not know a legal definition, being imposed a detailed analysis of it in the context of the case-law of the Constitutional Court and the European Court of Human Rights.

In order to respect the principle of legality of the criminal process, it is mainly the legislature"s task to lay down legal rules governing the conduct of the criminal proceedings, but, as any regulation of an activity, the law cannot capture in detail all the issues that will arise during the criminal process.

It also equates to the lack of a text of law and the assumption that there is a written law, but which does not meet the quality conditions.

In contrast to the field of criminal law when the lack of legal provision constitutes an impediment to the criminal liability of a person, the criminal process will not stop in the event of a lack of regulation of a particular procedural situation.

The inability of the legislator to provide in a text of law all situations which may be encountered in the conduct of the criminal proceedings or their respective regulatory provisions, leads to the exercise of obligations imposed on constitutional authorities or judicial bodies, precisely in order to comply with the principle of legality.

Thus, the exclusive competence to legislating, mainly attributed to the Parliament, is not discretionary, but is subject to scrutiny of the constitutionality of the Constitutional Court of Law. However, that intervention should not confer on the Constitutional Court legislative powers when the legislature has not fulfilled that obligation.

Despite the latter aspect, new rules of general binding criminal law have been established through the recent case-law of the Constitutional Court.

It remains to be determined whether, in those circumstances, the decisions of the Constitutional Court should be included in the notion of criminal procedural law, which is required to be analysed in the light of the case-law of the European Court of Human Rights, according to which the autonomous notion of "law" also includes jurisprudence, or if the decisions of the Constitutional Court acquire the nature of criminal procedural law sources.

The binding nature of the decisions of the Constitutional Court requires the adoption of one of the abovementioned solutions, although at this time, in the national legal order, in the concept of law, is not also included the compulsory case-law, and the doctrine is reserved in classifying the decisions of the Constitutional Tribunal as the sources of criminal procedural law.

The latter approach should be announced in the context of the evolution of the case-law of the Constitutional Tribunal, especially in the field of interpretative decisions, which, in certain specific cases, bear the valences of a true regulation.

In this legal context, the hardest task lies with the judicial bodies, as the main actors of the criminal process, who have an obligation to interpret the law in accordance with the principle of legality, to comply with the decisions of the Constitutional Court or, in the absence of the total laws or other rules of criminal procedural law, application of the analogue supplement.

It is therefore necessary to identify the legal pathways for carrying out the criminal liability activity of the persons who committed offences, by reconciling an imperfect law with the effects of the decisions of the Constitutional Court, when they appear nuances in fulfilling the obligations and observance of the legal competences of each of the two powers, the criminal process will be carried out in all

cases, imperative under the principle of legality.

## 2. Criminal Procedural law

### 2.1. The notion of law

As a consequence of the fact that the conduct of the criminal proceedings is governed by the adage, "*the nulum judicium sine lege*", "the repressive Courts must work only in the cases, in the form and, in the forms prescribed by law, avoiding and refusing any other process that does not bear the seal of legality, even if it were, in cases, more comfortable, propor and more rational. On the other hand, that principle requires the legislator to make a full and wise bundle of rules to ensure the proper conduct of the repressive action within the reach of repressive justice."[1]

In applying the principle of legality, the conduct of the criminal process must take place in accordance with the provisions laid down by law, so the existence of a law and the application and compliance with the legal provisions is required.

There is no regulated definition of the notion of "criminal procedural law", but relevant in this respect are the provisions of art. 173 of the Penal Code defining the notion of " criminal law " as any criminal provision contained in organic laws and emergency ordinances or other normative acts which, at the time of their adoption, had the power of law.

On the one hand, the determination of the meaning of "criminal law" is only a starting point for the identification of the framework for applying the principle of legality of the criminal process, since the provisions of art. 173 of the Penal Code concern substantive rules of criminal law, and the conduct of the criminal proceedings takes place on the basis of procedural criminal law rules, in the latter case, in relation to the principle of legality of the criminal process, the notion of law being interpreted *lato sensu*. The difference between substantive and procedural law rules has been highlighted by the fact that, "all the rules of law confering such a rights will constitute substantive rules, contrary to all the rules of their content, do not indicate only how the rights granted will be exercised and the formalities after which the entire activity leading to the realisation of the repressive justice will be carried out shall be rules of formal law (procedural provisions)."[2]

On the other hand, the conduct of the criminal process and other judicial proceedings involves the competition of both the judicial authorities and other parties or other persons in achieving its purpose, which implies the undertaking of numerous activities governed by secondary legislation, such as government decisions, orders or internal organisation regulations. The verification of compliance with the principle of legality of the criminal process is not limited to fully respecting only the provisions of the laws, but also by analysing the lower-level acts, without the power of law, but which come to detail the rules of procedural law compliance with the legal limits.

In this respect, in the literature of specialty[3] it has been shown that the

[1] I. Tanoviceanu, *Treaty of Law and Criminal Procedure*, vol. IV, Second edition of the course of law and criminal Procedure, reviewed and supplemented by V. Dongoroz and. A., typography, "The Judicial Courier", Bucharest, 1924, p. 35;

[2] *Idem*, p. 25;

[3] N. Volonciu, *Treaty of Criminal Procedure*, Vol. I, Peideia Publishing House, Bucharest, 1998, p. 83; V. Dongoroz etc., *New Criminal Procedure Code and previous Criminal Procedure Code*, Political Publishing House.,

compliance with the principle of legality is checked against all the rules governing an act, and not only in relation to a certain provision of law.

In the case-law of the Constitutional Court [4] as regards the notion of "law", it was noted that the notion of law "has several meanings according to the distinction between the formal or organic and material criteria."

Thus, a distinction is made between the existence of a law text according to the formal citerium (*lex scripta*) and the quality of the law – in relation to the substantive criterion (*lex certa*).

The formal criterion shall be assessed on the basis of the issuing body and the procedure to be complied with in the adoption of the law. According to art. 61 para. (1) the second sentence of the Constitution, the Parliament is (...) the only legislature of the country, further the provisions of art. 76, 77 and 78, stipulating that the law adopted by Parliament is subject to promulgation by the President of Romania and enters into force three days after its publication in the Official Gazette of Romania, part I, if no further date is foreseen in its content.

As regards the government"s Ordinances, The Court held[5] that, "by drafting such normative acts, the administrative body exercises a competence by award which, by its nature, falls within the legislative competence of Parliament. Therefore, the ordinance is not a law in a formal sense, but an administrative act of the law, assimilated to it by the effects that it produces, while respecting the substantive criterion."

Next, the analysis of the existence of a law from the point of view of the substantive criterion relates to the subject matter of the norm, namely the nature of regulated social relations. These conditions add to the clarity and accessibility of the text of law, the European Court of Human Rights, in its case-law[6] showing that there is not enough the existence of a procedural legal rule contained in laws, ordinances, Government emergency ordinances, in international conventions and treaties to which Romania is part or other acts regulating a particular activity, but the notion of law incorporates the right of origin both legislative and jurisprudential and involves some qualitative conditions, inter alia those of accessibility and predictability.

For the full understanding of the substantive nature of the law, the relevant considerations are the recitals of decision No. 600 of 9th of November 2005 of the Constitutional Court[7] by which, concerning the concept of "law", the Court held that, "by definition, the law, as a legal act of power, is unilateral, giving expression exclusively to the will of the legislature, whose content and form are determined by the need to regulate a particular area of social relations and its specificities. "

The condition of accessibility of the law is fulfilled through the provision of art.

Bucharest, 1969, apud. M. Udroiu, in M. Udroiu (coord.), *Code of Criminal Procedure. Commentary on articles*, ed. 2, C. H. Beck Publishing House, Bucharest, 2017, p. 6;

[4] Decision No. 146 of 25 March 2004 a Constitutional Court, Published in the Official Gazette of Romania, Part I, Nr. 416 of 10 May 2004;

[5] *Ibidem;*

[6] ECHR, judgment in Dragotoniu and Militaru-Pidhorni v. Romania, 24 May 2007, paragraph 34 and 35; ECHR, judgment in Cantoni v French, 15 November 1996, paragraph 29; Judgment of the ECHR, Coëme and Others v. Belgium, 32492/96, 32547/96, 32548/96, 33209/96 and 33210/96, paragraph 145, ECHR 2000-VII and E.K. v. Turkey, No. 28496/95, paragraph 51, 7 February 2002;

[7] Decision No. 600 of November 9, 2005 of the Constitutional Court, Published in the Official Gazette Nr. 1060, Part I, of 26 November 2005;

10 of Law No. 24 of 27 March 2000 to the fact that, with a view to their entry into force, the laws and other normative acts adopted by Parliament, the ordinances and judgments of the Government, the normative acts of the autonomous administrative authorities, as well as the orders, the instructions and other normative acts issued by the Central public administration bodies shall be published in the Official Gazette of Romania, part I.

It is therefore necessary to give the person the opportunity to acknowledge the content of the legal norm. By publishing it in the Official Gazette of Romania, the law fulfils the the requirement of accessibility, in the same vein as the European Court of Human Rights in in the cause Rotaru v. Romania, judgment of 29 March 2000, paragraph 54.

As far as secondary legislation is concerned, the condition of accessibility is achieved by bringing it to public knowledge, for example, by publishing on the websites of the institutions, and that the fulfilment of that condition is established in concrete, in relation to each subject and the circumstances of the case.

The predictability of the law provision presupposes that it must be sufficiently clear and precise to be applied.

In this respect, according to art. 7 para. (4) of Law No. 24 of 27 March 2000 on the rules of legislative technique for the drafting of normative acts, the legislative text must be formulated clearly, fluently and intelligible, without syntactic difficulties and obscure or equivocal passages. No affective load terms are used. The form and aesthetics of the expression must not prejudice the legal style, accuracy and clarity of the provisions.

With regard to the accessibility and predictability of the law, the Constitutional Court noted[8] that "one of the requirements of the principle of compliance with laws relates to the quality of normative acts and that, in principle, any normative act must fulfil certain qualitative conditions, including predictability, which presupposes that it must be sufficiently clear and precise to be applied. Thus, the wording with sufficient precision of the normative act allows the persons concerned, who may, if necessary, appeal to the advice of a specialist, to provide a reasonable measure, in the circumstances of the case, of the consequences which may result from an determined act . Concerning the same law-quality requirements, the guarantee of the principle of legality, the European Court of Human Rights, by judgments of 4 May 2000, 25 January 2007, 24 May 2007 and 5 January 2010, rendered in the cases Rotaru v. Romania ( Paragraph 52), Sissanis v. Romania (paragraph 66), Dragotoniu and Militaru-Pidhorni v. Romania (paragraph 34) and Beyeler v. Italy (paragraph 109), made it compulsory to ensure these laws quality standards as guarantee of the principle of legality laid down in article 7 of the Convention for the Protection of Human rights and fundamental freedoms.

Thus, by judgment in Sissanis v. Romania (paragraph 66), the European Court held that the phrase <prescribed by the law>requires the contested measure to have a basis in national law, but also seeks the quality of the law in question: it should indeed be accessible to the vigilante and predictability in relation to its effects.

It was also held that, in order for the law to satisfy the requirement of predictability, it must state with sufficient clarity the extent and modalities of the exercise of the discretion of the authorities in that field, taking into account the aimed legitimate purpose to provide the person

[8] Decision no. 1 of the 10th of January 2014 of the Constitutional Court, Publised in The Official Gazzette of Romania, Part I, no. 123 of the 19th of February 2014;

with adequate protection against the arbitrary.

In addition, it has been held that it cannot be regarded as <law> merely a rule set out with sufficient precision, in order to enable the citizen to control his conduct, by appealing in need of expert advice on the matter, he must be able to provide, to a reasonable extent, to the circumstances of the case, the consequences which may result from a particular act. "

Moreover, the European Court of Human Rights has shown[9] that the significance of the notion of predictability depends largely on the context of the text, the area it covers, and the number and quality of its recipients.

The predictability of the law does not preclude the person concerned from having to resort to good advice in order to assess, at a reasonable level in the circumstances of the case, the consequences that might arise from a certain action[10]. This usually happens with professionals, accustomed to proving a great prudence in the exercise of their profession. It can also be expected from them to pay particular attention to the assessment of the risks involved[11].

Consequently, as a normative legal act, in general, is defined both by form and by content, the law in a broad sense, thus including assimilated acts, is the result of combining the formal criterion with that material.[12]

### 2.2. International conventions and treaties

The conventions and international treaties to which Romania is a party are included in the notion of "law" in this regard being the provisions of art. 11 of the Romanian Constitution, which establishes that the treaties ratified by Parliament, according to the law, form part of national law, and if a treaty to which Romania is to become a party contains provisions contrary to the Constitution, the ratification can take place only after the revision of the Constitution.

Also, according to the provisions of art. 20 of the Constitution, the constitutional provisions on citizens" rights and freedoms will be interpreted and applied in accordance with the Universal Declaration of Human Rights, with the pacts and other treaties to which Romania is a party. If there are inconsistencies between the pacts and the treaties on fundamental human rights, to which Romania is a party, and domestic laws, they have priority over international regulations, unless the constitution or national laws Contain more favourable provisions.

### 2.3. Compulsory case-law

Decisions given in the appeal in the interest of the law and the decisions rendered by the Panel on the untying of legal matters have binding force for the courts from the date of publication of decisions in the Official Gazette of Romania.

According to art. 474 para. (4) of the Code of Criminal Procedure, the unlinking of the matters of legal proceedings is compulsory for the courts from the date of publication of the decision in the Official Gazette of Romania, part I.

Also, as regards the decisions of the High Court of Cassation and Justice, pronounced by the panel for the untying of legal matters in criminal matters, according to art. 477 para. (3) of the Code of Criminal

[9] ECHR, Groppera Radio AG and Others v. Switzerland of 28 March 1990, paragraph 68;
[10] ECHR, Tolstoy Miloslavsky v. The United Kingdom of Great Britain, July 13, 1995, paragraph 37;
[11] ECHR, Cantoni v. France, 22 June 2000, paragraph 29;
[12] Decision no. 146 of 25 March 2004 of the Constitutional Court, Published in the Official Gazette of Romania, Part I, no. 416 of May 10, 2004;

Procedure, the unlinking of matters of law is compulsory for courts from the date of publication of the decision in the Official Gazette of Romania, part I.

However, the judiciary cannot enter the field of legislative power.

In this respect, the Constitutional Court has held[13] that it has no power to engage in the field of law-making and criminal policy of the State, any contrary attitude constituting an interference with the jurisdiction of that constitutional authority. The Court acknowledges that, in that area, the legislature enjoys a rather large margin of discretion, given that it is in a position which allows it to assess, according to a number of criteria, the need for a particular criminal policy.

Therefore, on the basis of the principle of separation of powers in the state, the High Court of Cassation and Justice has no competence in the field of law.

This issue is relevant in the present case, given that the decisions of the High Court of Cassation and Justice on appeal in the interests of the law or for the untying of matters of law in criminal matters may also concern a question of procedural low. The High Court of Cassation and Justice has held[14] in this regard the following: "the question of which the untying is subject to the examination of the high Courts of Cassation and Justice must, as a rule, concern a matter of substantive law which depends on the substantive settlement of the case, which may only, as an exception, concern a procedural problem, i.e. to the extent that the solution given to it is significantly passed on to the settlement of the fund."

Regarding the absence of the law of a judgment of the High Court given on appeal in the interests of the law or for the untying of matters of law, it was stated that[15] că the "Decision No 2 of April 14, 2014 of the Supreme Court is not a normative act, in the meaning given to this notions of law no. 24/2000, republished, with subsequent amendments and additions, which in art. 11, makes a limitative enumeration of issuers of such acts, which does not include the High Court of Cassation and Justice by judgments given in the uniform interpretation and application of the law.

On the other hand, the judgments of the High Court on appeal in the interest of the law or for the untying of matters of law cannot be regarded as statutory laws, in the meaning of art. 173, the final sentence of the Penal Code, and, in the light of the fact that it does not regulate social defence relationships, does not establish rules of conduct and rules of crimination or which relate to criminal liability, its bases and limitations, but reflects only a interpretation of such provisions contained in normative acts drawn up and adopted in accordance with the legislative technical procedure applicable to the matter. In the same context, accepting the idea that the interpretative solutions rendered by the Supreme Court by prior judgments for the untying of matters of

[13] Decision no. 405 of 15 June 2016 of the Constitutional Court, Published in the Official Gazette, Part I, no.517 of 08 July 2016; Decision no.629 of 4 November 2014 of the Constitutional Court, Published in the Official Gazette of Romania, Part I, no.932 of 21 December 2014;

[14] Decision No. 7 of 17 April 2015 of the Panel for the untying of matters of law in criminal matters of the High Court of Cassation and Justice, Published in the Official Gazette of Romania, Part I, No. 359 of 25 May 2015;

[15] Decision No. 21/2014 of the High Court of Cassation and Justice-the panel for the untying of matters of law in Criminal Matters, Published in the Official Gazette of Romania, Part I No. 829 of 13 November 2014, *which established that the provisions of article 5 para. 1 of the Penal Code must be interpreted, including the limitation of criminal liability, in the sense that the more favourable criminal law is applicable to offences committed before 1 February 2014 which have not yet been definitively judged, in accordance with decision No. 265/2014 of the Constitutional Court;*

law and decisions given in appeal in the interest of the law are included in the sphere of criminal law would amount to a violation of the principle of separation of powers in the state by the judicial authority taking over the powers of the legislative power with the consequence of verifying the constitutionality of those judgments by the Court of Constitutional law. "

### 2.4. Case-law

In the Romanian criminal law, jurisprudence does not constitute a source of law, in this regard being also the decision no. 23 of 20 January 2016 of the Constitutional Court[16], whereby the Constitutional Court held that, in the continental system, the case-law does not constitute a source of law so that the meaning of a rule can be clarified in that way, because, in such a case, the judge would become a lawgiver.

However, this view must be nuanced with the case-law of the European Court of Human Rights[17], according to which the notion of " law ", within the meaning of the EU Convention for the Protection of human rights and fundamental freedoms, incorporates the right of origin both legislative and jurisprudential.

In order for the case-law to equate to the acceptance of the European Court of Human Rights with a law, it must undergo a stage of crystallization leading to the existence of a constant jurisprudence, formed over a large period of time, so as to enable the citizen to reasonably expect a certain interpretation of the rules, taking into account the developments in practice.

The analysis of jurisprudence as a source of law, in the light of the jurisprudence of the European Court of Human Rights, was made on the occasion of establishing the existence of a more favourable criminal law as a result of decision No. 2/2014 of the High Court of Cassation and Justice (by which it was decided that in the application of article 5 of the Penal Code, the limitation of criminal liability is an autonomous institution for the institution of the penalty) and subsequently to the decision of the Constitutional Court No. 265/2014 (by which it has been held that the provisions of article 5 of the Penal Code are constitutional in so far as they do not allow the combination of the provisions of successive laws in the establishment and enforcement of more favourable criminal law).

Thus, the High Court of Cassation and Justice recalled[18] that " it has been held in principle by the Strasbourg court that the notion <law>in the light of the European Convention encompass the right of origin both legislative and jurisprudential, but decision No. 2 of 14 April 2014 handed down by the High Court of Cassation and Justice-the Assembly for the untying of matters of law in criminal matters, does not subdue to this notion, constituting only a stage in the complex process of crystallization of a case of jurisprudences consistent with the determination and enforcement of more favourable criminal law after the entry into force on 1 February 2014 of the new Penal Code, adopted by Law No. 286/2009.

In other words, a single judgment, either in the untying of a matter of law by the Supreme Court, in accomplishing its powers of interpretation and uniform application of

[16] Decision No. 23 of 20 January 2016 of the Constitutional Court, Published in the Official Gazette of Romania, Part I, no 240 of 31 March 2016;

[17] ECHR, Kokkinakis v. Greece of 25 May 1993; ECHR, judgment of S.W. and C.R. v. The United Kingdom of 22 November 1995; ECHR, judgment in Cantoni v. Franceadin 15 November 1996; ECHR, judgment of the E.K. v Turciadin 7 February 2002; ECHR, judgment in Pessino v Franceadin October 10, 2006);

[18] Decision no. 21/2014 of the High Court of Cassation and Justice - The Criminal Law Enforcement Unit, Published in the Official Gazette, Part I no. 829 of November 13, 2014;

the law, does not amount to the European Court"s acceptance of a law, a concept which implies the existence of a constant jurisprudential guidance, formed over a long period of time.

However, the requirement of consistent case-law has not been met with regard to the determination and application of milder criminal law by national courts after 1 February 2014, given the very short period of time, only three months, pending the publication of the Constitutional Court"s Decision no. 265 of May 6, 2014, and the different interpretations made in judicial practice for the purpose of assessing criminal law more favorably either globally or autonomously, especially as there was no unitary view of the latter in the latter as autonomous of different criminal law institutions.

In those circumstances, it cannot be the shaping of a constant case-law either in the application of the more favourable criminal laws in matters of criminal prescription in the period of only 20 days following the publication on 30 April 2014 of the judgment of the Supreme Court of Untying this issue of law until the end of its effects on 20 May 2014, when the interpretation in accordance with the Constitution of the provisions of art. 5 of the Penal Code became of immediate application and general compulsory. "

In the light of the case-law of the European Court of Human Rights, as has been mentioned above, the autonomous notion of " legislation " also includes jurisprudence, but this case-law must be constant. The decision-making function for the courts serves precisely to remove the doubts that may exist with regard to the interpretation of the rules, taking into account the developments in the daily practice, provided that the result is coherent with the substance of the offence and clearly foreseeable [19].

Consequently, it can reasonably be argued that a jurisprudential rule, as it is respected by the majority of the internal courts, is clear and accessible and that its application in the present case is foreseeable[20], it can be considered, "law" within the meaning of Jurisprudence of the European Court of Human Rights.

## 3. Deciziile Curţii Constituţionale şi efectul general obligatoriu al acestora

According to the provisions of art. 147 para. (4) of the Constitution of Romania, from the date of publication, the decisions of the Constitutional Court are generally binding and have power only for the future. The Court[21] has ruled, with a value of principle, that the compulsory force accompanying the judicial Acts, so also the decisions of the Constitutional Court, attache not only to the device, but also to the considerations which it supports. Thus, it was noted that both the recitals and the device of its decisions are generally binding and are imposed with the same force on all the subjects of law.

Although its decisions are generally binding, the Constitutional Court has no competence in the field of law-making.

[19] ECHR, the decision of S.W. v. the United Kingdom of Great Britain, 22 November 1995, Series A no. 335-B, p. 41, paragraph 36;

[20] ECHR, Lupas and others v. Romania of 14 December 2006, paragraph 69;

[21] Decision of the Plenum of the Constitutional Court no. 1/1995 regarding the mandatory of its decisions under the constitutionality control, Published in the Official Gazette of Romania, Part I, no. 16 of 26 January 1995; Decision no. 1.415 of November 4, 2009 of the Constitutional Court,, Published in the Official Gazette of Romania, Part I, no. 796 of 23 November 2009 and Decision no. 414 of April 14, 2010 of the Constitutional Court, Published in the Official Gazette of Romania, Part I, no. 291 of May 4, 2010;

According to art. 2 para. (3) of Law No. 47/1992, the Constitutional Court shall only pronounce on the constitutionality of the acts in respect of which it was seised, without being able to amend or supplement the provisions subject to scrutiny. In its case-law[22], it held that Parliament is free to decide on the state"s criminal policy, any opposite attitude constituting an interference with the jurisdiction of that constitutional authority. While, in principle, Parliament enjoys exclusive competence in regulating measures relating to the State"s criminal policy, that competence is not absolute in the sense of excluding the exercise of constitutionality control over the measures adopted.

The principle of legality is naturally complemented by the principle of separation of powers in the state, the Constitutional Court having no legislative powers.

It must not be understood from that conclusion that the decisions analysing the constitutionality of a legal provision do not affect the rule of law. As previously mentioned, they are compulsory from the date of publication in the Official Gazette of Romania, and the application and interpretation of the provisions laid down by law must be carried out only in accordance with those which are made by simple decisions or interpretative finding of unconstitutionality.

Therefore, their contribution, in our particular case, in criminal procedural matters, in compliance with the limits of the principle of legality, shall be retreated to the legal provisions analysed, already existing, by excluding the non-constitutional norm from the Legal order or by granting the constitutional meaning.

Although this aspect proves to be clearly established, the general binding effect of the decisions of the Constitutional Tribunal continues to exist by imposing rules of law on the nature of criminal procedural law.

The establishment of a rule of criminal procedural conduct both by the recitals of decisions rejecting the exceptions of unconstitutionality and by the removal of unconstitutional legal rules in force, but especially by the imperative stipulation of a certain positive conduct exceeding the scope of the rule which formed the subject-matter of the exception of unconstitutionality – the aspect encountered in the interpretative decisions, gives to the decisions of the Constitutional Court the nature of sourses of procedural, criminal law[23].

This is the direct consequence of the general binding effect of the decisions of the Constitutional Court and the failure of the legislature to agree unconstitutional provisions with the provisions of the Constitution, within 45 days after publication of the decision, thus creating a legislative void.

However, the passiveness of the legislature does not take effect in the event of decisions rejecting unconstitutionality exceptions-when the legal rules continue to enjoy the presumption of constitutionality.

The provisions of art. 147 para. (4) of the Constitution of Romania, which establishes the binding of the general effect, do not distinguish between decisions which reveal the unconstitutionality of a legal provision and decisions rejecting unconstitutionality exceptions. A well-known rule of interpretation is that „where the law does not distinguish, neither should

[22] Decision no. 405 of 15 June 2016 of the Constitutional Court, Published in the Official Gazette, Part I, no. 517 of July 8, 2016; Decision no. 629 of 4 November 2014 of the Constitutional Court, Published in the Official Gazette of Romania, Part I, no. 932 of December 21, 2014;

[23] F. Streteanu, D. Nițu, *Criminal Law. General Part, Vol. I*, Universul Juridic Publishing House, Bucharest, 2014, p. 75;

we distinguish „(*ubi lex non distinguist, nec nos distinguere debemus*). Perfectly applicable in the present case, all the decisions of the Constitutional Tribunal, without distinguishing whether or not the unconstitutionality of a law or ordinance or a provision of a law or ordinance have been established, are general mandatory.

In the case of decisions establishing the unconstitutionality of a text by law, by virtue of the negative legislature, the Constitutional Court excludes the rules contrary to constitutional provisions from the legal order and is fully justified the effect generally binding *erga omnes*, without the possibility of a text being both unconstitutional and constitutional in the light of the subjects of law.

The general binding effects of erga omnes are a natural consequence of the constitutional provision found in art. 147 para. (1) stating that the provisions of the laws and ordinances in force and those of the regulations, as established as unconstitutional, cease to be legal effects at 45 days after the publication of the decision of the Constitutional Court if, in this The Parliament or the Government, as the case may be, do not agree the unconstitutional provisions with the provisions of the Constitution. During that period, the provisions established as unconstitutional are suspended by law.

As regards the decisions rejecting unconstitutionality exceptions, there is obviously no such effect of the suspension of law and, subsequently, the termination of legal effects. By the time the finding of its unconstitutionality is found, any rule is presumed to conform to the provisions of the fundamental law. However, as previously mentioned, the Romanian Constitution confers a generally binding effect on all decisions of the Constitutional Court. As a symmetry of the consequences of the finding of the unconstitutionality of legal provisions, the general binding effect is manifested in the case of decisions rejecting the exception of unconstitutionality by maintaining the obligation of application, in the rules of law considered constitutional within the limits of the control carried out. [24]

However, in that case, the determination of the framework of the binding general effect must be carried out in accordance with the authority of the court ruling of the judicial decision, the general binding effect being significantly diminished.

Therefore, we note that the rules on Civil Procedure, which are compatible with the nature of the proceedings before the Constitutional Tribunal, confer on the authority of the judgment, including the decision rejecting the exception of unconstitutionality, but only in Relation to a new exception of unconstitutionality raised by the same parties, in the same case and relating to the same legal provisions, for the same reasons. As such, the generally binding effect, is limited in this case, to the question cut with the authority of work judged. The analysis of the Constitutional Court is circumscribing the criticality and factual and legal situation existing in the case in which the exception was lifted. At the same time, the interpretation of the provisions of art. 29 para. (3) of Law No. 47/1992 on the organisation and functioning of the Constitutional Court, it is apparent that the provisions which have not been found unconstitutional by an earlier decision of the Constitutional Court may be subject to the exception. Therefore, the general binding effect of the decisions establishing the constitutionality of the legal provisions criticized should not be absoluted. Under no circumstances will such a decision be able to

[24] I. Morar, M. Constantinescu, *The Constitutional Court of Romania*, Albatros Publishing House, Bucharest, 1997, p. 162;

be opposed to the power of work judged in another case or even in the same procedural framework, but for other reasons.

By Decision No. 169/1991[25] The Constitutional Court held that, the same parties and for the same reasons cannot reiterate the exception of unconstitutionality, since the authority of the work on trial would be infringed. But in another process the exception can be reiterated, thus enabling the Constitutional Court to reanalyze the same issue of unconstitutionality, as a result of invoking new grounds or of intervening other new elements, which amend the case-law of the court. " The consequence of the elements of differentiation of law and of fact between the cases in which the exceptions of unconstitutionality are raised, the general binding effect of the decision establishing the constitutionality of a legal provision will operate only *inter partes*.

However, although a decision rejecting the exception of unconstitutionality enjoys the authority of the Court of Justice, that aspect is recognised only in respect of the considerations which support and explain the solution adopted (decisive considerations), As well as (...) of those who have been debated in the process (decision-making considerations). The Working authority shall not concern the indifferent considerations, which may be lacking in the content of the reasoning, without it leading to the lack of foundation of the judgment." [26]

Therefore, we do not exclude *de plano* the possibility of establishing in the recitals of decisions rejecting exceptions to non-constitutionality of general procedural law rules, and not strictly limited to the cause of the judgment, which, at the same time, constitutes decisive considerations supporting the given solution and thus the general binding effect imposed on all legal subjects.

In the case of interpretative decisions, the Constitutional Court establishes the constitutional interpetation of a text of law, thus saving the legal provision from its wholly removal from the legal order.

However, there are precedents when the constitutionality control has been adopted by the interpretative powers of judicial bodies, but also of positive legislating powers. By imposing a constitutional interpretation mechanism, the Constitutional Court excludes from application a certain procedural rule of law in a given interpretation or may determine its constitutional meaning even by effectively adding to the text of law of new rules of law, in order to confer to the rule a constitutional meaning.

If the limitation of the application of a text of law capable of several interpretations, by establishing its constitutional meaning, falls within the exercise of the powers of the Constitutional Tribunal"s negative legislature, the same cannot be stated in establishing constitutional interpretation by adding new rules of law. In the latter case, the nature of the legal source of the decisions of the Constitutional Tribunal is evident.

## 4. Effects of Constitutional Court decisions in criminal proceedings – sources of criminal procedural law on invalidity

"The first consequence of the principle of legality is absolute and legal invalidity (Ope Legis), of all acts carried out not in

[25] Published in the Official Gazette of Romania, Part I, no.151 of 12 April 2000;

[26] The Decision no. 554 of the 19th of September 2017 of the Constitutional Court, Published in The Official Gazette of Romania, Part I, no. 1013 of the 21 of December 2017;

conformity with or contrary to the positive rules of Criminal Procedure law."[27]

The Constitutional Court noted [28] that, "the nulities of procedural and legal acts occupy an important place in the sphere of collateral ensuring the effectiveness of the principle of legality of the criminal process and the principle of the finding of truth, being designed to remove infringements of the procedural rules which intervened on the occasion of the establishment of a procedural act or of the proceeding to the fulfilment of a legal act and the negative consequences which those infringements have caused in the criminal proceedings."

The matter of nullity has been reformed by the current regulation, being limited in cases of absolute nullity, with the excluding from the absolute nulities of non-compliance with the provisions on referral to the court, the conducting of the investigation of social responsibility for minors, material competence and the quality of the person of the Court superior to the competent legal authority, as well as the material competence and the quality of the person of the criminal prosecution body and the attenuated sanctioning thereof by the establishment of deadlines to which it may be invoked, as a consequence of the regulation of the preliminary chamber. As regards the exclusion from absolute nulities of infringements of the provisions relating to substantive jurisdiction and the quality of the person of the criminal prosecution body, in the doctrine[29] it was shown that it seeks to avoid exceeding the duration of the reasonable grounds for resolving the cases, the possible harm caused by the conduct of judicial research.

Furthermore, as regards the relative nulities, the relevant is to eliminate the possibility of the judge or court to invoke, on its own motion, the relative nulities and to take them into account at any stage of the process, except in breach of the rules of Material competence or the quality of the person, where the judgment was carried out by a court superior to the competent legal authority and the irregularity of the procedure for the citation of a party.

In the absence of a clearly defined purpose by the legislator and on the basis of the fundamental principle of legality, the Constitutional Court has penalised some of the amendments adopted in matters of nullity, in that regard by stating[30] regarding the provisions of art. 281 para. (1) lit. (b) of the Code of Criminal Procedure, that the legislative solution contained in those provisions, which does not govern in the category of absolute nulities, breaches of the provisions relating to material competence and the quality of the person of the Criminal prosecution is unconstitutional.

The consequence of the decision of the Constitutional Court, definitive and generally binding, is to sanction the absolute nulity of non-compliance with the provisions regulating the substantive competence and the quality of the person of the criminal prosecution body . Although it can be argued that the decision of the Constitutional Court has not been dictated by procedural law, but has established the constitutional meaning of the provisions of art. 281 para. (1) lit. b) of the Code of Criminal Procedure, we cannot omit the fact that the provisions of art. 281 para. (1) lit. (b) of The Code of Criminal Procedure have a clear and strictly delimited

[27] I. Tanoviceanu, *op.cit.*, p. 35;

[28] The Decision no. 554 of the 19th of September 2017 of the Constitutional Court, Published in The Official Gazette of Romania, Part I, no. 1013 of the 21 of December 2017;

[29] C. Ghigheci, The principles of the criminal trial in The Criminal Procedure Code, Universul Juridic Publishing House, Bucharest 2014, p.37;

[30] Decision no. 302/04 May 2017 of The Constitutional Court, Published in The Official Gazette of Romania, Part I, no. 556 of the 17 of July 2017;

content to the material competence and the quality of the person of the Superior Court, and is evident the intention of the legislator to express the removal from the absolute nulity of the infringement of the rules on material competence and the quality of the person of the criminal prosecution body.

An interpretative decision is likely to intervene if the legal norm has several interpretations, one of which is unconstitutional, the Constitutional Court rescuing the provision of law from its inapplicability by preserving the constitutional meaning.

In the present case, we note that the provisions of art. 281 para. (1) lit. b) of the Code of Criminal Procedure, only by an interpretation per a contrario, exclude from the category of absolute nulities the infringements of the provisions relating to material competence and the quality of the person of the criminal prosecution body. Although the latter interpretation was penalised by decision No. 302/04.05.2017 of the Constitutional Court, the direct effect is to establish a new case of absolute nullity, unregulated by law, so of a new rule of criminal procedural law.

Also, by Decision No. 554/2017 the Constitutional Court[31] upheld the exception of unconstitutionality and found that the legislative solution contained in the provisions of art. 282 para. (2) of the Code of Criminal Procedure, which does not allow for the invocation of the relative nullity, is unconstitutional. According to art. 282 para. (2) of the Code of Criminal Procedure, the relative nulity may be invoked by the prosecutor, the suspect, the defendant, the other parties or the injured person, where there is a procedural interest in the breach of the legal provision violated. In that case, the exclusion of the possibility of the judge and the Court of Justice to invoke the relative nulity is apparent from the logical interpretation – per a contrario of the provision which formed the subject-matter of the exception of unconstitutionality.

Both as a result of the fact that in the case of interpretative decisions the legal provision does not cease to have legal effects at 45 days after the publication of the decision of the Constitutional Court if, within that period, the Parliament or the Government, as the case may be, do not put in agreement the unconstitutional provisions to the provisions of the Constitution, but it continues to produce effects in the constitutional sense established and as a result of the general binding effect, by Decision No. 554/19.09. 2017 the Constitutional Tribunal, shall be granted directly to the judge and to the Court of Justice to invoke the relative nulity, although this is not governed by law.

In other words, the Constitutional Court does not remove from application a provision of a law, on the basis of its duties as a negative legislature, is not confined to preserving the constitutional meaning of the legal norm, but penalises the lack of regulation by the establishment of new rules of criminal procedural law, thus constituting a genuine source of law.

It should be pointed out that the object of the exception of unconstitutionality may only form a provision of a law, and not its absence, by decisions given to the Constitutional Court not having jurisdiction to amend or supplement the provisions subject to Control.

Moreover, with regard to the establishment of the constitutional meaning, it should be noted that the reasoning per a contrario, by itself, does not give the legal norm more meanings, but on the contrary, limits the applicability of a provision,

[31] The Decision no. 554/19 September 2017 of the Constitutional Court, Published in the Official Gazette of Romania, Part I, no.1013/21.December 2017;

without extended to unforeseen cases of law.[32]

Although an intrinsic issue of constitutionality is not identified in the aforementioned legal provisions, but only a lack of regulation, and the intervention of the Constitutional Court does not find it justified, we nevertheless consider that the solutions arranged on the merits of the case are in total agreement with the principle of legality of the criminal process, although the legislative powers are the legal power and the interpretation and enforcement of the law is incumbent upon judicial bodies.

In this context, the granting of the character of the source of criminal procedural law to the decisions of the Constitutional Court proves to be an imperative, in this way, the conduct of the criminal process taking place predictably, the consequence that according to art. 147 para. (4) of the Constitution of Romania, from the date of publication in the Official Gazette of Romania, the decisions of the Constitutional Court are generally binding.

That assertion is fully valid in the cases analysed, the sanction which arises in the event of non-compliance with the provisions relating to the jurisdiction of the material and the quality of the person of the criminal prosecution body and the possibility of the judge or the Court of Justice to invoke the relative nulity of its own motion.

However, the task of integrating and applying the new rule of criminal procedural law established by the decisions of the Constitutional Tribunal in the conduct of the criminal proceedings lies with the judicial bodies, without there being any rules for the application of the mandatory character .

Thus, the provisions of art. 281 para. (3) and (4) of the Code of Criminal Procedure, lay down deadlines in which or until absolute nulity can be invoked, depending on the time of the process in which it intervenes.

It is concluded from the economy of the rules of nullity that the legislature expressly limited the possibility of invoking absolute nullity in the criminal prosecution phase after the preliminary chamber procedure was concluded. According to art. 281 para. (4) lit. (a) the Code of Criminal Procedure breaches of the provisions sanctioned with absolute nullity which may intervene in the criminal prosecution phase (set out in article 281 para. (1) lit. e) and F):

The presence of the suspect or defendant, when his participation is obligatory according to the law; the assisting by the lawyer of the suspect or defendant and the other parties, where the assistance is obligatory must therefore be invoked until the procedure is concluded in the preliminary chamber, if the infringement intervened during the criminal prosecution or in the preliminary chamber procedure.

On the other hand, the cases of absolute nullity which may interfere with the preliminary chamber and Judgment (referred to in article 281 para. (1) lit. A)-D): Composition of the trial panel; the substantive competence and personal competence of the courts, when the judgment was carried out by a court lower than the competent legal authority; advertising of the court hearing; the prosecutor"s participation, when his participation is compulsory according to the law may be invoked in any state of the process.

Although the decision of the Constitutional Court No. 302/04.05.2017 concerns the provisions of art. 281 para. (1) lit. (b) of the Code of Criminal Procedure, the infringement of which may be invoked in any state of the criminal proceedings, in determining the period up to which the

[32] I. Neagu, *A Criminal Procedure Treaty, General part, second edition*, Universul Juridic Publishing House, Bucharest,2010, p. 57;

infringement of the provisions relating to material competence may be invoked and the quality of the person of the Prosecution cannot omit the rationale of the limitation of the allegation of absolute nulliity according to the procedural phase in which the infringement took place.

At the same time, the provisions of art. 282 para. (2) and (3) of the Code of Criminal Procedure, govern the deadlines to which the relative nulity may be invoked, without there being a legal provision at present to stipulate whether the judge or court is bound by those deadlines following the decision of the Constitutional Court No 554/19.09. 2017 through which was directly awarded to the judge, namely the Court of Justice, to invoke the relative nulity.

We are therefore witnessing the creation of a vicious circle in which the decisions of the Constitutional Court become sources of criminal procedural law by establishing rules of law, in the case of a legislative loophole inconsistent with constitutional principles, rules such as cover the legislative void but which generate new legislative loopholes by the lack of legal rules governing the application of the new rules of criminal procedural law.

In this situation, it is up to the judicial bodies to interpret the law by analogy or application of the analogue supplement, without being able to invoke the lack of legal provision in the conduct of the criminal proceedings. "The activity leading to the realisation of justice repressive must necessarily follow its course and reach the end. The law of Criminal Procedure disciplines this activity, but in the course of its conduct may arise exceptional situations, which have escaped the legislature"s provision and are therefore not governed by the law. The silence of the law does not dispense with the interpreter to settle the new situations, so the repressive activity would remain suspended and condemned to abandon.

While the interpretation of the substantive criminal law when it finds that the law is silent, absolses and terminates the prosecution, the interpreter of criminal procedural law, has to make the law speak even when it is silent, because it owes the action repressive to the end."[33]

In this respect, in the doctrine it was shown that "then, when the gaps in the criminal Procedure Law cannot be fulfilled by an extensive interpretation, it will necessarily have to resort to the analogue supplement.

For this it will be sought in the law of Criminal Procedure if there is no express provision regulating in another matter a situation or a similar report. If there is such a provision then the completion of the gap by analogy may be accepted if we encounter the same conditions as they make interpretation possible by analogy."[34]

Application of the interpretation to the case in question, in relation to the reason for the imposition of the deadlines for invoking absolute nullity, namely the limitation of the possibility to invoke infringements of the provisions sanctioned with absolute nullity in the follow-up phase following the preliminary chamber procedure, invoking the infringement of the provisions relating to material competence and the quality of the person of the criminal prosecution body will not be able to take place in any state of the process, but only until conclusion of the procedure in the preliminary chamber, according to art. 281 para. (4) lit. A) of the Code of Criminal Procedure.

Things are different for the time limit by which the judge or court may invoke the relative nulleness. In this respect, the recitals of Decision No. 554/2017 of the

[33] I. Tanoviceanu, *op.cit.*, p. 49;
[34] *Idem*, p. 50;

Constitutional Court, which also enjoys the general binding effect, which has established that the possibility of a relative nullity is required "in the light of the outcome of the procedure in the preliminary chamber concerning the determination of the legality of the administration of evidence and the conduct of procedural acts by the prosecution authorities, has a direct influence on the conduct of the judgment on the merits, which may be decisive for the determination of guilt/innocence of the defendant (...) and as regards the role of the court at the trial stage of the criminal proceedings, the court considers that such a legislative solution — which does not allow, as a rule, the claim of relative invalidity of its own motion — cannot be justified only by the philosophy of the restriction of the active role of the court and, in general, by rethinking the system of criminal proceedings, in the sense of its approximation, in certain respects, by the adversial system. In this respect, the Court notes that, unlike the adversial system, in which the judge bears responsibility, in principle, solely on the correctness of the conduct of the proceedings, the task of establishing the facts and the guilt of the jurors, in the Romanian criminal process the court also assumes responsibility for these essential elements, which constitute the purpose of the process —-the determination of the offence and the guilt."

Therefore, the possibility for the judge and the court to take account of its own motion of the relative nullity is required on the basis of the principle of finding the truth and for the full clarification of the circumstances of the case.

However, that judgment is not attained in the event of limitation of the possibility of relying on the relative nullity by the court under the conditions of art. 282 para. (2) and (3) of the Code of Criminal Procedure, namely in the course or immediately after the act or at the latest until the closure of the preliminary chamber procedure, if the infringement intervened during the prosecution or in this proceeding, until the first period of judgment with the legal procedure fulfilled, if the infringement intervened in the course of prosecution, when the court was seised of an agreement to recognise the guilt, until the next period of judgment with the full procedure, if the infringement intervened during the judgment.

Without identifying, in this case, express provisions regulating a similar situation or report and fully agreeing with the rules of compulsory procedural law laid down in the decision of the Constitutional Court, the judicial bodies will appeal to the systematic interpretation consisting, "in the clarification of the meaning of a legal rule by linking it with other provisions belonging to the same branch of law."[35]. Therefore, "from all the methods of interpretation will be used with priority in interpreting the rules of criminal Procedure all those methods that allow to the interpreter to converge towards the fundamental principles of Criminal procedure. Also between two methods of which one leads to a solution in accordance with these principles will be given priority to the latter. "[36]

Consequently, by a systematic interpretation it can be concluded that the judge of the preliminary chamber will be able to invoke the relative nullity when it is necessary to find out the truth and to resolve the case until the closure the preliminary chamber procedure, including in the procedure governed by the provisions of art. 347 of the Code on Criminal proceedings, to resolve the appeal against the conclusion of the preliminary chamber. As regards the

[35] I. Neagu, *op.cit.*, p. 56;
[36] I.Tanoviceanu, *op. cit.*, p. 46;

court, I conclude that, on the basis of the same arguments, the court will be able to invoke the relative nullity in any state of the criminal proceedings, that interpretation being consistent with the principle of legality of the criminal process and the finding of the truth.

## 5. Conclusions

The law constitutes the foundation of the principle of legality, and its observance is imperative in conducting the criminal proceedings. As an activity governed by law, but which also knows legislative loopholes and is not permitted to abandon the law, it is necessary to exclude equivalence between criminal procedural law and the source of criminal procedural law, with a wider area of existence.

The extensive interpretation of the notion of criminal procedural law encompasses both primary and secondary legislation, which comes to detail the rules of law, within the limits and conditions imposed by them. However, the rules of criminal procedural law are not confined to the law lato sensu, with the obligation to comply with compulsory jurisprudence, including the decisions of the Constitutional Court and the compulsory interpretation of the legal norms by Judicial bodies.

The establishment, mainly of the notion of criminal procedural law, led to the exclusion of the possibility of granting this nature to the decisions of the Constitutional Tribunal and their attribution of the nature of the source of criminal procedural law. Although the autonomous sense of the notion of law encompasses the concept of the European Court of Human Rights and the case-law, a single decision, even with a generally binding effect, does not satisfy the conditions for a consistent and crystallized practice over a long time. Therefore, I conclude that the decisions of the Constitutional Court do not fall within the notion of criminal procedural law, this possibility remaining open to the constant and lengthy case-law subsequently developed on the basis of the general binding effect of Constitutional Court decisions.

The affirmation of the nature of the criminal procedural law, the decisions of the Constitutional Tribunal, even in the absence of legislative intervention to implement the rules not conforming to the constitutional principles, are supported by the mandatory general effect of those stated by the constitutional authority.

Both the judicial bodies and all other participants in the criminal proceedings will also be held equally in compliance with the rules of criminal procedural law established by the decisions of the Constitutional Tribunal, which are governed by the principle of Fundamental nature of the general legality of the Romanian Constitution.

The impact of the lack of provision of a text of law or of sanctioning it through the decisions of the Constitutional Tribunal and the establishment of new rules of criminal procedural law conveys to judicial bodies the task of identifying the most optimal solutions in conducting the criminal process in agreement with the principle of legality. The interpretation by analogy or application of the analogue supplement is not contrary to the principle of legality, as the basis for any interpretation is the fundamental principles of the criminal process, including that of legality.

However, sanctioning the legislative void through the intervention of the Constitutional Court and its complacement by new rules of law lacking rules of application and integration as a whole of the regulation of the criminal process, in addition to the fact that it establishes as a responsibility of the Judicial bodies a much

too large burden, lacking predictability in the conduct of the criminal process.

The evolution of the case-law of the Constitutional Tribunal remains an open topic, with the aim of crystallizing or not its character as a source of criminal procedural law. Likewise, the passiveness of the legislature in fulfilling the obligation to agree unconstitutional provisions with the provisions of the Constitution requires a thorough analysis in order to justify the full transmission to the judicial bodies of the duty to comply with the principle of legality, although in this respect the main task lies with the legislator by providing for legal rules

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# THE PROCEDURE FOR THE REFERRAL OF THE CRIMINAL INVESTIGATION BODIES

**Denisa BARBU***

**Abstract**

*Vintil Dongoroz mentioned in one of his books that "the referral is the dynamic act that causes the prosecution to take place." We can say that the criminal prosecution is born when the criminal prosecution bodies are informed of a crime of a criminal nature by one of the above mentioned ways of referral.*

*The common point of all means of referral is that it always takes the written form, either by direct recording of the injured party or by the oral hearing. In practice, the document of referral is the document which will always contain the registration number of the prosecutor"s office and the resolutions of the hierarchical chiefs on the registration procedure and the worker to whom the work was assigned for verification and settlement.*

*The referral is the effect of a manifestation of will for the purposes of conducting criminal proceedings that may be brought by the criminal investigation body, the finding body or the injured party whose interests or rights have been violated as a result of committing an offense.*

*Any criminal offense brought before the categories of civil servants mentioned in this Chapter shall lead to their obligation to immediately notify the competent prosecution body. Also, the criminal investigation body should refrain from carrying out any criminal investigation if it clearly finds that it is not competent and the investigation is not urgent.*

**Keywords:** *jurisdiction, obligation, Criminal investigation, competence, the procedure*

## 1. Introduction Ways of Referring to Criminal Investigation Bodies

### 1.1. The Complaint

The most common way to refer criminal prosecution bodies is the complaint through which individuals can address the authorities by making them aware that they have been the victim of a crime.

Any complaint may be made in writing or by oral proceedings where the criminal investigation bodies record a report. This is done in his own name or by the trustee in a situation where a procuration is attached, by procedural substitutes or by legal representatives instead of persons without exercise capacity.

*Practical aspect:*

- On 15.05.2014, at 15.15, at the Police Headquarters of the Municipality of Târgu Mureș was presented named G.R. together with the minor G.F. who verbally reported the following: about one hour before, his child returned from school without having a Samsung mobile phone on it, and the child told him that his mobile phone would have been taken from the desk at the last hour when he had physical education.
- The police have recorded a report containing the data of the legal representative, the verbal ones, and the

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mention that they require identification of the perpetrators of the offense of theft. Following the notification, the criminal investigating authorities carried out criminal investigation activities which ultimately led to the identification of the authors.

The Code of Criminal Procedure states that the complaint may also be filed in electronic form, subject to the existence of an electronic signature. As regards the notion of electronic signature, it is defined in Article 4 (3) of the Law No. 455/2001 republished as data in electronic form that are attached or associated with other data also in electronic form, which will serve as an identification method. The electronic signature cannot take the form of the scanned signature.[1]

In practice, there is a situation where the author of the offense is the legal representative and an ex officio referral is recorded in this respect.

*Practical aspect:*

- On 14.02.2015, at 18.00, T.R presented herself at the headquarters of Onesti City Police, who notified the police that his son T.I. left the park to play in the nearby park and did not return. Police officers carried out specific activities to find the minor, and around 21:00 it was legitimized by a police patrol and was led to the police headquarters to record a report and hand him over to parents. Considering that the minor showed marks on the surface of the body, the police asked him about the origin of these signs, and the child reported verbally that they were made after the beatings he receives almost daily from his mother. Taking into account the visible traces of the juvenile"s body and those reported by him, the police officers as observers have been notified of the offense of "ill-treatment of the minor" and the case was taken over by the criminal investigation bodies who developed specific activities, also helped by a psychologist.

With regard to the form of the complaint, the complaint must contain the name, surname of the person who is making it, accompanied by the personal numerical code, the quality and domicile of the complaint, and, in the case of legal persons, the name, headquarters, single registration or fiscal identification code and indication legal or conventional representative. After these data the complaint describes the description of the act that he wants to claim, and the author indicates if it is known and non-mandatory to indicate the means of evidence that he considers necessary to be administered in order to prove the deed. Also, the injured party is not obliged to record the legal framing of the act or if the criminal prosecution bodies do not have the obligation to fit the act exactly as indicated, but how it considers it necessary. If the complaint is missing at least one of the mandatory conditions of the form, the petitioner shall be remanded by administrative means and shall indicate the missing items, and in the case where one of the substantive or formal conditions, for example the lack of all the name of the petitioner or the description of the deed, it is classified.[2]

Due to the fact that not all persons have legal education, they are unaware of the legal framing of the act they wish to claim, nor of the competence of the criminal investigation bodies or the courts. Thus, the wrongly directed complaint is submitted by administrative means to the competent judicial body. If the criminal investigation body draws up the order to initiate the criminal proceedings in rem on the basis of the complaint, the prosecutor will send the complaint to the competent body without taking into account the form of the refusal,

[1] Legea nr.455/2001 r. Art.4, pct.3

[2] Mihail Udroiu. *Procedură penală. Partea specială 2017*, Ed. Universul juridic, p. 26.

except in the case in which the prosecutor starts the prosecution.

*Practical aspect:*

- On 11.05.2015, at 09.00 at the Breaza City Police Headquarters, the so-called F.H. who filed a complaint in which it was recorded that on 10.05.2015, at 22.50 while listening to music in front of block No. 2, on Peace Street, together with a friend, two gendarmes presented, dressed in uniform that hit their bodies with sticks and sanctioned them for their contravention. He wanted to file a criminal complaint for the offense of hitting or other violence. Given that the Gendarmerie workers have the military status, the complaint was filed administratively with the Military Prosecutor"s Office attached to the Bucharest Military Tribunal for the investigation of the offense of abusive behaviour.

### 1.2. Denunciation

Any natural or legal person, even if he is not the injured person, has the possibility to inform the criminal prosecution bodies about the existence of any offense by denunciation.

Denunciation is a voluntary referral method that can be made by a natural or legal person without any legal obligation to do so. Exceptions make certain situations where denunciation becomes mandatory if the person has become aware of the commission of any crime. In this respect, the legislator incriminated at art. 266 para. (1) Criminal Code the offense of non-forfeiture which consists in a person"s act of not announcing the authorities, even though he was aware of an offense provided by the criminal law against life or that resulted in the death of a person. It is also stipulated in art. 410 par. (1) of the Criminal Code, the offense of non-infringement of national security crimes thus criminalizes the person"s deed to do so in the event that he has been informed of the preparation or committing of any offense that is likely to affect national security.[3]

There are situations in which the denouncer may be the person who committed the offense and thus benefit from the removal of criminal liability as a cause of non-punishment.

*Practical aspect:*

- On 14.09.2014 R.E. turned-out at the headquarters of the General Anticorruption Directorate - Argeş County Service, and filed a complaint about the fact that an employee of RAR Pitesti requested and received the amount of 500 lei to make his technical inspection of his BMW 3 Series without passing it through all the verification means. The DGA workers received the denunciation and under the direct coordination of a prosecutor within the Prosecutor"s Office attached to the Argeş Tribunal, investigated the denounced person, investigating activities that led to the identification and probation of several RAR employees receiving regular bribes for various services who were circumventing the proper performance of their duties. Since R.E. filed the denunciation before the criminal investigative bodies had been notified, he benefited from the elimination of criminal liability.

Also, self-denouncement may also have the value of a mitigating circumstance.

*Practical aspect:*

- On 20.08.2014 the workers of the Giurgiu Organized Crime Prevention Service under the coordination of a prosecutor within the DIICOT - Giurgiu Territorial Office carried out a flagrant, resulting in the fact that the DV received for resale from the named RT a number of 22 sachets containing a white powder, possibly cocaine. Being faced with clear evidence and

[3] V. Răмureanu,*Proceduri penale*, Bucuresti, 2016, Universul Juridic Publishing House, p. 28.

at the request of his lawyer, the defendant R.T. filed a complaint with the criminal investigating authorities about the persons who supplied him with high-risk drugs, as well as with other individuals on the same criminal level as he. Thus, the criminal investigating bodies initiated specific activities to investigate the facts, with 12 persons being prosecuted and the denouncer benefited according to art.15 of the Law no.143/2000 on the prevention and combating of illicit drug trafficking and consumption, to halve the penalty limits prescribed by law. Concerning the so-called D.V, it is worth mentioning that the flagrant was carried out following its denunciation and thus benefited from the provisions of art. 14 of the Law no. 143/2000 his deed was not punished because it was brought to the attention of the authorities before the criminal prosecution had begun.

A denunciation is made only personally, and if he is a person with restricted exercise capacity through his legal representative. There is a situation where the person who has been denounced by a person is his legal representative or a person who agrees with his acts if he has limited exercise capacity. In this case, the prosecution is made ex officio.

The denunciation having a written form must fulfil the formal requirements in the sense that it contains the name, surname, personal numerical code, its quality and domicile, and for legal persons the name, the registered office, the unique registration code, the fiscal identification code, the registration number in the trade register. Once personal data have been recorded, the description of the reported criminal offense, as well as the indication of the perpetrators and evidence, if known by the denouncer, must be given. The lack of one or more of these form elements involves redressing the administrative complaint by indicating the missing elements, and in the absence of an essential condition as the author"s identification data or the description of the act is incomplete or unclear, the organs of tracing criminal will dispose the classification.

*Practical aspect:*

- The workers of the Criminal Investigation Bureau of the Barlad City Police received by e-mail a denunciation from Popescu Robert stating that on 25.08.2016 he passed the Urological Department of the Emergency County Hospital at the 3rd floor where a person was screaming from pain, which is why the denouncer wishes to be held accountable the medical personnel for negligence in the service. Police officers proceeded to identify the denouncer and found that his identity could not be accurately determined, the sending address did not exist, and the databases contained a large number of people with that name. Regarding the description of the deed, the criminal investigating bodies have determined that the injured person cannot be identified because the name or even the ward in which he was present was not indicated and the concrete way of committing the negligence offense was not described in the notification. Taking into account the findings of the investigation bodies, they solved the denunciation in the form of a petition and did not find any real aspects of criminal nature, for which reason they ordered its classification.

If the denunciation is anonymous, it can not be considered as an act of indicating the criminal prosecution bodies, but the judicial bodies have the obligation to verify the veracity of the issues raised and if they find that they confirm, they will initiate the prosecution.

*Practical aspect:*

- On May 14, 2014 at the Police Headquarters of Constanţa Municipality an e-mail was received regarding a

denunciation from several detainees of Poarta Albă Penitentiary. The denunciation was anonymous, no name or surname being indicated, but it was brought to the knowledge of the criminal investigation authorities that the prisoner of F.L. of Cell No. 12, Body B boasts that he cheated more elderly people by "the accident method", earning big sums of money. In his criminal activity he uses a cell phone and several phone cards illegally obtained from other detainees and is helped by his former concubine N.E. who presented at the home of injured people to take money or jewellery from them. Considering that several facts of this kind were reported in the district of Constanţa County, being left with an unknown author, the criminal investigating authorities heard of themselves and under the supervision of a prosecutor they were able to prove the criminal activity of the detainee F.L. and the so-called N.E., investigations that were uncovered by a flagrant on 18.08.2014.

As in the case of the complaint, the denunciation may also have electronic form, subject to the existence of an electronic signature, and in the oral case, the criminal investigative body will record it in a minutes and then hear it in witness quality.

### 1.3. The referrals made by leadership persons or other people

On the same level with the complaint and the denunciation as a way of indicating the criminal prosecution bodies, there is the referral made by the persons with leading positions or by other people, being regulated in art. 291 para. (1) of the New Criminal Procedure Code. They are obliged to immediately notify the criminal investigating bodies the persons who hold leading positions within the public administration authorities or other public authorities, public institutions or other legal persons of public law who, in the exercise of their duties, have learned of the existence of any offenses. It is also the duty of the persons who have control duties when, in the exercise of their duties, they have been aware of the commission of any offense. These people can be part of public institutions, but also of private entities with their own control mechanisms. Also in the provisions of Article 291 are included those persons exercising a public interest service which have been invested by the public authorities or are subject to their control or supervision and in the exercise of their official duties have been aware of the existence of any crime, bailiffs, lawyers in the performance of certain tasks, notaries public.[4]

These referrals apply only to offenses for which the criminal action is initiated ex-officio and must have the content of a denunciation. We note, therefore, that this way of referral essentially takes the form of a mandatory denunciation.

Also included in this category are the minutes drawn up by the finding bodies listed in Articles 61 and 62 of the New Code of Criminal Procedure. They no longer resume the description and their examples, since both the theoretical and the practical part are entirely applied by the section of the finding bodies.

The public order and national security bodies shall draw up a report in the event of a finding of a criminal offense. This act has a dual function both as a means of referring the criminal prosecution body being provided in art. 288 para. (1) referring to art. 292 of the new Code of Criminal Procedure and as a means of proof provided in art. 198 par. (2) New Code of Criminal Procedure.

[4] Phd Judge Voicu Puşcaşu, Phd Judge Cristinel Ghigheci, *Proceduri Penale*, Vol. 1, pp. 41- 42.

In this category is also included the conclusion of a hearing made by the court in the case of the offense of audience.

*Practical aspect:*

- On 9 May 2014, 10 a.m., at the Iasi Tribunal, several defendants accused of criminal grouping, trafficking and money laundering have been tried. The public hearing was attended by defendants, including D.L. what managed to bring a gun with ammunition into the courtroom. When M.S. had to speak, D.L. pulled out a gun and directed it to the witness, but the trigger was not perturbed because the hitch was not drawn and a representative of the guard intervened. In this case, the referral was constituted by the closing of the sitting, and the prosecutor present in the court took over the case by immediately ordering the continuation of the criminal prosecution and taking the measure of apprehension of the accused person that he intended to kill the witness M.S.

### 1.4. The ex officio referral

Article 292 of the New Code of Criminal Procedure stipulates the way of the ex officio notification, so the criminal investigation bodies, if they have become aware of the committing of a crime in a different way than the complaint, denunciation or notifications made by persons with leading positions are bound to record an ex officio referral.

Starting from the ex officio notification of the criminal prosecution body, either personally proceeds with the prosecution, or hand it over to the competent prosecution body by administrative means.

As we have previously stated in the case that the complaint or denunciation does not meet the substantive or lawful conditions, the criminal investigation bodies can check the issues raised and, if it finds that they may be relevant, draws up a minutes from which they refer from office. A practical example was opened at the denouncing session.

One of the usual sources of information from which the criminal prosecution authorities complain ex officio is the media.

*Practical aspect:*

- On April 22, 2014, in the local press, in Neamt County a press article entitled "Find out who poisons the water in Bicaz Dam" appeared. It was mentioned in the article that a slaughterhouse in Bicaz-Chei drove dead animal remains in the Bicaz River, which later collapsed in the Bicaz Dam and became an outbreak of infection. Taking into account the ones mentioned in the press article, the criminal prosecution bodies heard of the offense of water infestation, and in the course of the criminal investigation it was ascertained that the reported issues are true.

In a rule of law, there are also specialized bodies with the objective of maintaining national security. These structures carry out specific investigative activities and the information obtained is confidential. Criminal Investigation Bodies have access to classified information up to various levels of classification according to the specifics of work, so they can be notified of offenses, but they can not use the documents they receive because they are not intended to be advertised. In order to capitalize the information it is necessary to initiate the criminal prosecution which starts from the official act of the ex officio notification.

*Practical aspect:*

- A specialized structure on the maintenance of national security carried out the specific investigation activity towards the foreign citizen I.H. As a result of the investigations, it has been shown that he travels regularly to Turkey by airplane and has more Romanian citizens known to be part of the so-called "underworld",

suspected of dealing with drug trafficking. Given that I.H. has a very high standard of living, with no visible source of revenue, and several people said they were buying high-risk drugs from Turkey that they made available to the interlopes, the structure informed D.I.I.C.O.T. prosecutors have heard of their case and initiated the prosecution.

In the case of offenses found in the flagrant, the minutes to be drawn up on this occasion constitute an act of indicating the criminal prosecution bodies, and the injured persons of the offense found may file a complaint.

If the information is accurate, no matter how they get to the criminal prosecution body, this is obliged to complain of its own motion.[5]

### 1.5. Preliminary complaint

Another way of indicating criminal prosecution bodies is the prior complaint in the form of a regular complaint, the difference being that the existence of this complaint makes the criminal action in the case of criminal offenses conditional. The existence of the prior complaint does not give rise to the obligation of the criminal prosecution bodies to order the commencement of criminal prosecution, the continuation of the criminal prosecution of the suspect or the commencement of the criminal action.

The prior complaint must meet the formal and substantive conditions, just as for a regular complaint, and in the absence of one or more of such elements, it is returned administratively by indicating the shortcomings.

The preliminary complaint is made in written or oral form, in which case the criminal investigative body records a report in this respect. This can be done both personally and for another person by procuration, and the New Code of Criminal Procedure stipulates that the prior complaint may be advanced electronically, subject to the existence of an electronic signature, just as with the other means of notification.

The injured person may be deprived of his/her capacity to exercise and the prior complaint may be made by his/her legal representative, and if he/she has limited exercise capacity, he may be personally made with the consent of the persons provided by the civil law. If the perpetrator is even his/her representative, the criminal prosecution bodies may order the commencement of criminal prosecution, the continuation of criminal prosecution of the suspect and the bringing of criminal proceedings, by virtue of the fact that, exceptionally, the existence of the preliminary complaint on certain offenses. Another exception to this rule is where the author is even the representative of the legal person whose interests should be protected.[6]

If we are in the situation of the provisions of art.199 of the Penal Code on domestic violence, where the commencement of the criminal action is conditioned by the existence of the preliminary complaint and the withdrawal of the preliminary complaint takes place, the prosecutor shall decide whether or not the will of the injured person, having the possibility to continue the prosecution as it deems necessary.

*Practical aspect:*

- On May 15, 2015, R.E. has filed a preliminary complaint, for the offense of hitting or other violence, against her husband, R.L., by making available to the criminal investigation authorities and a medical certificate, certifying that after the blows received it required 11 days of medical care. Subsequently, on 18 August

[5] PhD Judge Voicu Puşcaşu, PhD Judge Cristinel Ghigheci, *Proceduri Penale, Vol. 1*, p. 44.
[6] Mihail Udroiu. *Procedură penală. Partea specială*, 2017, p. 23.

2015, she appeared before the criminal prosecution authorities saying she wanted to withdraw his previous complaint. Since the evidence-based economy shows that for R.L. this is not the first offense of this kind, and two more criminal cases have been filed in the last year by withdrawing the preliminary complaint and the perpetrator is known as a very violent person, it is concluded that he presses the injured person in order to withdraw the preliminary complaint, which is why the prosecutor considered it necessary to continue prosecution with regard to the suspicion and the initiation of the criminal action as finally to forward the file to the competent court.

When referring to the existence of the prior complaint we also consider the active or passive indivisibility of criminal liability in the sense that if the preliminary complaint was formulated only by one of the injured persons although there are several persons who have been injured the author will answer the criminal as well if the prior complaint concerns only one person, the prosecution will extend to all the perpetrators of the crime regardless of whether they are authors, co-authors, instigators or accomplices.

As regards the procedural period of revocation, the New Code of Criminal Procedure establishes it at 3 months from the day when the injured party learned of the act and does not take into account whether at the time when he learned of the criminal offense he knew the author or not. If the injured party is a minor or an incapacitated person, the term of revocation shall run from the time when his legal representative has learned of the existence of the deed. It has been concluded in the case-law that in the case of an abuse of trust which is committed by the refusal to return a good, the period of decline begins to run from the moment the author has given his first refusal, a solution given by the Bucharest Tribunal. Also regarding the introduction of the preliminary complaint, we encounter a situation in which the mediation between parties is interrupted, and the mediation period is not taken into account when establishing the term of introduction, being considered suspended.[7]

In the case of flagrant finding of the offenses of which the criminal proceedings are triggered, is conditioned by the existence of the preliminary complaint, the criminal prosecution or finding body shall be obliged to state the perpetrator, to record the minutes, then the criminal prosecution body to ask the injured person if he/she wants to file a preliminary complaint.

*Practical aspect:*

- On May 14, 2015, a patrol of public order and safety, moving in the area of the block parking, in the city of Sinaia, surprised the named E.F. while hitting the door of a car. The author of the deed stated verbally that he had made this gesture because the car is parked on the place he usually parked. The police have drawn up a verbal record of the flagrant crime for destruction, and the criminal investigation authorities have identified the owner of the car that said he did not want to file a criminal complaint for the crime of destruction. A criminal case file was drawn up on the basis of the minutes and was submitted to the prosecutor"s office for classification, as the preliminary complaint was missing.

If the criminal prosecution for an offense has started and the legal classification of a criminal offense has subsequently changed depends on the existence of the prior complaint, the criminal prosecution bodies will ask the injured person if he wishes to make a preliminary complaint and the term for the forfeiture flows from that time.

[7] Mihail Udroiu. *Procedură penală. Partea specială*, 2017, pp.24-25.

### 1.6. Conclusions

The common point of all the means of referral is that it always takes the written form, either by direct recording of the injured person or by the oral hearing. In practice, the document of referral is the document which will always contain the registration number of the prosecutor"s office or, as the case may be, of the criminal prosecution body and resolutions of the hierarchical chiefs on the registration procedure and the worker to whom the work was assigned for verification and settlement.

The referral is the effect of a manifestation of will for the purpose of conducting criminal proceedings that may come from the criminal investigative body, the finding body or the injured person whose interests or rights have been violated as a result of committing an offense.

The referral is the procedural act by which a natural or legal person addresses the criminal prosecution body in order to achieve the object of criminal prosecution. The referral may refer to a partial or complete description of the offense, and the criminal investigative body is required to discover and collect material evidence to lead to the truth, even if some aspects are not to the liking of the person who made the referral.

According to the Code of Criminal Procedure the act of referral is not a material means of evidence, except for the rule, it makes the report of the flagrant offense.

The lack of the referral makes it impossible to draw up a procedural act of subsequent criminal prosecution such as the commencement of criminal prosecution, the continuation of criminal prosecution of the suspect or actuating criminal prosecution. The prosecutor or the criminal investigating body refers to the manner in which they are referred in most of the procedural or procedural acts that they draw up. Thus, the prosecutor reminds the act of referral in all the ordinances he makes when conducting the criminal prosecution.

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