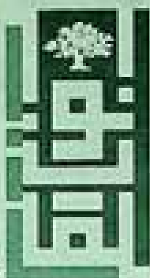

جامعة بيرزيت
BIRZEIT UNIVERSITY
INSTITUTE OF LAW
معهد الحقوق

Essays on The European Economic and Financial Integration: Selected Legal Aspects

2013

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Birzeit University

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Lifelong Learning

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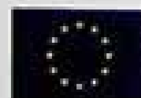
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Foreword

With support from the Jean Monnet Programme "Lifelong Learning Programme", the Institute of Law (IoL) at Birzeit University conducted a research project to examine selected legal aspects of the European Economic and Financial Integration. The research project was designed to achieve the following goals:

1. Support the development of specialised research, conducted by national and international experts on legal issues of economic and financial integration.
2. Reinforce awareness and initiate attention by official bodies, universities, research centres and civil society organisations to the EU integration approach.
3. Promote debate locally and in the Arab world on the integration theory in order to identify the opportunities for legal convergence regionally and their potential impact on the economic and financial development process in Palestine and the Arab World.

The research project was divided into several phases, including a) literature review, b) discussions with key experts and players, c) drafting of a document outlining issues and trends pertaining to dealing with issues of European Economic and Financial Integration, and c) release of a call for papers document, inviting interested researchers to contribute to the project's future activities. The project was able to bring into the discussion national and international experts and other parties with interest, and engage a larger than expected group of experts in researching various aspects of the questions the project focused on.

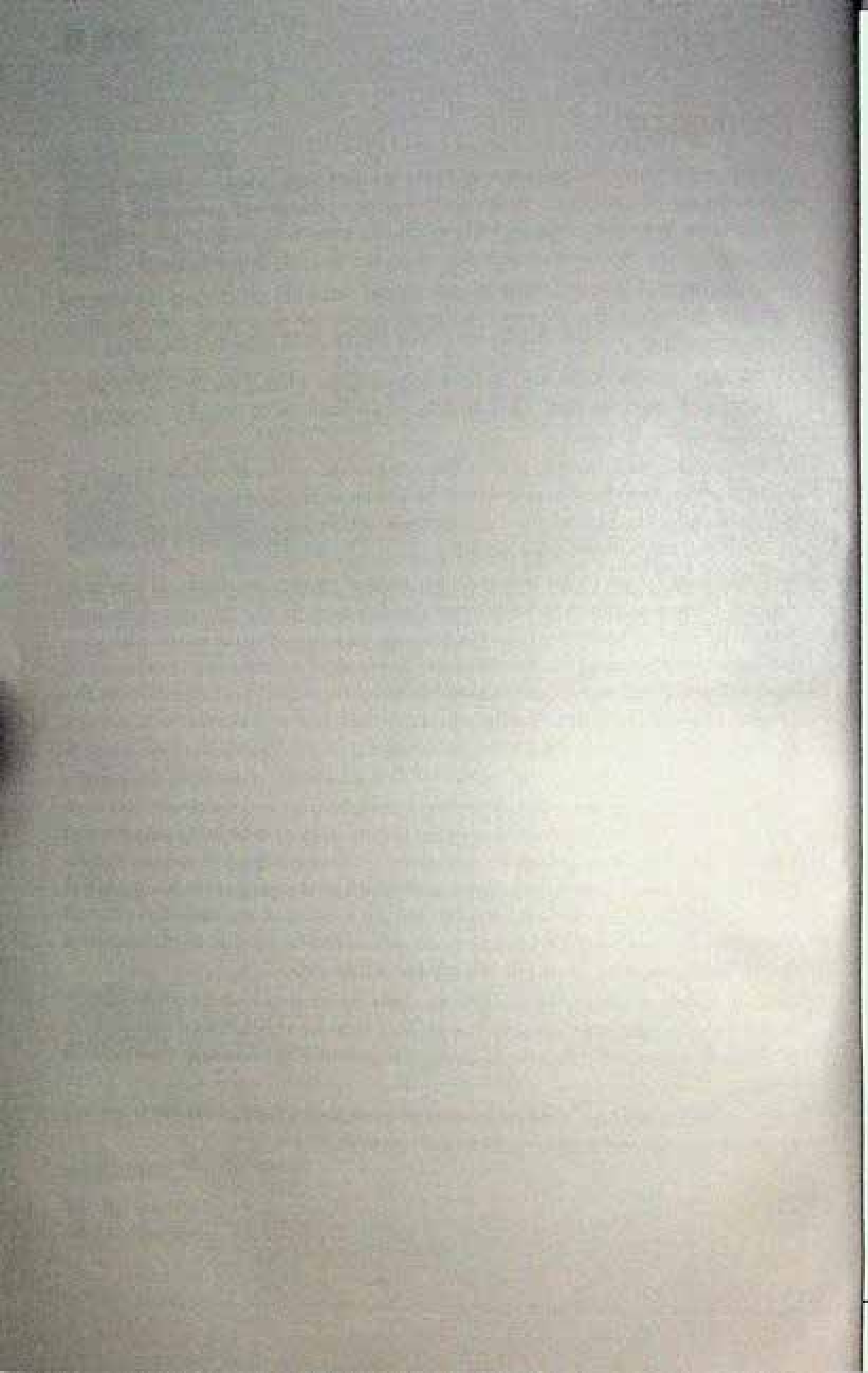
Through the project activities, including a workshop and a conference, that were organized and held at Birzeit University, the IoL was able to bring experts and people with interest together for discussion and modalities and approaches for dealing with the issues of economic and financial integration. In addition, the research project has made it possible for the IoL to put the edited version of the seven articles produced in this book, which can be used as a reference and guide for similar discussions in Palestine and beyond.

The IoL highly appreciates the efforts made by all those who contributed to making this publication a reality. The IoL also extends special thanks to the Jean Monnet Programme "Lifelong Learning Programme" for funding the research project.

Finally, the IoL reiterates its commitment to initiating further research studies examining legal and economic phenomena in Palestine.

Jamil Salem

Director of the
Institute of Law



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Chapter one

The Extension of Exclusive EU Common Trade Policy to Foreign Direct Investment

Chapter one

The Extension of Exclusive EU Common Trade Policy to Foreign Direct Investment

Walid Ben Hamida

University of Evry Val d'Essonne and Sciences Po, Paris

Introduction

The Lisbon Treaty includes foreign direct investment in the scope of Common Commercial Policy. This extension raises much controversy regarding the extent of this new area of competence on the status of existing BITs concluded by member states and third countries, and on the content of future investment agreements made by the European Union.

The Lisbon Treaty of December 1st2009 has added "[f]oreign direct investment" (FDI) to the list of issues belonging to the exclusive EU common trade policy (Article 207 of the Treaty on the Functioning of the European Union). The implication is that EU Member States are no longer able to continue their practice of concluding international investment treaties that concern FDI and that the European Union will assume their competences.

Prior to the application of the Lisbon Treaty, the EU's main competence concerned aspects related to foreign trade. The main competence of the Member States, however, concerned foreign investment. While the EU pursued the liberalisation of trade, particularly through its trade agreements with non-EU countries, the Member States remained free to enter into Bilateral Investment Treaties (BITs) with these countries.

BITs are international agreements concluded between two countries for the protection of investments made by an investor from one country in the territory of the other. BIT stypically offer investors: national treatment, most-favoured-nation treatment, fair and equitable treatment, compensation in the event of expropriation and the free transfers of funds. However, the most significant feature of BITs is that they, in almost all cases, allow investors to bring claims against the host State for violations of the treaty directly to legally binding international arbitration. Germany was the first nation in the world to conclude a BIT, in 1959, with Pakistan. Since then many countries around the world, including all EU states (except Ireland),

have followed suit. With a total of almost 1350 agreements covering all forms of investment, Member States together account today for almost half of the investment agreements currently in force around the world.

The practical consequence of this division of competences is that all international agreements that cover both trade and investment must be concluded as mixed agreements. A mixed agreement is an international treaty concluded by both the European Union and the Members States in which both the Member States and the Union must ratify it and give their consent to it being enforced. This is certainly the case for the World Trade Organisation (WTO) Agreement as it applies to both trade and investment. For example, commercial presence regulated in the General Agreement of Trade in Services (GATS) concerns the establishment of foreign investors. This is also the case of the Energy Charter Treaty (ECT),[1] signed in December 1994 and entered into force in April 1998. To date the Treaty has a total of fifty-four Signatories (fifty-two states, plus the European Community and Euratom). The ECT is an international agreement that establishes a multilateral framework for aspects of commercial energy activities including trade, transit, investments and energy efficiency. The Euro-Mediterranean Association Agreements - concluded between 1998 and 2005 with seven countries in the southern Mediterranean - regulate both trade and non-trade issues. Joint membership of the European Community and its Members was therefore required.

The Lisbon Treaty, by including it in the scope of the Common Commercial policy, establishes for the first time an expressed competence over foreign direct investment.[2] This inclusion was the most important expansion of EU competences as it empowered the Union to take external action in most fields of foreign investment regulation by establishing a single legal basis.[3] The central aim of this new competence is to enable the EU to benefit from increased bargaining power, thus allowingit, hypothetically, to "stand up to all major powers".[4]

The entering into force of the Treaty of Lisbon on December 1st 2009 and the consequent extension of common trade policy to foreign direct investment raises many questions. This article will try to answer the following: (I) What is the extent of this new area of competence? (II) What will be the legal status of BITs that were concluded by the Member States before the Lisbon Treaty? (III) How will the EU use its newly acquired powers with third states?

I. The scope of the new FDI competence

The provisions on the common commercial policy in the Treaty on the Functioning of the European Union (TFEU) can be found in Articles 206 and 207, which amend and modify former Articles 131(1) and 133 of the Treaty Establishing the European Community (TEC). Article 206 contains this specific trade policy objective: "[b]y establishing a customs union in accordance with Articles 28 to 32, the Union shall

contribute, in the common interest, to the harmonious development of world trade, the progressive abolition of restrictions on international trade **and on foreign direct investment,** and the lowering of customs and other barriers".[5] The progressive abolition of restrictions on foreign direct investment therefore becomes a new objective of EU trade policy.

The key provision in this regard, however, is Article 207(1) of the TFEU. It expressly added FDI to the treaty-making power of the European Union:

> [t]he common commercial policy shall be based on uniform principles, particularly with regard to changes in tariff rates, the conclusion of tariff and trade agreements relating to trade in goods and services, and the commercial aspects of intellectual property, **foreign direct investment,** the achievement of uniformity in measures of liberalisation, export policy and measures to protect trade such as those to be taken in the event of dumping or subsidies. The common commercial policy shall be conducted in the context of the principles and objectives of the Union's external action.[6]

The addition of "foreign direct investment" in the list of matters covered by commercial policy raises the problem of how we define this new concept. Although it is apparent from the wording of Articles 206 and 207 of the TFEU that the new competence is limited only to foreign direct investment, the Lisbon Treaty does not provide a definition of this term, thus creating uncertainty with regard to the scope of the new powers of the EU.

FDI is a purely economic concept. According to the International Monetary Fund's *Balance of Payment Manual*, direct investment is the category of international investment that reflects the objective of a resident entity (the direct investor) in one economy obtaining a lasting interest in a (direct investment) enterprise resident in another economy. The lasting interest implies the existence of a long-term relationship between the direct investor and the enterprise, and a significant degree of influence by the investor on the management of the enterprise.[7] According to the Manual, there is a direct investment relationship when a direct investor owns 10% or more of the shares or the voting rights of a company.[8] Consequently, FDI involves a long-term relationship between the investor and the enterprise. The investor must also exercise a significant influence over the management of the enterprise.The creation of subsidiaries and branches in the host State could be quoted as an illustration of this kind

of investment.[9] FDI should be distinguished from foreign portfolio investment (FPI) or foreign financial investment (FFI). FPI or FFI represents passive holdings of securities such as foreign stocks, bonds, or other financial assets, none of which entails active management or control of the enterprise. Therefore, unlike financial investment, direct investment implies a long-term relationship between the investor and the host country, allowing the investor to control the enterprise as opposed to a financial investor who does not seek to influence the management of the investment. As it is very easy to sell off the securities and pull out of the foreign portfolio investment, FPI has the potential to be much more volatile than FDI.[10]

In the context of European Law, the term "direct investment" appeared in both the Chapter on capital movements and payments of the EC Treaty and the capital directive.[11] The definition of the Court of Justice is largely based on definitions provided by the IMF and the OECD.[12] Foreign Direct Investment (FDI) is generally considered to include any foreign investment that serves to establish lasting and direct links with an undertaking to which capital is made available, in order to carry out some form of economic activity. When investments take the form of a shareholding, this objective presupposes that the shares enable the shareholder to participate effectively in the management or control of that company.[13] However, the Court of Justice of the European Union has described the notion of "portfolio investment" as "the acquisition of shares on the capital market solely with the intention of making a financial investment without any intention to influence the management and control of the undertaking".[14]

Whatever the definition of FDI, we can assert that the new EU competence is limited to FDI and does not cover portfolio investment, and that BITs traditionally cover both types of investment. This interpretation implies that the Union is exclusively competent concerning those aspects that relate to foreign direct investment, and that Member States remain competent concerning portfolio investments. The consequence of this assertion is that all investment agreements with both foreign direct and portfolio investmentneed to be concluded as mixed agreements. For any international treaty covering portfolio investment, therefore, the association of Member States is required in both the negotiation and the conclusion stages.

In its decision on the constitutionality of the Lisbon Treaty, the German Constitutional Court emphasised the limits of the new investment competence of the EU. It observed that,

> [t]he extension of the common commercial policy to "foreign direct investment" (Article 207.1 TFEU) confers exclusive competence on the European Union also in this area. Much, however, argues in favour of assuming that the term "foreign direct investment" only encompasses investment which serves to obtain a controlling interest in an enterprise. [...] The consequence of this would be that exclusive competence only exists for investment of this type whereas investment protection agreements that go beyond this would have to be concluded as mixed agreements.[15]

However, the European Commission did not share this interpretation. The Commission takes the view that the Union has exclusive competence to conclude agreements covering all matters relating to foreign investment, i.e. both foreign direct investment and portfolio investment. The Commission argues that the Union should have an implied external competence relating to portfolio investments based on the provisions of the free movement of capital (Articles 63-66 TFEU). Article 63 TFEU provides that the movement of capital between Member States of the Union and third countries is to be free of restrictions.[16] The Commission's position on this was disapproved by some scholars. It was noted, for example, that the Commission's argument ignores the express intention of the drafters of the Lisbon Treaty to limit the EU's competence to foreign direct investment. Furthermore, the argument cannot explain why the inclusion of foreign direct investment in Article 207 TFEU was necessary in the first place, because an implied external competence based on the free movement of capital would also cover foreign direct investment.[17]

There is another debate related to the limit of the EU's new competence regarding FDI. It could be argued that the EU's investment powers would be limited to aspects concerning access/admission of investments and would not extend to post-admission and protection. The investment process essentially has two successive phases: the phase of "pre-investment", admission or establishment when the investor seeks entry into the territory of the host State, and the "post-investment" phase, when the investment has been "made". Typically, post-investment is tightly protected by "hard-law" obligations, including compensation in the event of expropriation. This limiting interpretation could find support in Article 206 TFEU, which speaks of the "progressive abolition of restrictions on international trade and on foreign direct investment", suggesting that the CCP is primarily concerned with access/admission aspects.[18] It should also benoted that the wording of Article 207 TFEU does not refer to investment

protection, and it is possible to argue that it only covers issues of investment liberalisation. Finally, we might assert that the expropriation rule - a significant feature of the protection of foreign investment - is not covered by the new competence. This is due to the principle of neutrality vis-à-vis the Member States' systems of property ownership (Article 345 TFEU, ex Article 295 TEC) that excludes EU competence regarding expropriation.[19]

The Commission rejects a narrow reading of the EU's investment powers. It takes the view that the Union's competence covers all the standards provided for in an investment protection agreement, including expropriation. The Commission points out that the European Court of Justice has consistently held that the Union's competence for the common commercial policy is not limited to border measures and issues of market access but also covers post entry matters (i.e. after goods have been imported or a service supplier has been established). Following this logic, according to the Commission, the Union's competence for foreign direct investment and capital movements must also cover the standards that apply post-establishment, including protection against expropriation without compensation.[20]

The extension of competence was accompanied by a strengthening of the role of the European Parliament in the implementation of this new competence.[21]Articles 207 and 218 of the Treaty on the Functioning of the European Union lay down the applicable procedure with regards to FDI matters to be negotiated and concluded under the new Common Commercial Policy.

Before the Lisbon Treaty, the European Parliament had very limited powers. The Council and Commission were the main actors in the field of negotiating and concluding international trade agreements. However, according to the Lisbon Treaty, the Commission should make recommendations to the Council where agreements with one or more third countries need to be negotiated, who should thenauthorise it to open the necessary negotiations. The council may issue a directive relating to the negotiation. The Commission shall conduct these negotiations in consultation with a special committee appointed by the Council to assist the Commission in this task, and within the framework for such directives issued by the Council. The Commission shall report regularly to the special committee and to the European Parliament on the progress of such negotiations.

Consequently, the Lisbon Treaty strengthens the role of the European Parliament as an important player in the field of Foreign Direct Investment. Article 207(3) TFEU requires that the Commission reports to the Parliament during international trade agreement negotiations. This is a new reference

to the European Parliament and one that imposes a legal obligation on the Commission to inform the Parliament at the stage of negotiations. Prior to the Lisbon Treaty, the European Parliament had very little say on the aims of EU negotiations: all it could do was to adopt its own initiative reports.

Furthermore, international agreements on FDI negotiated between the Commission and third countries will also be subject to the approval of the European Parliament.[22] The consent of Parliament is now necessary for the conclusion of international agreements, which is the basic means of action in the field of Common Commercial Policy. This new power can lead to some surprises. Indeed, some Members of the European Parliament are fiercely hostile to investment treaties. History has shown that when the European Parliament has full power, it does not hesitate use it. On 12 February 2010, for example, it blocked the SWIFT interim agreement between the EU and the US.[23] It is certain that the involvement of the EP will add another face to the new FDI agreements concluded by the EU. It is still unclear how the EP will exercise its new powers to influence the European policy on FDI.

II. The impact of the new competence on the BITs concluded by members states

All EU member countries (except Ireland) have concluded BITs with third countries. With a total of almost 1,350 agreements, Member States have concluded almost half of all the investment agreements currently in force around the world. Through BITs, Member States have obtained guarantees on the treatment of their investors by the third countries involved, such as commitments against unfair or discriminatory treatment or guarantees of prompt, adequate and effective compensation in cases of expropriation. The TFEU does not contain any explicit transitional provisions for such agreements, which have now come under the Union's exclusive competence. What, we might ask, is the legal status of the existing BITs concluded by the Member States with third countries?

On December 12, 2012, the European Union issued Regulation (EU) No. 1219/2012 establishing transitional arrangements for bilateral investment treaties (BITs) between Member States and third countries.[24] The Regulation, which entered into force on January 9, 2013, determined the status of BITs entered into by EU Member States and non - EU post - Lisbon Treaty The aim of this Regulation is to maintain, under some conditions, bilateral investment agreements with third countries. By doing so, it provides legal certainty to both EU and foreign investors operating under the terms of these agreements.

The Regulation confirms that a BIT signed before December 1 2009 (the date of the commencement of the Lisbon treaty), or before a Member State's accession to the EU, may, subject to review by the European Commission, remain in force until replaced by an investment agreement between the European Union and the third State in question. The Regulation requires Member States to notify the Commission of BITs that they wish to maintain in force by February 8, 2013 or within 30 days of their accessionto the EU.[25] If, upon its review, the Commission considers that an existing BIT constitutes a serious obstacle to the negotiation or conclusion by the EU of a replacement BIT, the Commission will enter into consultations with the Member State concerned with a view to identifying the appropriate actions to resolve the matter.[26] The Commission will publish a list of the BITs notified to it pursuant to the Regulation, and an updated list of such BITs every 12 months thereon.[27] A list of 1350 bilateral investment agreements, referred to in Article 4(1) of Regulation, was published on 8 May 2013.[28]

However, the Regulation also establishes a framework according to which States may negotiate or enter into new BITs with third countries despite the exclusive competence that the EU has on FDI. In this regard it should be noted that EU law permits the Union to authorise the Member States to act in fields of its own exclusive powers. According to Article 2(1) TFEU, "[w]hen the Treaties confer on the Union exclusive competence in a specific area, only the Union may legislate and adopt legally binding acts, the Member States being able to do so themselves only if so empowered by the Union or for the implementation of Union acts".[29] Conclusion of new BITs with third countries is subject to authorisation by the Commission.[30] Member States intending to negotiate such BITs must notify the Commission and provide details of the provisions to be negotiated at least five months in advance.[31] The Commission will grant such authorisation if the negotiations are consistent with EU law and policies and are not superfluous, i.e.when the Commission has not already initiated negotiations[32] In accordance with its findings, the Commission may require a Member State to include or remove provisions from the draft BIT to ensure compatibility with EU law or investment policy. Once authorised by the Commission, the Member State may open negotiations for the new BIT; however, the Commission must be kept informed of their progress and may request to participate in the discussions.[33]

Finally, the regulation creates a regime for BITs signed between a Member State and a third party between December 1, 2009 (the date of entry into force of the Lisbon treaty) and January 9 2013 (the date of entry into force of the regulation). These BITs may be maintained or entered into force subject to certain conditions. Member State must notify the Commission of any such BITs that it wishes to maintain in force or permit to enter into force by February 8, 2013. The

Commission will authorise the maintenance in force or entry into force unless it determines that their provisions conflict with EU law or policies, or that it would constitute a serious obstacle to EU negotiations of an investment agreement with the same third country.[34]

The procedure of assessments and authorisation after notification could be considered as a cumbersome procedure. Some states do not favour this notification system. They proposed an alternative system in which the BITs with third countries remain in force until an investment agreement has been concluded by the Union. It should be noted that the draft regulation proposed by the Commission provides for stringent Commission screening powers, particularly with regards to existing BITs. Followingthe objections of some states, the adopted regulation regarding existing BITs,concluded before Lisbon Treaty, the authorisation system was dropped and the alternative system was implemented.[35]

The regulation creates some duties relating to dispute settlement mechanisms under the BITs that fall within the scope of its provisions. First, member States must inform the Commission of any request for a BIT dispute resolution, including requests for arbitration. Second, they must seek the agreement of the Commission before they activate any dispute settlement mechanisms against a third country under a BIT, and must activate such mechanisms only when requested by the Commission. Third, when a dispute resolution procedure has been activated, either by or against a Member State, the Member State and the Commission must cooperate in the conduct of the proceedings, which may include the participation of the Commission in the process.[36]

The regulations did not answer all the questions. Inconsistencies between EU law and BITs may create additional uncertainty for an investor. For example, if a Member State fails to comply with the Regulation's notification authorisation requirements, the question will arise as to whether this has had any effect under public international law on the relevant BIT. Furthermore, the Regulation does not address the status of investment agreements between EU Member States (intra-EU BITs). The statue and the future of intra-BITs have sparked much debate amongst the European Commission, Member States, arbitral tribunal and investors.At the core of this discussion are the validity of these agreements and the possibility of a European investor usingthe investor-arbitration that they offered.[37]

III. The content of the new FDI European policy

The EU will be a major player in investment matters. The Commission will negotiate a new investment agreement. It is interesting to know both *how* the Commission negotiates such agreements and *what* the content of the EU policy on foreign direct investment is. The immediate aftermath of the entry-into-force of the Lisbon Treaty was dominated by the debate between the EU Commission and the EU Member States regarding the distribution of their respective competences.[38] The regulation of 2012 does not provide much insight into the substance of a future EU investment policy.

On 7 July 2010, the European Commission outlined its approach for the EU's future investment policy in its Communication "[t]owards a comprehensive European international investment policy".[39] The Communication explains how the EU could develop its treaties in this field. This Communication is amongst the first steps in the development of a European international investment policy, which will be gradual and targeted and will take into account the responses of the otherplayers.[40] If we want to see the new face of EU agreements on investment, we should wait until such an agreement is concluded.[41]

According to the Commission, the EU policy will seek to join the admission and protection of investments. This approach seeks to integrate investment liberalisation and investment protection.[42] It should be noted that in contrast to BITs concluded by USA, Japan and Canada, BITs concluded by European States provide mainly for the treatment of investors "post-entry" or "post-admission" only. By suggesting this approach, the new European investment agreements will improve the conditions of market access for all EU investors.

With regard to the protection, the Commission pointed out that the Union should deliver better results than the results that have been or could have been obtained by Member States individually. Thus, the Union's future action in this field should be inspired and guided by the best available standards, so as to offer a level playing field of a high quality to all EU investors. Future agreements concluded by the European Union should provide for the traditional substantial right offered to foreign investors. They will prohibit discrimination, provide for fair and equitable treatment, allow free transfer of funds and prohibit expropriation. Specifically on expropriation, the Communication provides that "a clear formulation of the balance between the different interests at stake, such as the protection of investors against unlawful expropriation or the right of each Party to regulate in the public interest, needs to be ensured".[43]

As for the procedural rights, future EU agreements should include an investor-state dispute settlement, which permits an investor to take a claim against a government directly to binding international arbitration.[44] According to the Commission, the Union should build on Member State practices to arrive at state-of-the art investor state dispute settlement mechanisms. The process must be conducted in a transparent manner (including requests for arbitration, submissions, open hearings, amicus curiae briefs and the publication of awards). It must ensure consistency and predictability by creating quasi-permanent arbitrators (as in the EU's FTA practice) and/or appellate mechanisms. It must ensure ethical values by providing Rules for the conduct of arbitration.

The new provision on arbitration with a foreign investor will raise new challenges for the European Union. Current arbitration systems are to some extent ill adapted to the advent of the Union. To take one example, the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the ICSID Convention) is only open to signature and ratification by states, and the European Union couldn't sign the Washington Convention. Historically, the Union has not been a significant actor in this field. The Commission and other European institutions have no expertise on the administration and management of disputes with foreign parties before arbitral tribunal. According to the communication, the Commission will explore with interested parties the possibility of amending the Washington Convention by allowing the European Union to accede to the ICSID Convention.

Given the exclusive external competence, the Commission takes the view that the European Union will defend all actions of EU institutions and will be the sole defendant of dispute settlement mechanisms regarding any measure taken by a Member State which affects investments by third country nationals or companies falling within the scope of the agreement concerned.[45] In developing its new international investment policy, the Commission observed that it would address this issue, and particularly financial compensation relying on available instruments, and possibly includenew legislation. On 21 June 2013, the Commission adopted a Proposal for establishing a framework for managing financial responsibility linked to investor-state dispute settlement tribunals.[46] In this proposition, the Commission did admit, however, that in some situations a Member State would act as a defendant.[47]

Finally, to respond to criticism from some members of the European Parliament, the Communication provides that future investment treaties must take into consideration the protection of state interests. Investment agreements should be consistent with the other policies of the Union and its Member States,

including policies on the protection of the environment, decent work, health and safety at work, consumer protection, cultural diversity, development policy and competition policy. Investment policy will continue to allow the Union, and the Member States to adopt and enforce measures necessary to pursue public policy objectives. A common investment policy should also be guided by the principles and objectives of the Union's external action more generally, including the promotion of the rule of law, human rights and sustainable development (Article 205 TFEU and Article 21 TEU). The communication also refers to the possibility of including obligations for investors. It considers the OECD Guidelines for Multinational Enterprises to be an important tool to help balance the rights and responsibilities of investors.

IV. Conclusion

Negotiations on investment at EU level are currently on-going with Canada (the Comprehensive Economic and Trade Agreement (CETA),[48] Singapore, India, Japan, Malaysia, MERCOSUR, Morocco, Thailand and Vietnam within the context of the negotiations for Free Trade Agreements. In December 2011 the Council also adopted negotiating directives for deep and comprehensive Free Trade Agreements including investment for Egypt, Jordan and Tunisia.[49] On 23 May 2013, the European Commission asked the Member States to authorise the opening of negotiations with China in the area of investment protection.[50] On 14 June 2013, Member States gave the European Commission the green light to start trade and investment talks with the United States. The Transatlantic Trade and Investment Partnership will potentially representthe largest regional free trade and investment agreement in history.[51] The end of this negotiation process will provide us with a clear indication on how the future European agreements on investment are to be fashioned.

1. The Charter is available at: http://www.encharter.org/.

2. It is important to note that the inclusion of FDI in the scope of commercial policy corresponds largely to the proposals that were already discussed during the drafting of a Constitution Treaty. The travauxpreparatoires of the constitution showed that this inclusion received some rejections by France, England and Germany, *see Proposition d'amendement à l'article III-212 Déposée par M.de Villepin*, available at http://europeanconvention.eu.int/docs/treaty/pdf/866/Art%20III%20212%20de%20Villepin%20FR.pdf; *Suggestion for amendment of Article 24 by Mr. J. Fischer*, CONV 685/03, available at http://europeanconvention.eu.int/Docs/Treaty/pdf/866/Art24Fischer.pdf; *Suggestion for amendment of Article 24 by Mr D. Heathcoat-Amory*, available at http://european convention.eu.int/Docs/Treaty/pdf/866/Art24Heathcoat- Amory%20EN.pdf.

3. A. Dimopoulos, 'The Common Commercial Policy After Lisbon: Establishing Parallelism Between Internal and External Economic Relations,' *Croatian Yearbook of European Law and Policy*, 4 (2008),109

4. M. Burgstaller, 'European Law and Investment Treaties,' *Journal of International Arbitration*, 26 (2009), p.181, p.214; P.J. Kupjer, 'Foreign Direct Investment: The First Test of the Lisbon Improvements in the Domain of Trade Polity,' *Legal Issues of Economic Integration*, 37 (2010), p.261, p.272.

5. This article replaces Article 131 of the Nice Treaty, which states: "[b]y establishing a customs union between themselves Member States aim to contribute, in the common interest, to the harmonious development of world trade, the progressive abolition of restrictions on international trade and the lowering of customs barriers. The common commercial policy shall take into account the favourable effect which the abolition of customs duties between Member States may have on the increase in the competitive strength of undertakings in those States".

6. Article 133 (1) of the Nice Treaty did not list FDI. According to this article, "1. The common commercial policy shall be based on uniform principles, particularly in regard to changes in tariff rates, the conclusion of tariff and trade agreements, the achievement of uniformity in measures of liberalisation, export policy and measures to protect trade such as those to be taken in the event of dumping or subsidies".

7. IMF, *Balance of Payment Manual*, available at: http://www.imf.org/external/pubs/ft/bopman/bopman.pdf p.359.

8. Ibid, p.362.

9. See also, *OECD Benchmark Definition of Foreign Direct Investment*, 4[th]edn, 2008, p.11. "Direct investment is a category of cross-border investment made by a resident in one economy (the direct investor) with the objective of establishing a lasting interest in an enterprise (the direct investment enterprise) that is resident in an economy other than that of the direct investor. The motivation of the direct investor is a strategic long-term relationship with the direct investment enterprise to ensure a significant degree of influence by the direct investor in the management of the direct investment enterprise. The 'lasting interest' is evidenced when the direct investor owns at least 10% of the voting power of the direct investment enterprise. Direct investment may also allow the direct investor to gain access to the economy of the direct investment enterprise which it might otherwise be unable to do. The objectives of direct investment are different from those of portfolio investment whereby investors do not generally expect to influence the management of the enterprise".

10. For the distinction between the two types of investment, see Note by the UNCTAD secretariat: 'Foreign Portfolio investment (FPI) and Foreign Direct 1 Investment (FDI): Characteristics, similarities, complementarities and differences, policy implications and development impact,' TD/B/COM.2/EM.6/2, 15 April 1999.

11. Council Directive [EEC] 88/361 of 24 June 1988 for the implementation of Article 67 of the Treaty, (1988) OJ L 178/5. According to annex 1 of this directive, "[i]nvestments of all kinds by natural persons or commercial, industrial or financial undertakings, and which serve to establish or to maintain lasting and direct links between the person providing the capital and the entrepreneur to whom or the undertaking to which the capital is made available in order to carry on an economic activity".

12. See, for example, Judgment of 12 December 2006, *Test Claimants in the FII Group Litigation*, Case C-446/04, ECR p. I-11753, para. 181. See also the Judgments of 24 May 2007, *Holböck*, C-157/05, ECR. p. I-4051, para. 34; 23 October 2007, *Commission/Germany*, C-112/05, ECR p. I-8995, para. 18; 18 December 2007,

Skatterverket v A, C-101/05, para. 46; 20 May 2008, Orange European Smallcap Fund, C-194/06, para. 100; 14 February 2008, *Commission/Spain*, C-274/06, para. 18; and 26 March 2009, *Commission/Italy*, C-326/07, para. 35.

13. Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions, *Towards a Comprehensive European International Investment Policy* Brussels, 7.7.2010 COM(2010)343 Final, http://trade.ec.europa.eu/doclib/docs/2011/may/tradoc_147884.pdf, p.3.
14. See Judgment of 26 September 2008, *Commission/Netherlands*, Joined Cases C-282/4 and C-283/04, ECR p.I-9141, para. 19.
15. p. 379, German Constitutional Court, Decision on the Constitutionality of Lisbon treaty, 30 June 2009, http://www.bundesverfassungsgericht.de/entscheidungen/es20090630_2bve000208en.html.
16. European Commission, *Proposal for a Regulation of the European Parliament and the Council establishing a framework for managing financial responsibility linked to investor-state dispute settlement tribunals established by international agreements to which the European Union is Party*, Brussels, 21.6.2012 COM(2012) 335 final 2012/0163 (COD) http://eur lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2012:0335:FIN:EN:PDF, p. 3. The Commission also observed that Article 3(2) TFEU provides for the exclusive competence of the Union whenever rules included in an international agreement "may affect common rules or alter their scope". In the Commission's view, the Union must have exclusive competence also over matters concerning portfolio investment since the rules being envisaged, which would apply indistinctly to portfolio investment, may affect the common rules on capital movement set down in Article 63 of the Treaty.
17. M. Krajewski, 'The Reform of the Common Commercial Policy,' in A. Biondi and P Eeckhout (eds), *European Union Law after the Treaty of Lisbon*, p. 16.
18. A. Reinisch, 'The EU on the Investment Path – Quo Vadis Europe? The Future of EU BITs and other Investment Agreements,' available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2236192, p. 4.
19. "The Treaties shall in no way prejudice the rules in Member States governing the system of property Ownership".
20. Proposal for a Regulation of the European Parliament and the Council Establishing a Framework for Managing Financial Responsibility, p.4.
21. N. Lavranos, 'Bilateral Investment Treaties (BITs) and EU Law,' ESIL Conference 2010, available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1683348, p. 19.
22. For the role of the European Parliament, see K. Kazimirek, 'The New EU Competence over Foreign Direct Investment and its Impact on the EU's Role as a Global Player,' Jean Monnet Centre for Europeanisation and Transnational Regulations Oldenburg Fakultät, http://www.cetro.uni-oldenburg.de/download/CETRO_Selected_Theses-_Kazimirek.pdf, p. 40.
23. Indeed, Carl Schlyter (ZWE, Green Party), who is responsible for EU investment policy, has already made some strong statements regarding this. He has suggested that BITs are «neo-colonial» and enable developed Member States to «exploit» developing countries. He called for more balanced future EU BITs. See N. Lavranos, p. 20.
24. http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:351:0040:0046:En:PDF.
25. Art. 1.
26. Art. 1.
27. Art. 2.
28. http://www.italaw.com/sites/default/files/archive/List%20of%20EU%20BITs.pdf.
29. For the pre-Lisbon situation, see Case 41/76 Donckerwolke[1976] ECR 1921.
30. Art. 7.

31. Art. 8.
32. Art. 9.
33. Art. 9.
34. Art. 12.
35. See. A. Reinisch, p. 7.
36. Art 13.
37. See on this debate, Le DroitEuropeĺen et L'Investissement, eds, C. Kessedjian and Ch. Leben, Paris, 2009.
38. Reinisch, p.5.
39. Brussels, 7.7.2010 COM(2010)343 final, available at: http://trade.ec.europa.eu/doclib/docs/2011/may/tradoc_147884.pdf.
40. Ibid, p.1.
41. The communication of July 2010 received comments from the other EU institutions, the most important of which were the Council Conclusions of 25 October 2010 (http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/EN/foraff/117328.pdf), and the European Parliament resolution of 6 April 2011 (http://www.europarl.europa.eu/sides/getDoc.do?type=TA&reference=P7-TA-2011-0141&language=EN), adopting a report of its International Trade Committee of 22 March 2011 (http://www.europarl.europa.eu/sides/getDoc.do?type=REPORT&reference=A7-2011-0070&language=EN). On 5 July 2011, the Commission adopted a follow up to this resolution (www.europarl.europa.eu/oeil/spdoc.do?i...j=0...). The Economic and Social Committee submitted its opinion on 13 July 2011 (http://eur-lex.europa.eu/JOHtml.do?uri=OJ:C:2011:318:SOM:en:HTML).
42. Ibid, p. 5.
43. Ibid, p.9.
44. Ibid, p.9.
45. Ibid, p. 10.
46. Proposed Regulation (COM(2012)0335 – C7-0155/2012 – 2012/0163(COD)).
47. This proposal distinguishes three different situations, regarding the distribution of roles between the Union and the Member States in relation to the conduct of disputes under agreements to which the Union is a party. In the first situation, the Union would act as a respondent where the treatment alleged to be inconsistent with the agreement is afforded by one or several Union institutions. The Union would accept full financial responsibility in such cases. In the second, situation the Member State would act as a respondent where the treatment in question is afforded by the Member State. The Member State would accept full financial responsibility is such cases. In this situation, the Member State would need to keep the Commission informed of developments in the case, and permit the Commission to give direction on particular issues. In the third situation, the Union would act as a respondent in terms of treatment afforded by a Member State. This would occur where the Member State has opted not to act as a respondent. It would also occur where the Commission decides that issues of Union law are involved such that the Union may be financially responsible, in whole or in part. It would also apply where the Commission takes the view that a Union position is required in order to ensure unity of external representation, because it is likely that similar claims may be raised in disputes against other Member States or because the disputes raises unsettled issues of law that are likely to recur in other disputes.
48. http://ec.europa.eu/trade/policy/countries-and-regions/countries/canada/.
49. http://europa.eu/rapid/press-release_IP-13-458_en.htm.
50. http://europa.eu/rapid/press-release_IP-13-458_en.htm.
51. http://ec.europa.eu/trade/policy/countries-and-regions/countries/united-states/ and http://www.ustr.gov/about-us/press-office/fact-sheets/2013/february/US-EU-TTIP. See also on the evolution of the negotiations, Transatlantic Trade and Investment Partnership (TTIP), http://ec.europa.eu/trade/policy/in-focus/ttip/.

Chapter Two

EU Investor Protection in the Post-crisis Era

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Introduction

The financial turmoil that has shaken global financial markets since 2007 has highlighted various fundamental dysfunctions in the regulatory environment of banks and financial markets. Regulation and supervision have clearly failed both to maintain a solid and stable financial system and to minimise the likelihood of financial institutions failing. The accumulation of risks on and off banks' balance sheets, amplified by disproportionate leverage, enables banks to inflate return on equity, indicating that the existing prudential rules have not managed properly to measure and contain risks within the banking sector. It is therefore unsurprising that the global regulatory response to the financial crisis has been mainly to change its focus on bank regulation, including: strengthening capital requirements, subjecting systemically important banks to stricter rules, improving macro-prudential regulation, enhancing co-operation between prudential supervisors, limiting the exposure of banks to high-risk activities (notably in the field of proprietary activities, e.g. Volcker rule), elaborating robust regulatory toolkits for the recovery and resolution of distressed financial institutions, and upgrading the deposit guarantee systems.

However, part of the fall-out of the financial crisis was the exposure by various market participants, both wholesale and retail, to highly complex financial products designed and distributed by financial institutions, which suffered total or substantial write-offs due to their toxic character. Many retail investors, who were generally unfamiliar with financial market products, acquired structured investment products that were supposed to offer a relatively high return combined with mechanisms to contain losses on the invested capital through capital protection. Financial institutions often marketed these structured products as lowrisk investments providing more profitable substitutes for traditional low risk debts. In reality, these structured products expose retail clients to the fluctuations of capital markets, while the capital protection mechanisms entail a counterparty risk for the protection sellers. Similarly, investors who were supposed to be more literate, such as large enterprises or (local) public authorities, acquired complex financial products, such as CDOs, as

part of their treasury management. The top rating attributed to these products by rating agencies overshadowed the risk awareness by the investors, and helped financial institutions offering these products to market them as low risk, high return investments.
For many financial institutions, the 'originate to distribute' business model proved more profitable than the traditional intermediation activity. Instead of holding assets on their balance sheet, banks would transfer the risks to other market participants by setting up securitisation structures and providing various services (servicing of loans, credit enhancement for the special purpose vehicles etc.) to the special purpose vehicles that repackaged the transferred loans and funded them with debt securities issued publicly or through private placements in the market. The 'originate to distribute' model did, however, stimulate excessive lending without proper risk assessment by banks, which could then immediately transfer the risks to other market players. This moral hazard problem laid the foundations for the massive subprime lending in the US, which triggered the financial crisis.

The developments that propagated the financial 'meltdown' were in part induced, or at lest made possible, by the regulatory framework, notably the regulatory capital requirements. In view of the cost of capital for banks, the latter were incentivised to explore and exploit regulatory loopholes or look for possibilities of regulatory arbitrage.On the one hand, capital requirements were mainly geared towards risks on the banks' balance sheets, while building off-balance sheet positions offered more possibilities for banks to increase their profits under less strict regulatory requirements. The development of the securitisation business in the years preceding the financial crisis can be largely ascribed to the search for maximising the regulatory efficiency of capital requirements: securitisation removed loans and other traditional bank assets from the balance sheet, while banks would take other, contingent liabilities under the form of guarantees or other commitments as part of credit enhancement mechanisms designed to cover possible losses on the securities issued in the market to fund the securitised assets. In the end, although some banks were nevertheless exposed to similar risks that they faced prior to the securitisation, they no longer suffered the same regulatory costs under the form of capital requirements. More importantly, the opaqueness of the risks underlying the debt securities issued to fund the securitised assets (or 'tranches') exposed many investors to risks that they were unaware of and often unprepared to take.
Part of the regulatory agenda in the aftermath of the financial crisis has been concerned with re-calibrating the regulatory toolkit on investor protection. In this chapter, we want to highlight the main developments in this regard in the European Union, with a view to uncovering the concepts underlying the

regulatory developments. In particular, we want to examine to what extent EU investor protection regulation, which prior to the crisis relied heavily on the so-called 'information paradigm', has been substituted by more intrusive forms of investor protection rules, assigning more weight to supervisory intervention in the design and distribution of financial products. After a sketch of the concepts of EU investor protection regulation prior to the crisis (Section 1), we describe the ongoing developments regarding investor protection regulation in response to the crisis (Section 2). We focus our analysis on developments in the EU and some of its Member States.

Section I. Pre-crisis approach to investor protection: the 'information paradigm'

The gradual EU harmonisation of investor protection rules, which aimed at creating a common set of rules across Member States, thus enabling them to realise an internal market,was built upon the 'information paradigm'. Investor protection is supplied by obliging relevant market participants to provide prospective investors with the information that the latter need to make a well-informed investment decision. Investing in a company naturally entails risk:an investor will only be prepared to take such a risk if he possesses sufficient information to assess it, and to value the reward offered to him by the issuer of the investment instrument as compensation for taking that risk. By nature, issuers of financial instruments possess more information regarding the value and prospects of their company ('information asymmetry'), and are therefore in a position to supply the information needed by prospective investors.[1] The information paradigm is closely connected with the 'efficient capital market hypothesis' (ECMH) that has dominated market regulation in recent decades. According to this hypothesis, financial markets function efficiently in the sense that investors use all the information that is available in the market, who by nature act rationally, and reflect the price of the financial instruments. In line with the ECMH, the main task of the regulator in supplying optimal investor protection is to make sure that the relevant information needed by rational investors is made available in the markets by way of disclosure obligations incumbent on issuers of financial instruments. As investors are deemed to act rationally, regulation should not put any *ex ante* limits on the supply of investment products. All investors (including retail investors) are able to make a rational judgment on the suitability and the price of any investment opportunity, provided that the information available is comprehensive. Consequently, to the extent that the market itself does not manage to guarantee the quality and comprehensiveness of the information supplied to investors, regulation should avoid possible market failures in this regard.

The information paradigm and the assumption that investors act rationally underpin EU investor protection regulation, both at the level of the design and issue of financial products, and at the level of their distribution.

1. Public offer of securities and the information paradigm

At the level of product design, the 2003 Prospectus Directive[2] did not impose any *ex ante* limitation on the offer of investment products to (retail) investors: as a rule, any issuer (whether a public authority or private entity; a legal or a natural person) has the opportunity to make a public offer of securities, under the sole condition of prior approval and by the competent authority of the home member state[3] of the issuer, of a prospectus containing all information needed by the targeted investors to make a well-informed decision. Although the structure of the prospectus and its substance have been laid down in detail in an EU regulation,[4] the general legal standard for a prospectus is still formulated through a functional criterion: the prospectus must enable prospective investors to assess the risks of the investment properly. The role of the supervisor is limited to scrutinising the draft prospectus in order to ascertain that this criterion is met. Hence, once the prospectus contains the required information, the competent authority is under a legal obligation to approve it, without any further possibility of requiring the issuer to limit the offer to more experienced investors. Under the 'information paradigm', each investor should be able, based on the information contained in the prospectus, to assess properly whether or not the proposed investment is suitable.

Contrary to the former EU rules on prospectuses, the 2003 Prospectus Directive does implicitly deter prospective investors from reading the prospectuses prior to making an investment decision: the broad scope and level of detail of information to be included in a prospectus has a direct bearing on the volume and technical wording of a prospectus, which is clearly at odds with the retail investor's capacity to understand and absorb all the information deemed necessary to make a proper investment decision. Therefore, the 2003 Prospectus Directive made it obligatory that the full prospectus be accompanied by a summary prospectus, containing the main elements regarding the issuer and the securities issue, and phrased in a non-technical manner. Ideally, the information contained in the full prospectus would be read and interpreted by specialist market actors, and subsequently translated into analysts' reports, recommendations or information provided by financial institutions in the distribution chain of the issued securities. The summary prospectus,an abridged, more digestible version of the full prospectus, would act as a complement to the full prospectus, adapted to make the information more easily accessible to retail investors.

The dual prospectus regime introduced by the Prospectus Directive still assumes that the investor's decision on whether or not to acquire the securities on offer is based on all the information supplied by the issuer, and that at least part of the relevant information is "absorbed" by other market players, including the financial institutions involved in the distribution of the securities. Although part of the relevant information is thus supplied in an indirect manner, the approach is still consistent with the efficient capital market hypothesis.

The prospectus liability regime contained in the Prospectus Directive nevertheless further consolidates the information paradigm in its pure form: although the directive does not contain a proper liability regime, but merely obliges Member States to put a civil liability regime in place for incomplete or misleading information,[5] the Prospectus Directive made it clear that the liability will as a rule be measured against the information contained in the full prospectus. Liability will have to be borne by thepersons mentioned in the prospectus taking responsibility for it. In order to trigger liability, the wronged investor should not, however, demonstrate that he hasrelied upon the prospectus: consistent with the efficient capital market hypothesis, the (supposedly misleading or incomplete) information is deemed to be in the market and it will be assumed that every rational investor has used it. However, the directive also specifies that liability cannot be based solely on the summary prospectus, unless it is misleading in conjunction with the full prospectus or contradicts it. Consequently, there may be a lack of consistency between the disclosure regime and the liability regime: civil liability of the issuer is based solely on the (lack of) information in the full prospectus, which is often too complex and voluminous for the retail investor to understand and absorb, while the investor is dependent on the financial intermediaries to properly absorb and interpret the information contained in the full prospectus and pass it on to the final investors.

2. Investment product distribution and the information paradigm

A similar pattern emerges from the obligations incumbent on financial institutions to act as a distributor of financial instruments, particularly in relation to retail clients. Under the conduct of business rules contained in the Markets in Financial Instruments Directive (MiFID),[6] investment firms should first inform their clients on the services they offer, in order to enable the latter to make a well-informed investment decision.[7] This includes providing general information on the risks associated with different kinds of financial instruments offered through the intermediary of the investment firm. Furthermore, for the client not using the (brokerage) services in 'execution only'mode[8] the 'know

your customer' obligation of the financial intermediary essentially entails requesting from the client his knowledge of financial instruments and his experience with investments. This information should enable the investment firm to assess the client's capacity to understand the (risks associated with the) financial instruments proposed or advised to him. As, except in the case of asset management, the final investment decision is with the client, the conduct of business rules is therefore consistent with the information paradigm, as regulatory obligations are geared towards the supply of information needed for the client to make a well-informed decision. However, the obligation to offer suitable advice (when the investment firm advises the client) or to propose only appropriate financial instruments (in the case of non-advisory services) does impose an *ex ante* limit on the kind of investment products that the investment firm may advise or propose to the client, as the products should fit into the risk profile of the client (suitability) or be consistent with the client's knowledge and experience regarding investments (appropriateness). No such limit is imposed for execution only-services, which, by definition, apply only to non-complex financial instruments. For these latter products, the unsophisticated retail investor should be able to make a proper risk assessment, based on publicly disclosed information.

II. Post-crisis regulatory reforms regarding investor protection

The regulatory response to the financial crisis generally points towards stronger investor protection, and particularly in the form of more intrusive regulation that empowers supervisory authorities to impose more *ex ante* limits on the offer of financial products to retail investors. In this section, we look more closely at the underlying concepts of these regulatory reforms: is regulation still based on the information paradigm, which focuses on the rational investor, or does it depart from the assumption that the disclosure of information is a necessary and sufficient tool for adequate investor protection?

1. Information disclosure in the primary markets: Key Investor Information

With regard to the (public) issue of securities, the fundamentals of the existing permissive regime contained in the Prospectus Directive have not undergone major modifications. However, the trend to target the disclosure requirements to the investors' information absorption capacity and to what investors consider relevant when making investment decisions, has resulted in new amendments to the prospectus regime. The introduction of the 'key investor information document', first in the area of collective investment, and subsequently in the general prospectus regime and, more recently, in the field of retail structured

finance instruments, seems to be in part based on insights gained from behavioural finance research that challenges the rationality of investors in terms of their ability to make well-founded investment decisions based on the supply of complete information. The operation of the summary prospectus under the 2003 Prospectus Directive and the UCITS regime indicated that even the summary was too elaborate for retail investors. Disclosure in the 'key investor information' document is therefore limited to a few very essential elements, condensed into a standardised document of limited length, the contents of which is strictly regulated.

Interestingly, the successive regulatory initiatives that introduce the concept of 'key investment information'also comply with a shift in the civil liability regime surrounding the information disclosure regime. As indicated above, a 'no liability' regime was applied to the summary prospectus under the 2003 Prospectus Directive. The Key Investor Information Document, introduced by the 2009 UCITS IV directive in the field of collective investment, essentially followed the 'no liability' rule of the summary prospectus.[9] The 2010 revision of the Prospectus Directive, which *inter alia* narrowed down the substance of the summary prospectus to key information, also introduced a further exception to the 'no liability rule'. Civil liability can now also result from the summary prospectus if it does not provide the key information to aid investors when considering whether or not to invest in the offered securities.[10] While the liability standard is still essentially based on the quality of the full prospectus, the incomplete character of the summary prospectus regarding the prescribed key information can at present form a separate basis for civil liability. More importantly, in setting this liability standard, the Prospectus Directive emphasises the function of the summary prospectus with key information in assisting investors in their investment decision: the shift in the liability regime seems to confirm that investors are no longer required to base their investment decision in any event on the full prospectus.

A further step has been taken in the draft regulation on Packaged Retail Investment Products,[11] which targets structured investment products in various forms (including insurance contracts or structured deposits) when specifically targeted at retail investors. The regulation introduces the obligation to supply a *key information document* (KID) for a range of structured financial products, including products for which no specific disclosure regime has yet been applied (e.g. unit-linked life insurance). As this document in some cases is the only piece of information to be supplied to prospective retail investors,[12] the civil liability regime is fully tailored to the quality of that key information document: according to the draft regulation (Article 6), the information contained in the

KIID should be accurate, fair, clear and not misleading. Civil liability will apply when these standards have not been met and the investor has relied on the KID (Article 11). Contrary to the liability regime for key documents in the Prospectus and UCITS IV directive, the KID should itself satisfy certain quality standards, non-observance of which can lead to civil liability on the part of the product manufacturer. Moreover, the draft regulation operates a reversal of the burden of proof, where it is up to the product manufacturer to demonstrate that the KID satisfies the standards of the regulation when the investor has showed that he has suffered losses by relying on the KID. However, the explicit requirement that the victim also prove reliance on the document in order to engage civil liability is new in the regime for PRIPs, and constitutes a further departure from the efficient capital market hypothesis: the investor is no longer, as a rational person, automatically supposed to have used all the information available in the market. Herding behaviour, impulsive or emotional investment decisions by the investor, without relying on information made available to him, will no longer be protected under the liability regime. Although this may, at first sight, be a step backwards from the perspective of investor protection, the fact that key information in itself can constitute the basis for civil liability represents a clear improvement for the investor seeking a civil remedy for investment losses. This is ever the more the case as the PRIPs liability regime is also applied when the KID has been produced for securities issues falling within the scope of the Prospectus Directive, for which a full and a summary prospectus have also been drafted.

In sum, the regulatory response to the crisis has not, so far, fundamentally altered the philosophy underlying the disclosure regime for the offer of investment products on primary capital markets: as a rule, no *ex ante* limits exist on the design of financial instruments targeted at (retail) investors, who are supposed to base their investment decisions on information supplied by the issuer. However, the regulatory regime does gradually depart from the assumption that investors are fully informed and are able to absorb all information supplied to them or otherwise available in the market. Instead, in view of inherent cognitive limitations of investors, the latter should be supplied only with the (key) information that will actually impact on their investment behaviour. Investors should no longer have to rely on all the information available in the market, but rather make investment decisions based on other considerations. Hence, the assumption that investors rely on the information in the market should no longer to be taken for granted. On the other hand, issuers will to a lesser extent be able to use a full prospectus as a disclaimer against investors, as it will no longer be automatically assumed that the investors have used all the information in making their investment decision.

2. The role of financial intermediaries in post-crisis investor protection: towards more intrusive regulation

While the prospectus regime accompanying the offer of securities on the primary market remains largely unchanged, financial institutions acting as distributors of financial products have come under closer scrutiny by regulators, following different examples of mis-selling and distribution of highly complex financial products. Various initiatives have been taken, both at a national and at an EU level, that have resulted in a patchwork of measures aimed at avoiding some of the weaknesses in investor protection identified during the financial crisis. Apart from institutional reforms, where several Member States adopted a 'twin peaks' approach to supervision, insulating market and conduct of business supervision from prudential supervision, a common orientation of Member States' reform initiatives is to put filters on the conduct of financial intermediaries in the supply of financial instruments to retail customers. These can take different forms, with varying degrees of supervisory involvement. These include streamlining internal organisation processes, by obliging regulated firms to introduce a product approval process[13] that will determine the adequate target group for financial products; enhanced disclosure and risk warning by financial intermediaries[14]; self-restraint by financial institutions in the offer of certain financial products[15] and product bans imposed by the supervisor,[16] which results in an *ex ante* prohibition to distribute certain products. From a market integration perspective, this situation of non-coordinated national initiatives presents a serious risk of market fragmentation, inconsistencies and regulatory overlap. A common EU approach should therefore aim to strike a fair balance between adequate investor protection and market integration.

The current EU initiatives, particularly in the context of the MiFID reform, are likely to result as well in a more proactive role of supervisory authorities at the level of the distribution of financial products to retail investors, putting filters on the supply side. Both a product approval process, and a product ban are contemplated in the MiFID-II reform package.[17]

a. Prudential dimension: 'product approval process'

Although the initial Commission reform proposal, launched in October 2011, was silent on this point, the amendments approved by the European Parliament in its first reading included the obligation for all investment firms and credit institutions providing investment services to introduce a product approval process as part of their internal organisation requirements (Article 16.3 of the directive).[18] More generally, the regulated firms would have to elaborate a

policy and other necessary arrangements to meet the following objectives:

- to assess the compatibility of the investment product with the needs of the clients to whom it would be offered;
- to ensure that investment products or structured deposits designed by the firm for sale to professional or retail clients meet the needs of an identified target market;
- to ensure, for investment firms marketing investment products, that the investment product is marketed to clients within the target group

For financial products designed by the investment firm itself, the product approval process implies that no investment product or financial instrument can be placed or distributed in the market without prior internal approval. Moreover, the product approval process is a dynamic, ongoing process: it requires existing products to be regularly reviewed in order to ensure that the product continues to meet the needs of the identified target market.

Conceptually, the product approval process is part of the prudential requirements incumbent on regulated firms with respect to their internal organisation. The product approval process will oblige regulated firms to have the necessary procedures in place to assess internally the target market and the intended marketing techniques for each newly designed financial product, thereby introducing a formalised internal system that will necessarily entail an *ex ante*, upfront filter on the offer of financial products to (retail) clients. The role of the supervisory authority in this regard seems rather limited: the supervisor will ascertain whether the procedure is designed well enough to enable the regulated firm to properly identify the relevant parameters to determine the target group, and to apply the approval and review process in a comprehensive manner. The product approval itself essentially remains an internal (business) decision of the regulated firm, with no space for the supervisor to intervene directly into the process or its outcome. Viewed from this angle, the product approval process is not intrusive, but rather constitutes a further specification of the general prudential requirement for regulated firms to possess sound internal organisation arrangements.

Within the system of the MiFID-directive, the inclusion of the product approval process into the prudential sphere implies that it follows the home country control principle underpinning the exercise of prudential supervision in a cross-border setting. Consequently, the product approval process will also be monitored by the competent home country supervisor for the investment services provided under the regime of branch establishment or freedom to provide services.

It is not clear, however, to what extent the introduction of an explicit product approval process-requirement, as proposed by the European Parliament, will be maintained in the final text of the directive, which still needs the formal approval of the Council and the European Parliament in plenary session. Quite surprisingly, the compromise text submitted by the European presidency in June 2013 did not include the proposed amendments to Article 16 by the European Parliament. This is not to say that the product approval process has been dismissed as a viable technique for ensuring increased investor protection awareness upfront in the transaction chain of investment products. Investor protection should not be part of the general principles of good internal organisation.

1. In the absence of regulation, investors could enquire the issuers to satisfytheir information needs. In the absence of regulation, this will prove feasible only when a limited number of prospective investors are targeted and whentheseinvestors are willing to invest for a sufficiently large amount, as gathering and interpreting the information entails transaction costs. Once the transaction cost for the prospective investor out weighs the possible profit to begained from the investment, a system of one-on-one supply of information between the issuer and the investors will no longer besufficient. Regulatory intervention, by way of an obligation to supply information in a standardised format, enables the transaction cost for individual investors to bereduced, and will more over produce information in a standardised format, thus enabling investors to compare investments.

2. Directive 2003/71/EC of the European Parliament and of the Council of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC, OJ L 345, 31 December 2003, p. (INSERT PAGE NUMBER)

3. The 2003 Prospectus Directive instituted a fully-fledged 'European passport' system for prospectuses: once approved by the competent authority, as determined according to the directive, the issuer can offer the securities, usingthis prospectus, in anyother EU Member State, without having to comply with any additional disclosure requirement.

4. See Commission Regulation 809/2004 of 29 April 2004 implementing Directive 2003/71/EC of the European Parliament and of the Council as regards information contained in prospectuses as well as the format, incorporation by reference and publication of such prospectuses and dissemination of advertisements, OJ L 149 of 30 April 2004, p. 1.

5. See Article 6, Prospectus Directive.

6. Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EE, OJ L 145, 30 April 2004, p. 1.

7. See Article 19.2, MiFID.

8. When the client uses an 'executiononly' service, the investment firm is still under obligation to inform the client properly about the (brokerage) service and the risks generally associated with certain kinds of financial instruments. The more individually targeted obligations to warn clients against inappropriate investment products or to offer suitable advice do not apply for 'executiononly' services. 'Executiononly' will only apply to brokerage services regarding 'non-complex' financial instruments and where the initiative for the investment lies with the customer.

9. See, notably, Article 79 of Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS), OJ L 302/32 of 17 November 2009. Article 79.2 of the directive attaches liability only to situations where the key investor information document ismisleading, inaccurate or inconsistent with the relevant parts of the prospectus.

10. Article 6.2 Prospectus Directive, as amended by Directive 2010/73/EU of 24 November 2010, provides that: "Member States shall ensure that no civil liability shall attach to any person solely on the basis of the summary, including any translation thereof, unless it is misleading, inaccurate or inconsistent, when read together with the other parts of the prospectus, *or it does not provide, when read together with the other parts of the prospectus, key information in order to aid investors when considering whether to invest in such securities.* The summary shall contain a clear warning to that effect." (Italics added by the author).

11. Better known under its acronym PRIPs. See Proposal for a Regulation of the European Parliament and of the Council on key information documents for investment products, COM(2012) 352 final, 3 July 2012.

12. The obligation to supply a KID will possibly apply in parallel to other disclosure requirements, such as the full prospectus and the summary prospectus when the structured financial product takes the form of "securities".

13. Better known as the 'product approval process', which has been adopted *inter alia* in the Netherlands by

the financial market authority, and in the United Kingdom by the Financial Conduct Authority, as part of the supervisory regime of regulated financial institutions.

14. See, for instance, in the Netherlands, the practice of producing a financial information leaflet ('financiëlebijsluiter') for complex financial products.

15. This iscurrently the case in Belgium, where almost all financial institutions have voluntarily agreed on a 'moratorium' on the distribution of 'overly complex' financial products. The voluntary character of the moratorium should be somewhat mitigated, as the initiative for the moratorium emanated from the supervisory authority, which may have produced a compelling effect on the regulated firms to subscribe to the moratorium.

16. In the United Kingdom, the Financial Conduct Authority has the option to issue product intervention rules (see section 137D Financial Services and Markets Act (FSMA), as introduced by the Financial Services Act 2012. The UK Financial Conduct Authority has elaborated a 'policy statement' under section 138N FSMA, detailing under what circumstances it will make use of its product intervention powers: See FCA, *The FCA's use of temporary product intervention rules*, PS13/3, March 2013, availableat http://fca.org.uk

17. The reform proposals take the form of a proposal for a directive modifying the MiFID directive 2004/39/EC on the one hand (See COM(2011)0656, 20 October 2011), and a proposal for a regulation on markets in financial instruments on the other (better known as "MiFIR": see COM(2011)652 of 20 October 2011).

18. For the text, see: European Parliament, doc. P7_TA(2012)0406, 26 October 2012, availableat http://www.europarl.europa.eu.

Chapter Three

Role of the Prospectus Directive in Integrating the EU Exchange-Regulated Markets

Chapter Three

Role of the Prospectus Directive in Integrating the EU Exchange-Regulated Markets[1]

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1. Introduction

The Prospectus Directive 2003/71/EC[2] regulates the prospectus when securities are offered to the public or admitted to trading on a regulated market.[3] Accordingly, the Directives have left the regulation of non-public offers to the Member States' legislative bodies.[4]

Thus, an exchange-regulated market for professional investors is outside the scope of the EU Prospectus. The distinction between wholesale and retail markets does not apply to this market, which allows securities with denominations under €50,00000 to be offered to the wholesale market. In addition, financial information can be provided under any national GAAP (Generally Accepted Accounting Principle).[5] The professional investors market therefore provides an alternative for those issuers that either do not prepare or do not wish to prepare their financial information in accordance with IFRS (International Financial Reporting Standards) or an equivalent set of accounting standards, or that wish to offer lower denomination securities to wholesale investors.[6]

The key purpose of the Directive 2003/71/EC (amending Directive 2001/34/EC) is rather to harmonise requirements for the drawing up, approval and distribution of the prospectus, which is to be published in instances where securities[7] are either offered to the public or admitted to trading on a regulated market.[8] The Directive is amongst other European Commission initiatives on accounting standards and transparency requirements, which together are aimed at producing a strategy to improve the quality of information that is provided to investors. It also intends to unify the regulatory regimes to enhance cross-border offers.[9] The

Directive does not, however,harmonise the system of enforcement,civil or criminal liability or other relevant areas.[10] A false statement in the prospectus, for example, could therefore potentially trigger different local liability regimes, principles and doctrines, depending on the applicable law and according to the conflict of laws.[11]

Investments in securities, like any other form of investment, involve risk.The Directive assures safeguards for protecting the interests of actual and potential investors,thus enabling them to make their respective investment decisions alongside informed assessments of such risk, with all relevant facts and information disclosed. Such information, which must be as objective as possible in terms of the issuer's financial circumstances and the rights that are attached to the securities, and of a sufficient amount, should be presented in a form that is both digestible, and easily analysable.[12]

2. Substantive Provisions of the Prospectus Directive

The key provisions of the Directive 2003/71/EC could be summarised in the following way: (a) prospectus requirements, which prescribes the content and format of the prospectuses, allowing issuers to incorporate by reference, allowing the use of three-part prospectuses and setting out the exemptions from the requirement to produce prospectuses;[13] (b) approval and publication of the prospectus, which lays down procedures for the approval of prospectuses, and how and where they must be published;[14] (c) passport rights, which introduces administrative measures to facilitate the passporting of prospectuses on a pan-European basis, making it easier for companies to raise capital across Europe;[15] (d) third country issuers, where prospectusesdrawn up under a third country's law can be treated as equivalent to the Directive requirements (determined on a case-by-case basis); and (e) other provisions requiring issuers to produce annual information updates and the establishment of a qualified investors register.[16] The prospectus directive thus seeks to impose an exhaustive maximum disclosure regime that applies uniformly across the EU and leaves no room for Member States to impose additional requirements on issuers.[17]

The prospectus Directive applies with immediate and ongoing effect to issuers of certain types of non-exempt securities,[18] namely equity securities and low denomination debt securities. Each issuer of non-exempt securities will have a single, permanent home Member State whose competent authority is responsible for the approval of all of the issuer's prospectuses for non-exempt securities.[19]

Moreover, the obligation to publish a prospectus does not apply when the offer

is addressed to qualified investors,[20] and to fewer than 150 persons (natural or legal) per Member State (private placement).[21] Subsequent resales of securities are treated as offers in their own right.[22] The exemption from producing a prospectus in the case of conversion offers, takeovers, mergers and employee offers is provided inthe consolidated Directives.[23]

The Prospectus Directive, however, does not give precise guidance as to when an offer is made "to the public". This may lead to different judicial interpretations as to what constitutes an offer to the public; namely whether something more than a specific number of recipients, such as 150 persons, for example, is needed to trigger disclosure obligations.[24]

Both the prospectus Directive and the transparency Directive[25] distinguish between the retail regime and the wholesale regime. This distinction applies to debt securities and asset-backed securities (provided that they do not carry any rights to acquire shares) and, significantly, is linked to the denomination of securities rather than to the number or category of the investor. Securities that have a minimum denomination of less than €50,00000 are classed as retail, whilst securities that have minimum denominations of more than €50,00000 arecategorised as wholesale. Under this regime, issuers of retail debt will be required to undertake more onerous disclosure requirements, whilst issuers of wholesale debt will benefit from alternative, less onerous requirements. Financial information to be included in a prospectus for retail debt for any financial year must be prepared in accordance with international financial reporting standards (IFRS) or another equivalent set of accounting standards.[26] In such cases they are required to restate their accounts in IFRS in order to maintain the validity of their prospectus.[27]

Issuers of debt securities under the wholesale regime must instead provide: (a) a statement declaring that the financial information included in the prospectus has not been prepared in accordance with the IFRS and that there might be material differences in the financial information than had the IFRS been applied to the accounts; and (b) a description of the differences between IFRS and the accounting principles used in the preparation of the financial statements.[28]

For interim financial information, the same distinction applies. In the case of retail debt, an issuer that has published quarterly or half yearly financial information since the date of its last audited financial statements must include the interim financial statement in its prospectus. Additionally, for retail debt issuances that closed more than nine months after the date of the end of the last financial year, the prospectus must include interim financial information, covering a minimum of six months of the financial year. This requirement applies irrespective of whether the issuer has published any interim financial information. The latter information, provided in a

prospectus, must also include comparative statements for the same period of the previous financial year.[29]

Issuers of wholesale debt do not need to comply with these interim financial information requirements. Moreover, it is required that enhanced and more detailed issuer disclosure be included in the prospectus for debt as opposed to wholesale issuances. For debt issuances of less than €50,00000, descriptions are required of the issuer's main markets of operation and principal investments. For further clarification, the prospectus should contain all information which, according to the particular nature of the issuer and of the securities offered to the public or admitted to trading on a regulated market, is necessary to enable investors to make an informed assessment of the assets and liabilities, financial position, profit and losses, and prospects of the issuer and of any guarantor, and of the rights attaching to such securities.[30]

3. Prospectus: Summary and Circulation of Various Documents

The prospectus contains information concerning the issuer and the securities. It should also include a summary.[31] The Directive illustrates the contents of the summary, which should, in a manner that is brief and free from technical language, convey the essential characteristics and risks associated with the issuer, any guarantor and the securities, or the securities themselves. The summary should provide key information in the language in which the prospectus was originally drawn up. It should also contain a warning, insisting that: (a) it should be read as an introduction to the prospectus; (b) any decision to invest in the securities should be based on a consideration of the prospectus as a whole by the investor; (c) civil liability attaches to those persons who have tabled the summary including any translation thereof, and applied for its notification, but only if the summary is misleading, inaccurate or inconsistent when read together with the other parts of the prospectus.[32]

In order to achieve maximum regulatory convergence throughout the EU, the obligations have been outlined again in broad detail in the Commission regulations, which, without further transposition, are binding for Member States.[33] Hence, the rules on prospectuses are not just found in the prospectus Directive, but in the Commission regulations, and arguably the recommendations issued by the Committee of European Securities Regulators (CESR) in interpreting the Directive and regulations.[34]

The Directive allows the issuer, offeror or company asking for admission to trade

on a regulated market to draw up a prospectus, whether as separate documents or as a single document. The required information in a prospectus composed of separate documents shall be divided as a registration document, securities note and a summary note.[35] The registration document shall contain the information relating to the issuer, and the securities note shall contain the information concerning the securities offered to the public or to be admitted to trading.[36]

Thus, to facilitate the circulation of the various documents that constitute the prospectus, the Directive encourages the use of electronic communication facilities such as the Internet. To ensure easy access to information, the prospectus should always be delivered in paper form, and should be free of charge upon request to investors. Moreover, a new event liable to influence the assessment of the investment[37] that arises after the publication of the prospectus, but before the closing of the offer or the commencement of trading on a regulated market,[38] should be properly evaluated by investors; and therefore necessitates that a supplement to the prospectus be approved and disseminated.[39]

In order to avoid detrimental consequences for an issuer, the prospectus Directive authorises that competent authority in certain circumstances to omit sensitive information from a prospectus.[40] This actually serves the aims of disclosure as it ensures that the information presented is both current and reliable, and that investors are fully versed in the facts of the situation regarding dealing in securities.

4. Base Prospectus

The prospectus can, at the choice of the issuer, offeror or person asking for admission to trading on a regulated market, consist of a base prospectus.[41] This will contain all of the relevant information concerning the issuer and the securities that are offered to the public or admitted to trading on a regulated market for the following types of securities: (a) non-equity securities, including warrants in any form, issued under an offering programme; (b) non-equity securities issued in a continuous or repeated manner by credit institutions, (i) where the sums deriving from the issue of said securities, under national legislation, are placed in assets which provide sufficient coverage for the liability deriving from securities until their maturity date; and (ii) where, in the event of the insolvency of the related credit institution, said sums are intended, as a priority, to repay the capital and interest falling due.[42]

The information given in the base prospectus shall provide updated information

on the issuer and on the securities to be offered to the public or to be admitted to trading on a regulated market. However, if the final terms of the offer are not included in either the base prospectus or a supplement, the final terms shall be provided to investors and filed with the competent authority when each public offer is made, which must be made as soon as practicable and, if possible, in advance of the beginning of the offer.[43]

The idea of the base prospectus is to introduce a fast track procedure for issuers admitted to trading and who frequently raise capital on these markets. The advantage of a base prospectus is that all the relevant information about the issuer and the securities can be filed and then supplemented by filing the final terms of particular issues without the competent authority having to approve these additional supplements.[44]

5. Publication of the Prospectus

The prospectus Directive provides clear provisions in relation to the publication of the prospectus. Once approved, the prospectus shall be made available to the public as soon as practicable, and, in any case, at a reasonable time in advance of the offer to the public or the admission to trading of the securities involved. Additionally, in the case of an initial public offer of a class of shares not already admitted to trading on a regulated market that is to be admitted to trading for the first time, the prospectus should be made available at least six working days before the end of the offer.[45] Furthermore, the Directive explains when the prospectus should be made available to the public; i.e. when it is published either by insertion in one or more newspapers circulated throughout, or widely circulated in, the Member States in which the offer to the public is made or the admission to trading is sought; or in a printed and electronic form. However, where the prospectus is made available by publication in electronic form, a paper copy must nevertheless be delivered (free of chargeand upon request of the issuer, the offeror, the person requesting admission to trading or the financial intermediaries placing or selling the securities) to the investor.[46]

Consequently, adopting the rules of prospectus publication stated in the aforementioned Directive might cover the legislative gaps in other regimes, including Palestine. In principle, a reasonable period for publishing the prospectus before the beginning of the subscription should be identified in the regulations, where the competent authority is given the power to specify the appropriate time on a case-by-case basis. The time criterion in this regard should satisfy the needs of the investor or its advisers to make an informed

investment decision. Otherwise, the objectives of requiring the prospectus will not be fully achieved.

6. Liability for the Safety of the Prospectus

In relation to the responsibility attached to the prospectus, the prospectus Directive ensures that responsibility for the information given in a prospectus is attached at least to the issuer or its administrative, management or supervisory bodies, the offeror, the person asking for the admission to trading or the guarantor.[47] The persons responsible shall be clearly identified in the prospectus by their names and functions or, in the case of legal persons, their names and registered offices, as well as declarations by them that, to the best of their knowledge, the information contained in the prospectus is in accordance with the facts and that the prospectus makes no omission likely to affect its import.[48] Additionally, civil liability applies to those persons.[49] Yet, as mentioned earlier, the Directive certifies that no civil liability shall attach to any person solely on the basis of the summary, unless it is misleading, incorrect or incoherent when read holistically with the remainder of the prospectus.[50]

Nevertheless, the Court of Justice of the European Union has ruled that the liability attaching to the prospectus should apply to the issuer of the securities and also to its board, even if they were not explicitly mentioned as responsible. The court adds:

> [a]rticle 21 of Directive 2001/34/EC of the European Parliament and of the Council of 28 May 2001 on the admission of securities to official stock exchange listing and on information to be published on those securities is to be interpreted as meaning that it does not preclude a national legislature from laying down, for cases where the information recorded in listing particulars published with a view to admitting securities to official stock exchange listing proves to be inaccurate or misleading, administrative penalties imposable not only upon the persons expressly mentioned in those particulars as responsible but also upon the issuer of the securities and, indiscriminately, upon the members of the issuer's Board of Directors, regardless of whether the board members have been identified as responsible in the listing particulars.[51]

The aforementioned provisions, laid out in the prospectus Directive,due to their clarity and perhaps their capacity to achieve deterrence and be consistent with the stated judgment of the European Court of Justice are nevertheless transferable to other regimes. Hence, any person that subscribes to a public offer has the right to pursue a claim for compensation if that person suffers loss or damage when acquiring the securities to which the offer document relates. Compensation will be payable where the damage or loss occurs as a result of any untrue or misleading statement, or any omission in the offer document that should have been included within the prospectus or listing particulars. Liability, therefore, is not dependent upon whether the subscriber had placed reliance on the misstatement or had knowledge of any omission.[52]

7. Conclusion

Despite the fact that the prospectus Directive represents developments on several aspects of public offering in comparison with the consolidated Directives, some issues are still left untreated by this Directive. Thus, it could be criticised for granting extensive powers to the competent authorities that might reduce the volume of harmonisation intended by the Directive, leaving uncertain legal matters relating to private placement (an exception not to public offering but to the obligation to publish a prospectus), and forallowing each Member State the right to determine their own standards of liability regarding prospectuses.[53]

Nevertheless, various provisions of the prospectus Directive, on both policy and technical levels, could be effortlessly adopted in other regimes. In particular, consultations with stakeholders and the conducting of regulatory and periodic impact assessments according to the associated rules, and the specific manner in which investors are protected.This may also refer to the way in which the prospectus is drawn up and published (e.g., its summary, components and electronic dissemination).

The prospectus Directive also helps to facilitate the integration process of some technical approaches in other jurisdictions in the field of offering securities, such as the single "passport", and incorporation by reference. The national capital market authorities can transplant the principle of these concepts for foreign issuers, but requires controls to make implementation possible. Yet, complicated procedures for approval or significant administrative arrangements

should not be required by the national capital market authorities in relation to other state issuers. The fundamental criterion that must be sought in this respect is the availability of investor protection.Thus national authorities, e.g. Palestine, may not require a foreign issuer to prepare the prospectus according to the national regime if the issuer and/or its sponsor or advisor certifies that the prospectus meets, at least, the national requirements. Or, if the competent authority of the state of the issuer, if that state follows the advanced models in drawing up prospectuses, declares in writing that the prospectus was drawn up in accordance with the relevant applicable legislation.

1. The idea of this paper has been taken from the doctoral thesis of the author entitled, 'The Efficiency of the Listing and Disclosure Rules of the Palestine Stock Exchange: A Critical Review', (Brussels: Vrije Universiteit, 2011) (unpublished).
2. Directive 2003/71/EC of the European Parliament and of the Council of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC, OJ L 345, December 31, 2003, 64–89. Directive 2001/34/EC has been also amended by Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC, OJ L 390, December 31, 2004, 38–57. Directive 2003/71/EC has been amended by (1) Directive 2008/11/EC of the European Parliament and of the Council of 11 March 2008 amending Directive 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading, as regards the implementing powers conferred on the Commission, OJ L 76, March 19, 2008, 37–38; (2) Directive 2010/73/EU of the European Parliament and of the Council of 24 November 2010 amending Directives 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading and 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market, OJ L 327, 11.12.2010, pp. 1–12.
3. Article (2) of this Directive defines "offer of securities to the public» as "a communication to persons in any form and by any means, presenting sufficient information on the terms of the offer and the securities to be offered, so as to enable an investor to decide to purchase or subscribe to these securities. This definition shall also be applicable to the placing of securities through financial intermediaries". Thus, it appears that the Directive introduces a new EU-wide definition of an "offer to the public", as well as new EU-wide transactional exemptions for non-public offers. See H. Hofmann and A. Türk, *EU Administrative Governance* (Cheltenham: Edward Elgar Publishing, 2006), p.185
4. Item (9) and article (20) of Directive 2001/34/EC provide that safeguards for the protection of the interests of actual and potential investors are required in most Member States of undertakings offering their securities to the public, either at the time of their offer or of their admission to official stock exchange listing; such safeguards require the provision of information which is as sufficient and as objective as possible concerning the financial circumstances of the issuer and particulars of the securities for which admission to official listing is requested. The form in which this information is required usually consists of the publication of an information sheet, referred to as "listing particulars".
5. See article (1) of the Commission Regulation (EC) No 1787/2006 of 4 December 2006.
6. Despite the fact that the Prospectus Directive and the implementing regulation thereunder have made it easier to publicly offer and list securities not only in one country, but in several countries at the same time, the procedures and cost of preparing a prospectus might have led issuers to avoid the prospectus regime, either by listing their shares only on markets that are not classified as regulated markets for the purposes of Community law without a public offering, or by restricting their offering to qualified investors or otherwise ensuring that the offer falls within an exemption under the Directive. European Securities Markets Expert Group (ESME), 'Report on Directive 2003/71/EC of the European Parliament and of the Council on the Prospectus to be Published when Securities are Offered to the Public or Admitted to Trading,' 4, Brussels, September 5, 2007.
7. Article (2) of the this Directive defines «securities» as transferable securities as defined by article 1(4) of Directive 93/22/EEC with the exception of money market instruments as defined by article 1(5) of Directive 93/22/EEC, having a maturity of less than 12 months. For these instruments, national legislation may be applicable. This article has been replaced by article (4) of the Directive 2004/39/EC which provides that: "transferable securities" means those classes of securities which are negotiable on the capital market, with the exception of instruments of payment, such as: (a) shares in companies and other securities equivalent to shares in companies, partnerships or other entities, and depositary receipts in respect of shares; (b) bonds or other forms of securitised debt, including depositary receipts in respect of such securities; (c) any other securities giving the right to acquire or sell any such transferable securities or giving rise to a cash settlement determined by reference to transferable securities, currencies, interest rates or yields, commodities or other indices or measures. (Directive 2004/39/EC of the European

Parliament and of the council of 21 April 2004 on markets in financial instruments amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EEC, Official Journal of the European Union, April 30, 2004, L145/1).

8. Council Directives 80/390/EEC of 17 March 1980 coordinating the requirements for the drawing up, scrutiny and distribution of the listing particulars to be published for the admission of securities to official stock exchange listing, and 89/298/EEC of 17 April 1989 coordinating the requirements for the drawing up, scrutiny and distribution of the prospectus to be published when transferable securities are offered to the public, were adopted several years ago introducing a partial and complex mutual recognition mechanism which is unable to achieve the objective of the single passport provided for by this Directive. Those directives should be upgraded, updated and grouped together into a single text. Meanwhile, Directive 80/390/EEC was integrated into Directive 2001/34/EC of the European Parliament and of the Council of 28 May 2001 on the admission of securities to official stock exchange listing and on information to be published on those securities, which codifies several Directives in the field of listed securities. For reasons of consistency, however, Directive 2003/71/EC came to regroup the provisions of Directive 2001/34/EC, which stem from Directive 80/390/EEC together with Directive 89/298/EEC and to amend Directive 2001/34/EC accordingly. See the preamble and article (1) of Directive 2003/71/EC. Art. (4/14) of the Directive 2004/39/EC defines «Regulated Market» as "a multilateral system operated and/or managed by a market operator, which brings together or facilitates the bringing together of multiple third-party buying and selling interests in financial instruments- in the system and in accordance with its non-discretionary rules - in a way that results in a contract, in respect of the financial instruments admitted to trading under its rules and/or systems, and which is authorised and functions regularly and in accordance with the provisions of Title III". This Directive requires Member States to draw up a list of its regulated market.

9. S. Griffin, *Company Law: Fundamental Principles* (Harlow: Pearson Education Ltd, 2006), p.185. The Forum of European Securities Commissions, the predecessor to the CESR, in late 2000 concluded to the Commission that the mutual recognition of prospectuses did not work in practice as Member States had imposed inconsistent requirements, posing an obstacle for risk capital allocation across national borders. The Forum of European Securities Commissions (FESCO), 'A European Passport for Issuers, a Report for the EU Commission,' December 20, 2000, Ref.: Fesco/00-138b.

10. H. Hofmann, A. Türk (eds), *EU Administrative Governance*, 246 (Cheltenham, UK: Edward Elgar Publishing, 2006). This may be justified by the general tendency in reducing the role of criminal sanctions in securities sector, in turn expanding the role of civil and administrative liabilities and penalties. It is thus believed that civil punishments represented by heavy fines and suspension from trading could provide an adequate sanction that could be effectively implemented. To this effect, the competent authorities could be given investigative powers in a manner similar to a court conducting investigations into circumstances constituting breach. See B. Ali El-Dean, *Privatisation and the Creation of a Market-basedLegal System: the Case of Egypt*, 61-63 (Leiden, Boston, and Koln: Brill 2002). Such investigations exist in the Palestinian regulatory regime, as will be shown later. However, we think that the investigators must be given the power to refer violations to a criminal tribunal where appropriate if the actions represent a contravention of the effective laws and regulations so as to achieve deterrence, which is important to protrect the economic and financial sectors from threat in response to the public interest.

11. L. Enriques& M. Gatti, 'Is There a Uniform EU Securities Law After the Financial Services Action Plan?,*Stanford Journal of Law, Business & Finance, 14 (2008), p.59.*

12. Items (19 and 20) of the Directive.

13. By reference to one or more previously or simultaneously published documents that have been approved by the competent authority of the home Member State or filed with it in accordance with this Directive, in particular pursuant to the prospectus directive (or the transparency Directive 2004/109/EC as in the proposed amendment). The information available to the issuer should be up-to-date. However, the summary shall not incorporate information by reference. When information is incorporated by reference, a cross-reference list must be provided in order to enable investors to identify easily specific items of information. Art. (11).

14. Article (14) permits the publication of the prospectus either in printed or electronic form. In cases where the prospectus is published in electronic form, this article grants the right of the investor to receive a paper copy of the prospectus. The commission, however, is to consider that the electronic provision of information would be solely sufficient for effective supervision. See EC, 'Commission Staff Working Document accompanying the proposal for a Directive of the European Parliament and of the Council amending Directives 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading and 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market, Impact Assessment,' 17, supra.
15. Passport mechanism means that the prospectus approved by the competent authority in one Member State is valid for public offers and admission to trading of securities in the entire EU. This means that once the competent authority in the relevant Member State has approved the prospectus, it will then be accepted elsewhere in the EU. An issuer's home Member State will determine which competent authority is responsible for approving the prospectuses and for ensuring that the obligations of issuers and others under the Directive are met. Indeed, the Commission has been aware of the need to update the prospectus regime to facilitate raising cross-border capital since 1998. See Commission of the European Communities, 'Risk Capital a Key to Job Creation in The European Union,' Action Plan, Jun 1998, retrieved on September 15, 2009 from http://ec.europa.eu/internal_market/securities/docs/risk_capital/risk_cap_act_plan_en.pdf.
16. It should be noted that the Commission has implemented the regulation of this Directive in Commission Regulation (EC) 809/2004, implementing Directive 2003/71/EC of the European Parliament and of the Council as Regards Information Contained in Prospectuses as well as the format, incorporation by reference and publication of such prospectuses and dissemination of advertisements. OJ L 149, April 30, 2004, pp. 1–126. This regulation has been amended by the following: a. Commission Regulation (EC) No 1787/2006 of 4 December 2006. OJ L 337, 5.12.2006, pp. 17–20, b. Commission Regulation (EC) No 211/2007 of 27 February 2007. OJ L 61, 28.2.2007, pp. 24–2, and c. Commission Regulation (EC) No 1289/2008 of 12 December 2008. OJ L 340, 19.12.2008, pp. 17–19.
17. E. Ferran, *Building on EU Securities Market* (Cambridge: Cambridge University Press, 2004), p.138.
18. The exemptions from publishing prospectus are prescribed in Art. (1) of the Directive as amended in 2010.
19. Art. (2) of the Directive.
20. Article (2/e) of the consolidated Directive defines «qualified investors» as "persons or entities that are described in points (1) to (4) of Section I of Annex II to Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments, and persons or entities who are, on request, treated as professional clients in accordance with Annex II to Directive 2004/39/EC, or recognised as eligible counterparties in accordance with Article 24 of Directive 2004/39/EC unless they have requested that they be treated as non-professional clients. Investment firms and credit institutions shall communicate their classification on request to the issuer without prejudice to the relevant legislation on data protection. Investment firms authorised to continue considering existing professional clients as such in accordance with Article 71(6) of Directive 2004/39/EC shall be authorised to treat those clients as qualified investors under this Directive".
21. Article (3/b) of the Directive as amended in 2010.
22. L. Bertran, *Raising Capital in Europe: The legal FrameworkFollowing the EU Prospectus Directive* (UK: Richmond Law, 2005), p.23. Article (3) of the Directive also exempts the following types of offer from the obligation to publish a prospectus: (c) an offer of securities addressed to investors who acquire securities for a total consideration of at least EUR 100000 per investor, for each separate offer; and/or; (d) an offer of securities whose denomination per unit amounts to at least EUR 100000; and/or; (e) an offer of securities with a total consideration in the Union of less than EUR 100000, which shall be calculated over a period of 12 months.
23. Provided that a document is available containing information regarded by the competent authority as equivalent to that of the prospectus, taking into account the requirements of Union legislation. For further information see Art. (4) of the Directive as amended in 2010.

24. L. Enriques and M. Gatti, supra, p.56. U. Tauboeck, H. Jackson and H. Scott, supra, pp.27-28. The European Securities Committee suggested to the EC to set up an exact definition of offers of securities to the public. See summary record of the 63rd meeting of the European Securities Committee of February 11, 2009, working document ESC-3-2009.

25. Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC, (and its amendments) Official Journal L 390, December 31, 2004, 38- 57.

26. These standards are the Generally Accepted Accounting Principles of Canada, Japan or the United States of America. See article (1) of the Commission Regulation (EC) No 1787/2006 of 4 December 2006 amending Commission Regulation (EC) 809/2004 implementing Directive 2003/71/EC of the European Parliament and of the Council as regards information contained in prospectuses as well as the format, incorporation by reference and publication of such prospectuses and dissemination of advertisements. Official Journal L 337, December 5, 2006, pp. 17– 20.

27. Art. (3) of the prospectus Directive. Item (15) of the transparency Directive.

28. J. Kravitt, *Securitization of Financial Assets*, (New York: Aspen Publishers, 2009), pp.134-136.

29. Ibid, p.135.

30. See chapter (II) of the Directive.

31. In accordance with article 5 of the Directive, summary is not required for a prospectus relating to non-equity transferable securities that have a denomination of at least EUR 100000 (or an equivalent amount) if the prospectus relates to an admission to trading.

32. Art. (5); and items (15, 16) of the Directive/2010. There are other materials that should be included in the summary such as statistics and expected timetable, those responsible for auditing the financial statements, capitalisation, indebtedness and risk factors, taxation, significant changes, research and development, patents and licences. For more details, see annex (I) of the directive.

33. Supra.

34. Consult the CESR on http://www.cesr-eu.org/. The regulations provide more than fifteen "building blocks" of information that must be provided in prospectuses relating to securities of different types, such as securities notes relating to derivatives, asset-backed securities or securities notes relating to debentures denominated in excess of or below 50,000 Euro. These building blocks are lists of itemised information specified in annexes. For details see I. Chiu, *Regulatory Convergence in EU Securities Regulation*, (The Netherlands: Kluwer Law International, 2008), pp.20-22.

35. The information that should be included in each document is stated in the directive's annexes II, III and IV respectively.

36. Art. (5/3). Also see art. (12).

37. Such as any significant new factor, material mistake or inaccuracy relating to the information included in the prospectus. Art. (16). Investors who have already agreed to purchase or subscribe for the securities before the supplement is published shall have the right, exercisable within a time limit which shall not be shorter than two working days after the publication of the supplement, to withdraw their acceptances. Ibid. This period may be extended by the issuer, the offeror or the person asking for the admission to trading on a regulated market as suggested by the amendment to article (16) of the prospectus directive.

38. The proposed amendment to article (16) of the prospectus directive makes clarifications about the new matter required in the supplements to include any matter that arises or is noted between the time when the prospectus is approved and the final closing of the offer to the public or the time when trading on a regulated market begins, whichever occurs earlier. Such a supplement has to be approved in the same way, within a maximum of seven working days and published in accordance with the same arrangements as were applied when the original prospectus was published.

39. Items (31 and 34) of the Directive.

40. Item (25). A study of the relationship between the amendment of the registration statement and stock price movements in the USA, found that the market reaction to the amendment of the registration

statement is negative in general, becoming more negative as the amendment is filed repeatedly, and contains non-neutral information. The findings imply that the review procedure of the U.S.A Securities and Exchange Commission (SEC), including corporate disclosure regulation, forces issuing firms to reveal unfavourable information during the new equity issuance process. See J. Chang and H. Shin, 'The SEC's Review of the Registration Statement and Stock Price Movements During the Seasoned Equity Issuance Process,' 12(4), *Pacific-Basin Finance Journal*, 12 (2004), pp.359-386.

41. Art. 2(r) defines "base prospectus" as a prospectus containing all relevant information as specified in articles 5, 7 and 16 (drawing up of the prospectus, supplement and minimum information), in cases where there is a supplement, concerning the issuer and the securities to be offered to the public or admitted to trading, and, at the choice of the issuer, the final terms of the offering.
42. Art. (5). The rationale behind such an exemption is that investors are covered by other means of protection such as deposit guarantee schemes and solvency control by competent authorities. See European Savings Banks Group, 'Position Paper on the Amended Proposal of the Commission for a Directive on the Prospectus to be Published when Securities are Offered to the Public or Admitted to Trading and Amending Directive 2001/34/EC,' DOC 865/02 (final), October 17, 2002.
43. Art. (5) of the prospectus directive..
44. L. Bertran, supra, p.45.
45. Art. 14.
46. The electronic form could be published on a) the issuer's website and, if applicable, on the website of the financial intermediaries placing or selling the securities, including paying agents; (b the website of the regulated market where the admission to trading is sought; or (c the website of the competent authority of the home Member State if the said authority has decided to offer this service. Yet, issuers who publish their prospectus in newspapers or in printed form may be required also to publish their prospectus in an electronic form as mentioned above. The directive also allows the competent authorities to require publication of a notice stating how the prospectus has been made available and where it can be obtained by the public. See art. (14).
47. Art. 6 of the prospectus directive.
48. Ibid.
49. The persons responsible for the contents of the prospectus differ from state to state. Some Member State laws only include legal persons, others also natural persons, while a third group also extends to the financial institutions involved in the issue of a security, even if they do not explicitly accept responsibility. It has been thus recommended that it should be made clear that the issuer should be primarily liable for the information contained in a prospectus. The wording of the Directive "at least" gives rise to ambiguous or different interpretations in this respect. Although it is recognised that the minimum harmonisation in this respect was intentional, the result is nevertheless detrimental for issuers. The general principle of maximum harmonisation is to be extended to the harmonisation of the liability standards applicable to a prospectus. European Securities Markets Expert Group (ESME), 'Report on Directive 2003/71/EC of the European Parliament and of the Council on the Prospectus to be Published when Securities are Offered to the Public or Admitted to Trading,' supra, 19.
50. Art. (6). See also P. Mäntysaari, The Law of Corporate Finance: General Principles and EU Law: Cash Flow, Risk, Agency, Information, (New York, London: Springer, 2009), p.458. The proposed amendment to this article also adds instances wherein the summary or any translation thereof does not provide key information that would enable investors to take informed investment decisions and to compare the securities with other investment products.
51. Judgment of the Court (First Chamber), 5 July 2007, Case C-430/05, European Court reports 2007, p. I-05835.
52. S. Griffin, p.185; and B. Ali El-Dean, p.63, supra.
53. L. Bertran, supra, pp.28-30. Suggested that the Commission's affirmation of the harmonisation of the liability standards was an aim that exceeded the prospectus directive, and thus it preferred to keep the status quo. See, 'Commission Staff Working Document accompanying the proposal for a Directive of the European Parliament and of the Council amending Directives 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading and 2004/109/EC on the

harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market,'Summary of the Impact Assessment, (Brussels, September 23, 2009). This is also the opinion of the commission of European Securities Regulators. See CESR's 'Report on the Supervisory Functioning of the Prospectus Directive and Regulation,' 28, June 2007. The European Banking Federation argues that attaching liability to the summary prospectus would run contrary to the very concept of a summary and would imply unacceptable legal risks for issuers. In addition, it suggests more amendments to the prospectus directive, such as the introduction of a light disclosure regime for capital increases and convertible bond issues. For more information see the European Banking Federation, 'Prospectus Directive - EBF comments on European Commission Amendment Proposals,' Document COM(2009) 491 final.

Chapter Four

Key Legal Adjustments for Promoting Investments in Palestinian Enterprises: What Role for the EU?

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1. Preface

This paper explores some of the main impediments in the Palestinian legal framework hindering, to some extent, potential economic cooperation between Palestine and the European Union (EU), and focuses specifically on the promotion of investment activity in Palestinian enterprises. This paper looks at the economic relationship between the EU and Palestine, as one of the EU's neighboring countries in the Mediterranean region. The main issue of this paper is the role of law in enhancing potential European investments in the Palestinian private sector, considering the current political and economic situation. The underlying assumption of this paper is that a more investor-friendly legal framework could foster foreign investment flows into Palestinian enterprises.

It must be emphasised that according to recent reports by international organisations, the main obstacles hindering foreign investments into the Occupied Palestinian Territories (OPT) remains the Israeli occupation and restrictions.[2] As long as this devastating reality exists, and continues to impose high levels of uncertainty and political risk, investments in Palestinian enterprises[3] will remain fairly limited and far from its potential.

This reality has a direct negative impact on the Palestinian economy, preventing Palestine from achieving acceptable levels of sustainable growth, business development opportunities andsatisfactory employment rates.[4] Without undermining the importance of the above obstacles, this paper attempts to assess the current Palestinian legal framework and to highlight some of the aspects that require modernisation and development.

This paper discusses aspects of economic cooperation between the EU and Palestine. Such economic cooperation can be evident in two main segments of commercial activity: trade (in goods & services) and investments.[5] In order to

promote trade, a national market should aim to achieve competitive prices, high quality products and tariff incentives. On the other hand, in order to promote foreign investments, the country must have both attractive investment opportunities and a suitable business environment, whilst at the same time providing investors with satisfactory levels of protection. The scope of this study is limited to the promotion of investments, and will not discuss trade related obstacles; although, trade issues are of high significance as well.[6]

It is worth noting that, although the title of this paper focuses on Europe's role in assisting Palestine in the promotion of investments in local enterprises, this does not suggest that there is a need for preferential treatment of European investors. Therefore, resolving the impediments in the Palestinian legal framework and business environment, as outlined in the following sections, can help to facilitate legitimate foreign investments, regardless of their origin. Nevertheless, the emphasis on the promotion of European investments derives from the relatively developed and structured nature of Palestine's relationship with the EU, as part of the EU's policy towards the Mediterranean region in general, and Palestine in particular.[7]

The remaining sections of the paper are structured as follows: Section 2 outlines the political and economic context that informs this debate; Section 3 discusses key legal issues that require some modernisation or reform to better promote foreign investments in the Palestinian private sector; Section 4 provides a historical overview of the agreements that have been made between the EU and Palestine to date, highlighting the main aspects of economic cooperation in these agreements; and Section 5 concludes the discussion set forth by this study.

2. Background

2.1. Palestinian Institutions and Economy

The Palestinian Authority (PA) was established following the signing of the Oslo Accords in 1993-1994. The OPT were divided into three different areas -A, B and C - the latter of which constituted more that 60% of the OPT, and an area of which the PA has neither civil nor security control. The Annex to the Oslo Agreement that defined the relationship between Palestine and Israel came to be known as the Paris Protocol. The mechanisms in the Paris Protocol were based on cooperative actions. However, these actions cooperative approaches were not sustained, and particularly after the second Palestinian Intifada (uprising), in 2000.[8]

Adding to the severity of the Palestinian situation was the lack of Function of the Palestinian Legislative Council in 2007. The election of Hamas party since 2007 led to an internal political division between the West Bank (WB) and Gaza. This has resulted in adivision of political control of WB and Gaza, where Fatah controls the

WB, and Hamas controls Gaza. This reality has further stunted the development of the Palestinian economy, and complicated its state building plan, of which the development of the legal frame work was part. Consequently, the legislation process has been confined to more crucial and urgent matters, and in the WB, the legislative power has remained for the last years de facto in the hands of the Palestinian President.

The Palestinian economy is a new economy. According to the Palestinian Amended Basic Law of 2003, Article 21 (1): "[t]he economic system in Palestine shall be based on the principles of a free market economy". The main economic sectors in Palestine include: agriculture (year round cultivation); industry and construction (stones and else); services and tourism (religious and else); and the ICT sector, towards which recent efforts have been directed to develop. In 2012 the services and public administration sectors constituted the highest share, more than 30%, of the GDP.[9] The Palestinian economy remains, however, under severe restrictions imposed by the Israeli occupation.These restrictions, including civil and security control by the Israelis (particularly in Area C); restrictions on movements of individuals, goods and services; restrictions on imports/exports (customs, taxes and quotas); and the control of land, water, and other natural resources, were reinforced by the Paris Protocol.[10] The occupation, lack of sovereignty and lack of border control prevent Palestine from benefiting from potential trade and economic relationships with other countries, including the EU and its neighboring Arab countries.

The development of the Palestinian private sector remains high on the national agenda, as it poses substantial potential benefits for the national economy. However, the Palestinian economy, since the establishment of the PA in the mid 1990's, has been reliant to a large extent on foreign aid to allow for the development of the local market and state building. Consequently, the decline in donors' money in the last years, mainly due to political and economic reasons, has led to noticeable contraction in the economy.[11] Currently, the Palestinian economy is facing various hardships, including declining growth rates,[12] a severe fiscal crisis[13] and high unemployment.[14] Therefore, foreign investments and technical assistance are essential for the generation of sustainable growth in the Palestinian private sector.

In terms of market structure and competitiveness, in some sectors the competition remains insufficient, particularly where there are large controlling companies and concentration in the market.[15] As more than 95% of the Palestinian enterprises are micro, small and medium size enterprises (MSMEs),[16] it is worth focusing on the needs of this sector, in terms of the enterprises' ability to obtain financing that adhere to their needs, and to develop and expand their operation both locally and internationally. These enterprises have been facing various obstacles that impede their potential development, and require improvements in terms of their access both to financial capital, and to technical assistance to developing their capacities.[17]

The Palestinian financial and banking sectors are relatively sound and well-functioning. The Palestinian capital market (the Palestine Exchange (PEX)) is supervised by the Palestine Capital Market Authority (PCMA).[18] Currently, 49 companies are listed on the PEX, and various foreign investors are also active in the public securities arena.[19] The banking sector includes seventeen commercial banks, of which nine are local[20] (supervised by the Palestine Monetary Authority (PMA)).[21] However, these financial institutions and intermediaries provide only limited financial resources to SMEs. A listing on PEX requires a minimum capital of $500k,[22] and commercial banks require high collaterals for providing credit for MSMEs, which has been repeatedly recognised as one of the main obstacles faced by MSMEs in obtaining credit.[23]

Some private investment funds (i.e. private equity and venture capital) providing equity investments for local SMEs and start-ups have, in recent years, become active in the OPT.[24] Furthermore, there have been significant developments in the Microfinance Institutions (MFIs) sector, and MFIs have also been an important source of finance for SMEs.[25]

2.2. Foreign Investments and Trade Export in Palestine

Although the above presents a relatively functioning, but deteriorating, market economy, foreign investment in the Palestinian private sector has, over the past decade, remained marginal. According to the Palestinian Central Bureau of Statistics (PCBS) reports on foreign investments in Palestinian enterprises, the highest share of the total foreign portfolio investments and foreign direct investments (FDI) in 2010 came from Jordan, with 55.7% and 80.5% respectively.[26] The remaining share of foreign investments also came mainly from Arab countries, including Qatar, UAE, Saudi Arabia, Egypt and Kuwait. Britain's share in FDIs was 0.9% in 2011, and Switzerland also had a high share in the foreign portfolio investments in Palestine of 8.6% in 2010.[27] It is also worth adding that most of these foreign investments (29.5% of which were foreign portfolio investments and 53.3% FDI) were directed into 'financial intermediation'.

Similarly, Palestinian exports remain very low. In 2012, exports from Palestine were $1,898.6 million, compared with $7,165.2 million imports.[28] The high level of imports may be explained by the need to supply the demand for material and products that are not produced locally, and for raw material for local production. A large proportion of Palestinian exports (around 84% in 2012) go to Israel, and 69.6% of the total imports come from Israel.[29]

3. Required Key Legal Adjustments

The question of how to promote foreign investments in Palestinian enterprises remains a challenging one. In order to provide investors with desired levels of protection and a healthy business environment, there should be a sound legal system and an effective dispute resolution mechanism.

According to Article 15 (1) of the Law for Investment Promotion (1998), it is the responsibility of the board of the Palestinian Investment Promotion Agency (PIPA) to attract foreign investments. Moreover, Article 15 (15) of the same Law indicates that the PIPA board is responsible for developing and modernising the investment-related legislations, and for putting together plans and programs aimed at creating a suitable investment climate.

The World Bank 'Investment Climate Assessment' report of 2007, undertook an extensive analysis of Palestinian laws, in which several deficiencies were identified.[30] While some of these deficiencies were addressed, at least partially, by the PA, the WB and Gaza were nevertheless ranked no. 135 (out of 185 countries) in 2013 by the World Bank 'Doing Business' report, indicating that several obstacles remained, and various areas still required reform.[31] Among the ten indicators in the report, the WB and Gaza were ranked above no. 100 in five (starting a business, dealing with construction permits, getting credit, trading across border, and resolving insolvency). This suggests that,in comparison with other countries, the conditions in the WB and Gaza are least favourable to "doing business."In order to improve Palestine's ranking in the 'Doing Business' report, the Palestinian Ministry of National Economy is currently working on filling these gaps through legal reforms.[32] Although 'Getting Credit' is indicated as one of the main obstacles facing businesses in Palestine, there have been several developments that present some sort of alternative to businesses for financing , including credit guarantee facilities, microfinance, and private investment funds. These remain, nevertheless, far from sufficient to fill the local demand of businesses for financing .

It has been repeatedly recognised that legal certainty and a well-functioning legal system have a positive impact on market economy, and on attracting investors. In order to promote investments in the private sector, investors need to be protected under local law and have a reliable system for resolving disputes to turn to.[33] It is not within the scope of this essay to analyse the Palestinian legal framework in all its components. Therefore, the following section focuses on elective key issues that were identified as crucial for the promotion of investments in the Palestinian private sector: (1) a business enabling legal framework, including the protection of investors under company law, bankruptcy law, and secured transactions law; (2) investment promotion, based on the Investment Promotion Law; and (3) dispute resolution mechanisms, and, in particular, arbitration. Although this paper does not treat the issue of ensuring market

competition, as a crucial factor for the development of the market economy, it does not ignore its importance.[34]

3.1. Business Enabling Legal Framework

It has been recognised that the Palestinian business legal framework has several deficiencies, resulting from several factors, including the complexity of the legal system and the outdated laws that, have not been amended for several decades, mainly due to the absence of a functioning Legislative Council.

There are two separate legal regimes in the WB and Gaza with regards to Company Law. The law currently applying in the WB is the Company Law No. 12 of 1964, amended in 2008 (the 2008 Law), although there has been a draft company law since 2010, which is pending approval by the Palestinian President.[35] In Gaza the applicable laws had always been the Company Law No. 18 of 1929, and No. 19 of 1930 (known as the Regular Companies Law), until the recent enactment of the new Company Law of 2012 that came into force in May 2013.

One of the main crucial issues that concern investors (both local and foreign) is the protection of investors' rights, and, particularly, minority shareholders' rights. This issue is dealt with to some extent in the current Company Law in the WB, although some additional improvements could certainly benefit investors. Under the current law, directors shall disclose their ownership of a company's shares (Article. 112) and are prohibited from self-dealing, unless the company issues a public tender and the director submits the best offer, which must be approved by 2/3 of the board (Article. 144). Also, shareholders can submit a derivative suit (Article. 130). The following are some of the weaknesses of the 2008 law in the WB:

a. The minimum capital requirement for private shareholding company remains high, JD 10,000 (Article 6 of 2008 Amendment).
b. There is a restriction on the share of foreign investors in local companies, as foreign investors are not allowed to have a majority share in a local company, i.e. owning a maximum of 49% of the shares.[36] This, however, does not exclude the possibility of foreign companies to register locally with the Palestinian Ministry of National Economy, i.e. the Companies Registrar.
c. There is no possibility of registering a sole shareholder company.
d. The law does not include extensive reference to restructuring procedures, or mergers between companies.

As for the new Company Law in Gaza, some criticism has been made regarding various provisions in the law. According to Article 2 of the Law, it is indicated that the law should be compliant with Islamic Law, and yet it is unclear how such a

provision should be interpreted. Additional criticisms included the limitation on the types of companies. For example, the law excludes non-profit companies and does not provide for advanced types of companies, etc. Moreover, the law increased the capital requirement to a minimum of JD 50,000- compared to JD 10,000 in the 2008 Law applying in the WB.

In addition to the modernisation of company law, a framework for secured transactions needs to be adopted, as it has been repeatedly indicated that one of the main obstacles facing Palestinian businesses in obtaining credit is the inability to provide the level of collateral required by local banks. In the current state of limited equity investments by private funds, companies that rely mainly on commercial bank loans to fund their businesses operations and growth face several challenges. Due to the absence of a registry for movable assets, those businesses mainly rely on their immovable assets for their collateral base, which are in many cases insufficient or unavailable. This, among other causes, such as political risk, results in interest rate on loans remaining high.

Finally, the modernisation of bankruptcy and restructuring law must be considered. The importance of constructing an efficient bankruptcy law has been also reiterated in Principle II of the EU 'Small Business Act', which asserts that policies should "ensure that honest entrepreneurs who have faced bankruptcy quickly get a second chance".[37] Providing an efficient and clear legal framework for resolving distressed businesses through restructuring or bankruptcy procedures can reduce the "fear of failure", which might have a negative impact on entrepreneurship and business development. This law can also provide alternative options for distressed business, which would otherwise be forced out of business when faced with distress. There is currently a draft bankruptcy law under discussion.

3.2. Investment Promotion Laws

In order to facilitate investments in the Palestinian private sector, it is important to provide businesses with adequate incentives, based on a sound national strategic plan. The Investment promotion law is the core legal act that sets forth the main incentives for attracting investment in the private sector; and being so, the Palestinian Investment Promotion Law has played an important role in structuring such incentives.

The Investment Promotion Law has undergone several phases in the last two decades. The Initial Investment Promotion Law, No. 6, was adopted in 1995 following the establishment of the PA. The law granted incentives to companies, in the form of tax exemptions, and based on either the company's capital, or its number of employees, with various thresholds.

The second Investment Promotion Law, No. (1), was adopted in 1998 (hereinafter:

'the second law'),which led to the creation of the PIPA in 2000. The second law abolished the 'number of employees' as a criterion for granting incentives, and relied on the company's capital as the only criterion, with various thresholds.[38] This second law remained in force until the end of 2011.The law granted equal incentives to foreign investors, on the basis of 'Reciprocal Treatment'.[39]

The third development was the amendment of the second law in 2011 (hereinafter: 'the 2011 Law') and included some modifications of the tax incentives. The 2011 law, which remained in force until the end of 2012, gave special attention to the Information Technology (IT) sector, where IT companies were given incentives based on their number of employees, e.g. they were favoured when employing five or more professional Palestinian employees (Article 9 of the 2011 Law).[40] However, as shown in the table below, only two IT companies received incentives through PIPA in 2012. Also, it is worth noting that companies that exported more than 30% of their production also received additional incentives (under Article 31 of the 1998 Law).

A committee has recently been appointed to draft a new law to replace the 2011 law. The committee includes representatives from PIPA and the various Ministries. The role of the committee is to advise on how the new law should be structured, taking into consideration the national economic development plan and the current economic climate, including the PA's financial crisis.

The thresholds that were granted by the 2011 Law (Article 9) granted longer periods of tax exemption for higher levels of investment in a company. As shown by the data in the table below, however, the majority of the companies that were granted these incentives had a median capital that ranged between $271,352 and $345,571 over the years 2009-2013.This suggests that SMEs do indeed constitute the majority of companies that benefited from the investment promotion law. A policy that provides tax incentives for longer periods for investments that exceed $1million, therefore, does not necessarily favour SMEs.

In my view, the investment promotion law should provide more focused incentives in particular strategic sectors, i.e. those that have inherent economic potential, such as IT, agriculture or in sectors that require high Research & Development investment.[41] Moreover, the law should give enhanced incentives to enterprises that operate in underdeveloped geographical areas, areas that have a special national significance or areas in which the risk is higher than average.

Finally, Palestinian lawmakers should ensure more certainty and long-term consistency with respect to the incentives that the investment promotion law grants, to encourage investors to initiate new enterprises based on the assumption that they are eligible for such incentives.[42]

Table: Summary of Beneficiary Enterprises of the Palestinian Investment Promotion Law- 2009-2013:

Year	2009	2010	2011	2012	2013 Q1
Number of Beneficiary Enterprises	24	28	105	68	35
Aggregated Total Capital of Beneficiaries* ($ Millions)	12,384,685	16,336,462	84,442,765	61,877,604	26,749,691
Average Capital of Beneficiary	516,029	583,445	796,631	909,965	764,277
Median Capital of Beneficiary	271,352	277,675	256,989	328,010	345,571
Beneficiaries Involving Foreign Investors	0	0	2	1	0
Beneficiaries based on Number of Employees	0	0	4	4	0
Beneficiaries Exporting Goods	0	0	1	1	2
Number of Geographical Regions	6	8	10	9	7
Tourism	1	4	24	10	4
Industry	19	21	69	47	30
Services	2	1	0	0	0
Agriculture	2	0	4	2	1
Telecommunications	1	2	6	1	0
Information Technology	0	0	0	2	0
Education	0	0	1	3	0
Health	0	0	1	3	0

* For aggregated capital, companies that were granted incentives based on their no. of employees or exports were not included, as the data on their capital was not provided.

Source: data from the Palestinian Investment Promotion Agency.

3.3. Dispute Resolution Mechanisms

The Palestinian judicial system has been characterised by several deficiencies, and mainly by the length of its trials and its lack of a sufficiently specialised judiciary. The division of the OPT into the three Areas (A, B and C) has had an adverse impact on the court proceedings, creating more causes for delays in the judicial decision-making process. In recent years, significant efforts have been made to enhance the Palestinian judicial system, by making it more efficient, and improving the professionalism of the judiciary.[43]

In the above-mentioned circumstances, it has become ever more important to find an alternative resolution system, particularly in cases of transactions involving foreign parties.[44] Arbitration is known as an attractive alternative dispute resolution mechanism. Some advantages of arbitration over the formal judicial system include: confidentiality; freedom of choice of forum and legal jurisprudence; shorter resolution periods (in general); professional and technical expertise in the field of dispute; and better chances of reconciliation.[45] Moreover, arbitration can be a more efficient medium for resolving disputes that involve both Palestinian and foreign Parties, and especially in commercial disputes.

The current law governing arbitration in Palestine is the 2000 Law of Arbitration, No. 3. This legal framework is currently being revised. The Ministry of Justice is drafting some amendments to the Law of Arbitration, which regulates the arbitration profession by imposing international standards, ensures the credibility of the arbitrators' decision-making process, and encourages the training of arbitrators. It is important that the arbitration law and procedures follow international standards in a clear manner, so as to ensure the reliability of these mechanisms.

Until recently, there had been no sign of institutional arbitration in Palestine.[46] Recently, however, there have been significant attempts to establish an arbitration centre, named the Palestinian International Arbitration Chamber (PIAC). Also, the Palestinian Prime Minister's office has recently drafted the Basic Law for the PIAC.[47]

Achieving professional arbitration decisions through an accountable and efficient process is, however, only half the battle. It is also highly important to enable an effective enforcement of such decisions through the domestic judicial system. To achieve this end, the Ministry of Justice is trying to encourage the acknowledgement of the arbitrators' decisions by the judiciary.

All the above-mentioned actions are undoubtedly crucial for fostering business activity with foreign entities, as they provide a credible setting for resolving disputes, based on accountable and internationally recognised standards.

4. European-Palestinian Agreements and Economic Relations

Palestine is part of the multilateral agreements (known as the 'Euro-Mediterranean Partnership') made between the EU and the Mediterranean countries. The Euro-Mediterranean Partnership started with the signing of what is now known as the 'Barcelona Process', whose objective was to foster economic, political and cultural cooperation between the EU and the Mediterranean countries. The 'Barcelona Declaration' included three pillars: political and security partnership; economic and financial partnership; and partnership in social, cultural and human affairs. The means that were defined for the 'economic and financial partnership' included the establishment of a free-trade area by 2010, and economic and financial cooperation.[48] As part of the implementation of the Barcelona Process, two grants and loans programs were allocated by the European Council, known as 'MEDA I' and 'MEDA II'. These programs included support for economic reform, private sector development and investment promotion. In 2004, following the Barcelona Process, the EU introduced the 'European Neighbourhood Policy', defining its relations with the neighboring countries in the East and the Mediterranean region, including the OPT, based on the "values of democracy, rule of law and respect of human rights".[49]

The EU, in 1997, following the Oslo Accords and the establishment of the PA, signed an Interim Association Agreement (AA) with the Palestinians.[50] According to Title III of the AA, in which the parties agreed to cooperate economically: "[t]he objective of cooperation will be the creation of a favourable and stable environment for investment in the West Bank and Gaza Strip [...] This will entail the development of: [...] co-investment machinery, especially for small and medium-sized enterprises (SMEs) of both Parties" (indicated in Article 39, entitled 'Investment promotion and investment'). However, this AA was never fully implemented or upgraded to a full Association Agreement. The main reason for not upgrading the AA was Israeli objection.[51]

Following the AA, the EU signed two Action Plans with the Palestine. The first Action Plan was signed in 2005.[52] In Article 2.2 of this Action Plan, entitled "Economic reform and development," Action No. 13 stressed the importance of "improv[ing] the conditions for the establishment and functioning of a market economy", including "carry[ing] out necessary legislative reform and ensur[ing] adoption and implementation of a basic regulatory framework (including: Capital Market Authority Law, amended Income Tax Law, Companies Law, Competition Law)".

Recently, a second Action Plan was drawn up.[53] In the Complementary Objective of this Action Plan, it was asserted (in Objective 61) to "improve the economic

environment in order to promote domestic investment and attract foreign investment in the occupied Palestinian territory, notably in East Jerusalem, Area C and the Gaza Strip".

Moreover, the EU has laid down some common principles for enterprise policy, known as the 'Euro-Mediterranean Charter for Enterprise' (hereinafter: 'the Charter').[54] The Charter contains *ten* common principles that the Mediterranean partners to the EU should implement in their policies.[55] Furthermore, there are currently efforts being made to implement the 'European Small Business Act'.

The EU is a major supporter of the Palestinian people in terms of the aid and support that it provides the PA. The total aid received from the EU in 2012 was $212.3 million, mostly for paying public officials' salaries, pensions and security expenditures.[56] It is unclear to what extent this aid had a positive impact on governance.[57] However, the EU trade relations with Palestine and investments in Palestinian enterprises remain low. In terms of trade, although the EU has been considered a strategic partner to the Palestinians, trade with the EU remains marginal: as 2012 figures show, around 96% of the Palestinian exports go to Israel (84%) and the Arab world (12%), and the remaining 4% goes to the rest of the world.

The EU has been providing support to the Palestinians for the promotion of the private sector. However, the assistance and cooperation of the EU in this respect has been relatively low compared to other examples of European assistance to Palestine.[58] One of the major European investment channels to the OPT is managed by the European Investment Bank (EIB), within the Facility for Euro-Mediterranean Investment Partnership (FEMIP). The objective of the FEMIP program is to support the country in economic recovery and restructuring. Since 1995, the EIB has channeled around Euro 116 million for projects in the OPT in the form of loans, private equity and technical assistance. However, the total FEMIP investments in the WB and Gaza, between the years 2002-2012, were only Euro 60 million (Euro 45 million for energy projects and Euro 15 million for private equity). This makes Palestine the country with by far the lowest total investments of all the Mediterranean countries included within the FEMIP program. Also, when compared with investments in other countries, investment in Palestine is marginal.[59] Jordan, by comparison received Euro 449 million, Lebanon Euro 740 million, and Israel Euro 792 million in investment.

Without undermining the involvement and assistance of the EU to Palestine throughout the past decades, the role of the EU in this context should be bolstered, both in terms of the more active role that it should take in the legal reform process and the level of investment allocations that it should provide to the Palestinian private sector. Such an active involvement is in line with the EU

policy in the region, and the agreements that have been made with Palestinians. Moreover, without fostering a real productive private-sector market led economy, all the efforts to build a Palestinian state will be futile.

5. Concluding Remarks

This paper examined key legal issues in the Palestinian legal framework that were identified as crucial for the promotion of investments in Palestinian enterprises. It suggested that more emphasis made on modernising the legal framework with respect to business-friendly laws, investor protection, legal incentives for investments in businesses and efficient dispute resolution mechanism. There are currently legislations under discussion and consideration in all of these areas, and it is very important that these legislative actions proceed and provide investors with legal certainty and more efficient and modern laws. In this context, the role of the EU should be enhanced, both in terms of a more active role in the legal reform process and the investment allocations that are made by the EU to the Palestinian private sector.

1. The author would like to thank the organizers of the symposium from the Institute of Law at Birzeit University and the participants of the symposium for their discussions on this paper. The author would like also to thank various officials that provided valuable infomation for this paper, from the Palestinian Ministry of Justice, the Palestinian Ministry of National Economy, the Palestinian Investment Promotion Agency, the Palestine Monetary Authority, and last but not least, the Palestine Economic Policy Research Institute (MAS). I am responsible for any errors or anomalies in the article.

2. In a recent report, the World Bank emphasised that "restrictions put in place by the Government of Israel (GoI) continue to stand in the way of potential private investment and remain the major impediment to sustainable economic growth" (the World Bank (2012), 'Fiscal Crisis, Economic Prospects: The Imperative for Economic Cohesion in the Palestinian Territories, Economic Monitoring Report to the Ad Hoc Liaison Committee,' available at: http://siteresources.worldbank.org/INTWESTBANKGAZA/Resources/AHLCReportFinal.pdf, p. 4. Also, in the UNCTAD (2012), "Report on UNCTAD assistance to the Palestinian people: Developments in the economy of the occupied Palestinian territories," p. 10-12, available at:http://reliefweb.int/sites/reliefweb.int/files/resources/tdb59d2_en.pdf, it was asserted that "[t]he key obstacles facing the Palestinian economy are all related to occupation". Many of the restrictions on the movement of goods, foreign trade and business activity stem from the economic agreement between the Palestinians and Israel, Protocol Paris, and unless this agreement is amended many of the current constrains will remain prevalent. See also See the World Bank (2012), 'Towards Economic Sustainability of a Future Palestinian State: Promoting Private Sector-Led Growth', available at: http://siteresources.worldbank.org/INTWESTBANKGAZA/Resources/GrowthStudyEng.pdf, p. 20-21; and Paltrade (2010), 'Investment in Palestine: The Reality', pp. 9-15, available at: http://www.paltrade.org/cms/images/enpublications/Investment%20in%20Palestine%20-%20The%20Reality.pdf.

3. Political risk has been identified in the literature as one of the main obstacle limiting foreign investments. Also, in the Global Entrepreneur Monitor (GEM) 2013) 'Political, Institutional and Social Context', it was been identified as the first key factor constraining entrepreneurship, see Palestine Economic Policy Research Institute (MAS), 2013, 'Palestine Country Report 2012' - The Global Entrepreneur Monitor (GEM), p. 22.

4. "[T]he sustainability of growth in the Palestinian territories depends upon increasing private investment." The World Bank (2012), 'Fiscal Crisis, Economic Prospects: The Imperative for Economic Cohesion in the Palestinian Territories, Economic Monitoring Report to the Ad Hoc Liaison Committee', available at: http://siteresources.worldbank.org/INTWESTBANKGAZA/Resources/AHLCReportFinal.pdf, p. 4.

5. In addition to trade and investment, aid and technical assistance are other major components of economic assistance. It is, however, directed more to the public sector, which still has an indirect impact on the economic development of the private sector. For additional information on EU aid to the Palestinians, see section four.

6. With respect to the enhancement of trade, many efforts have been made in recent years to improve the Palestinian private sector trade and export capacity. See, for example, a project funded by the EU, 'Trade, competitiveness and private-sector development programme', available at: http://eeas.europa.eu/delegations/westbank/projects/list_of_projects/268587_en.htm. In addition, efforts have been made to prepare the Palestinian State for joining the WTO. See for instance, the Palestine Economic Policy Research Institute (MAS) Roundtable No. 6, 2012, 'Palestine and the WTO', available at: http://www.mas.ps/2012/sites/default/files/Round%20Table%206-%20Trade%20WTO.pdf.

7. Palestine has signed several trade related agreements with various countries including Arab countries, e.g. Egypt and Jordan, the US, Turkey and elsewhere. The list of agreements is available at the website of the Palestinian Ministry of National Economy, at: http://www.mne.gov.ps/agreements.aspx?lng=1&tabindex=100&m=0. See also, Birzeit University- Institute of Law (2009), 'The Palestinian Business Law Guide', pp. 464- 467.

8. See Konrad-Adenauer-Stiftung (2012), 'The Paris Protocol- Historical Classification', available at: http://www.kas.de/palaestinensische-gebiete/en/pages/11895/ .

9. The Palestinian Amended Basic Law of 2003 is available at: http://www.palestinianbasiclaw.org/basic-law/2003-amended-basic-law. On the main economic sectors in Palestine, see the Palestinian Central Bureau of Statistics (2013), Palestine in Figures 2012, p. 42, available at: http://www.pcbs.gov.ps/Portals/_PCBS/Downloads/book1967.pdf.

   According to the Palestinian Amended Basic Law of 2003, Article 21 (1): 'The economic system in Palestine shall be based on the principles of a free market economy', available at: http://www.palestinianbasiclaw.org/basic-law/2003-amended-basic-law. The main economic sectors in Palestine remain: the agriculture

(year round cultivation), industry and construction, services and tourism (religious and other), and recent efforts have been directed towards the development of the ICT sector. The services and public administration sectors constitutes the highest share of the GDP, more than 30% in 2012, see the PCBS (2013), supra note 9.

10. On the severe negative impacts of the Israeli occupation in the OPT, see supra note 2. See also the Palestinian Ministry for National Economy and the Applied Research Institute - Jerusalem (ARIJ) (2011), 'The Economic Costs of the Israeli Occupation for the Occupied Palestinian Territory,' available at: http://www.mne.gov.ps/pdf/EconmiccostsofoccupationforPalestine.pdf. For a brief historical overview of the Palestinian economy before and after the Oslo Accord, see Birzeit University - Institute of Law (2009), supra note 7, pp. 71-76.

11. The World Bank (2013), 'Fiscal Challenges and Long Term Economic Costs,' pp. 1-2.

12. In recent years, according to the Palestinian Central Bureau of Statistics (PCBS), the GDP growth rate in Palestine has declined from 9.3% 2010, to 8.7 % 2011 and 5.9% in 2012, see the PCBS (2013), supra note 9, p. 8.

13. See the Palestine Economic Policy Research Institute (MAS), 'Roundtable No. 5 (2011): Financial Crisis of the Palestinian National Authority,' p. 10, available at: http://www.mas.ps/2012/sites/default/files/round5.pdf. See also, World Bank (2013), supra note 11, p. 6-11.

14. Total unemployment rates in 2012 were 23%: WB 19%, Gaza 31%, see the PCBS (2013), supra note 9, p. 8.

15. Currently, there is a draft competition law pending approval by the Palestinian president and efforts are being made to establish a Competition Commission as well, see FirasMilhem (2012), 'Towards Establishing the Palestinian Competition Commission,' the Palestine Economic Policy Research Institute (MAS), executive summary is available at: http://www.mas.ps/2012/sites/default/files/Ex%20Sum%20Competition%20.pdf.

16. MSMEs are the backbone of the Palestinian economy, and their share in the economy is very high: more than 90% of local businesses are MSMEs. See Khaled Zeidan (2012), 'Investment Opportunities for Small and Medium Enterprises [SMEs] in the Palestinian Transportation Sector,' the Palestine Economic Policy Research Institute (MAS), p. 9.

17. According to the report on the 'Ease of Doing Business,' the ranking of the Palestinian Territories remains unsatisfactory, no. 131 out of 183 in 2012 and 128 in 2011, World Bank (2012), The World Bank (2013), 'Doing Business 2013 - Smarter Regulation for Small and Medium-Size Enterprises, 10thedn, available at: http://www.doingbusiness.org/~/media/GIAWB/Doing%20Business/Documents/Annual-Reports/English/DB13-full-report.pdf". The main difficulties include: starting a business, getting credit, trading across borders, and resolving insolvency. It must be noted that these reports have been subject to much criticism, and therefore, this note is only meant to point out the main problematic points of the Palestinian system.

18. See www.pcma.ps.

19. See www.pex.ps.

20. On the number of banks in Palestine, see http://www.pma.ps/index.php?option=com_content&view=article&id=78&Itemid=94&lang=en. So far, no incident of defaulting bank has occurred in Palestine, and the Palestinian banking system has managed to prevent local repercussions of the global financial crisis. See International Monetary Fund (2013), 'Recent Experience and Prospects of the Economy of the West Bank and Gaza,' available at: http://www.imf.org/external/country/WBG/RR/2013/031913.pdf. See also, PMA (2013), 'Palestinian Banks Weather Crisis But Govt Debt is Threat,' press release 23.1.13, available at: http://www.pma.ps/index.php?option=com_content&view=article&id=336%3Apalestinian-banks-weather-crisis-but-govt-debt-is-threat&catid=37%3Apma-in-news&Itemid=164&lang=en.

21. For an overview of the Palestinian capital market and banking laws, see the websites of the PCMA and PMA, supra notes 18 and 19 above; see also Birzeit University- Institute of Law (2009), supra note 7, pp. 243-289.

22. See listing rules on PEX, available (in Arabic) at: http://www.pex.ps/psewebsite/publications/PEX%20Listing%20Regulation.pdf

23. Collateral requirements recognised as the main obstacle faced by companies seeking bank lending. See World Bank (2012), supra note 2, p. 2.

24. See the Palestine Economic Policy Research Institute (MAS), 'Roundtable No. 8 (2012): The Palestinian

Private Investment Funds: Challenges and Opportunities', p. 10, available at: http://www.mas.ps/2012/sites/default/files/Round%20Table%208-%20Investment%20Funds.pdf.

25. The MFIs sector has been put under regulatory and supervisory scrutiny of the PMA, as new legal framework governing the MFIs establishment and operation, including a minimum capital requirement of $5 million, has been enacted. See Abdelkarim, Naser et al. (2013), 'The Economic Role of the Microfinance Institutions and their Impact on the Financial Stability in Palestine'.

26. OECD (2008), OECD Benchmark Definition for Foreign Direct Investment, 4th edn, 2008, available at: http://www.oecd.org/fr/daf/investissementinternational/statistiquesetanalysesdelinvestissement/oecdbenchmarkdefinitionofforeigndirectinvestment-4thedition.htm.

27. Data available on the PCBS website: http://www.pcbs.gov.ps/pcbs_2012/Publications.aspx.

28. Data available on the PCBS website: http://www.pcbs.gov.ps/Portals/_Rainbow/Documents/HTML-BopTabl-Q1-2013-arab.htm.

29. PCBS (2013), supra note 9, pp. 44-45.

30. The World Bank (2007), 'West Bank and Gaza Investment Climate Assessment: Unlocking the Potential of the Private Sector', p. 34, available at: http://siteresources.worldbank.org/INTWESTBANKGAZA/Resources/294264-1166008938288/ICA2007.pdf. See also, Al-Mustakbal (2006), 'Developing a Palestinian Roadmap for Legislative Reform in the Business Sector', pp. 58-64, available at: http://www.almustakbal.org/publications/Palestinian%20Legis%20Roadmap%20English%20Final%20March%2007.pdf. In addition, all the proposed amendment of the commercial laws are found on the website of the Palestinian Ministry of National Economy, at: http://www.mne.gov.ps/laws.aspx?lng=2&itemid=1&tabindex=100&m=0.

31. "'The Euro-Mediterranean Charter for Enterprise', available at: http://ec.europa.eu/enterprise/policies/international/files/charter_11_dimensions_en.pdf.

32. US AID supports the Ministry of National Economy with this reform plan through the 'Investment Climate Improvement' project. See http://www.wbg-ici.com/pro/docs/Snapshot%20CTT.pdf

33. The World Bank (2012), supra note 2, pp. 105-106. See also FirasMilhem (2010), 'Improving Palestinian Investment Legislation to the Advantage of SMEs', the Palestine Economic Policy Research Institute (Arabic), pp. 53-69, available at: http://www.mas.ps/2012/node/56#.UerdCkJu9UQ.

34. Additional legal topics of significance such as intellectual property and electronic signature are not discussed in this paper.

35. All draft commercial laws that are under discussion are available on the website of the Palestinian Ministry of National Economy (in Arabic): http://www.mne.gov.ps/laws.aspx?lng=2&itemid=1&tabindex=100&m=0.

36. Palestinians holding foreign passports may request an exemption in certain cases so as to avoid this restriction on owning a majority stake in a local company.

37. The Charter, supra note 35.

38. The thresholds were as follows: Tax exemption for 7 years for companies with capital between $100k-$1m, 9 years for companies with capital between $1m-$5m, and 11 years for companies with capital more than $5m (Article 9 of the 2011 Law)

39. Article 5 of the second Investment Promotion Law.

40. IT companies included companies that focused on programme development and not on trade in hardware.

41. IMF (10.7.13), 'IMF Urges the Palestinian Authority and Donors to Reassess Priorities', available at: http://www.imf.org/external/country/WBG/RR/2013/071013.pdf.

42. Due to the PA financial crisis in 2012, income tax exemptions were suspended for 13 companies for two years. See the Palestine Economic Policy Research Institute (MAS) (2013), 'Quarterly - Economic and Social Monitor', Vol 32, May 2013, available at: http://www.mas.ps/2012/sites/default/files/Monitor%2032English.pdf.

43. See The Palestinian National Authority (2011), 'National Development Plan 2011-2013: Establishing the State, Building Our Future', available at: http://www.apis.ps/up/1332062906.pdf, pp. 27-28. See also, the 'Seyada' project that has been aimed at modernising the judicial system since 2008, www.lacs.ps/documentsShow.aspx?ATT_ID=3714; and 'Seyada II' project supported by the EU, http://eeas.europa.eu/

delegations/westbank/projects/list_of_projects/215524_en.htm.

44. For a detailed description of the available alternative dispute resolution mechanisms in Palestine, see Birzeit University- Institute of Law (2009), supra note 7, pp. 110-126.

45. For an overview of the general advantages of alternative dispute resolution systems, see Birzeit University - Institute of Law (2009), supra note 7, pp. 114-115, and p. 110: "[t]he continued development in commerce and services has resulted in increased complexity of transactions, a need for speed and efficacy in settling disputes, and a need for specialization by those who examine these disputes or participate in their resolution. Thus, a need has grown for parties to have access to legal methods through which they can resolve disputes in a quick, just, and efficient manner which would grant them flexibility and freedom not usually found in the court system."

46. Currently there is no organization that provides institutional arbitration services. However, Chambers of Commerce in the various Palestinian regions provide arbitration services, based on Article 18 of the Ministers Council, No. 39, of 2004.

47. A copy obtained from the Palestinian Ministry of National Economy, with the author.

48. The Barcelona Declaration is available at: http://trade.ec.europa.eu/doclib/docs/2005/july/tradoc_124236.pdf.

49. The EU Neighbourhood Policy is available at: http://ec.europa.eu/world/enp/index_en.htm.

50. Available at: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:21997A0716(01):EN:HTML.

51. The Israeli objection was that the "EA-EU agreement [was] a breach of Article IX of Oslo II". See Kanafani, Numan (2000). 'Associating Palestine with the European Union', the Palestine Economic Policy Research Institute (MAS), p. 22.

52. Available at: http://ec.europa.eu/world/enp/pdf/action_plans/pa_enp_ap_final_en.pdf.

53. A copy of the Action Plan of 2013 was obtained from the EU Delegation office in Jerusalem. See, EU press release from 24.10.12, that the negotiations on a new Action Plan were concluded, see http://europa.eu/rapid/press-release_IP-12-1155_en.htm?locale=en.

54. "The Charter, supra note 37"

55. The tencommon principles of the charter are as follows: 1. Simple procedures for enterprises; 2. Education and training for entrepreneurship; 3. Improved skills; 4. Easier access to finance and investment-friendly taxation; 5. Better market access; 6. Innovative companies; 7. Strong business associations; 8. Quality business support schemes and services; 9. Strengthening Euro-Mediterranean networks and partnerships; and 10. Clear and targeted information, available at: http://ec.europa.eu/enterprise/policies/international/files/charter_11_dimensions_en.pdf.

56. Data obtained from the Palestinian Ministry of Finance, http://www.pmof.ps.

57. In their recent paper, Ayadi, R. and S. Gadi, indicate that due to "the low levels of funding committed for democracy promotion, development of civil society and promotion of government accountability. Instead, the EU's assistance in this area has revolved around security cooperation, including counter-terrorism, tackling illegal migration and neutralizing weapons of mass destruction in Libya and Syria". See (AyadiRym&SalimGadi (2013), 'The Euro-Mediterranean Partnership and Development Assistance: Past Trends and Future Scenarios', MEDPRO Technical Report No. 32, available at: http://www.ceps.eu/book/euro-mediterranean-partnership-and-development-assistance-past-trends-and-future-scenarios.

58. No aggregated data on European investments flows into the Palestinian private sector was found. In the data from the PCBS on foreign investments, referred to in section two, aside from the Arab countries, there was a category defined as the 'rest of the countries' (in which the EU is probably included). The share of this category in foreign portfolio investments and FDI in Palestinian enterprises were 15.1% and 5% in 2010, and 11.3% and 3.5% in 2011, respectively. No further specification is provided.

59. Data is published by the EIB in the FEMIP 2012 Annual Report, p. 18, available at: http://www.eib.org/attachments/country/femip_annual_report_2012_en.pdf.

Chapter Five

The Objectives of Competition Law: Lessons from the EU for Palestine

The Objectives of Competition Law: Lessons from the EU for Palestine*

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Introduction

As other laws, competition lawseeks to achieve particular objectives. The objective(s) of competition policyare derived from the objective(s) of a wider economic policy. Consequently, the objectives of the competition law must express the needs and requirements of the economy. Reviewing the EU's competition policy shows that the objectives of the competition policy have changed according to itsvarious political and economic situations. The competition policy has sought to achieve such economic objectives as productive efficiency, allocative efficiency and dynamic efficiency. In addition, it has sought to achieve such non-economic objectives as: consumer protection; protection of small and medium firms; and the promotion of European political and economicintegration. Consumer protection has been an integral part of European competition policy as an end-objective in the adoption of competition policy. The objective(s) of the European competition policy are referred to in order to assess anticompetitive practices including restrictive agreements, abuse of dominant positions and anticompetitive mergers of economic firms.

The Palestinian draft law of competition has not clarified its objectives expressly in its texts. However, the Explanatory Note of the draft law does provide several objectives, including: protecting market factors (consumer, traders, and small businesses);creating a healthy investment environment to attract foreign investors; promoting competition between local products in local and international markets; and realising the economic potential of the market. Nonetheless, the mentioned objectives contradict with each other as explained below.

Competition law is a branch of the law that regulates anticompetitive practices, such as restrictive agreements or arrangements, the abuse of dominant positions in the market and anticompetitive mergers.[1] Jurisdictions worldwide adopt competition laws as part of the regulation of their respective economic

policies, and thus, the objectives of this law differ from one jurisdiction to another.Jurisdictions do, however, share some similarities in this regard.[2]The Palestinian Authority is currently seeking to adopt a competition law, known as the Palestinian draft law of competition. This paper attempts to shed light on the objectives of this draft law through a comparison with Europe's experience of this process. This article explains firstly the importance of regulating the objectives of competition law; it then goes on to discuss the objectives of competition law in the EU; and finally approaches the objectives of the Palestinian draft law.

The importance of regulating the objectives of competition law

Assessing abusive practices is likely to be challenging for several reasons. One such reason is the similarity of the effects of anticompetitive and procompetitive practices on markets; both effective and exclusionary competitions force weak firms to leave markets.[3] For such considerations, competition authorities assess alleged abusive practices on a case-by-case basis.[4] To fill the gap, European Courts have devised several leading and guiding principles, among which is the objective of the law.[5] As competition law is a part of regulatory framework of any economic policy, the economic policy adopted by a country decides its own competition law objective(s). The objective(s) of such law play(s) a key role in distinguishing lawful practices from unlawful ones. Adoption of a particular objective dictates that the same practice might be legal under particular provisions and illegal under provisions adopted by another country. In light of such circumstances, it is essential that the objectives of competition law be regulated. Competition law must be accurate, and the objectives adopted clear and precise. In this way, the objectives of the competition law must agree with the objectivesof the economic policy.

The objectives of European competition law

The objectives of European competition rules have changed in accordance with the economic and political developments within the European Union. The European competition policy and rules have been employed as important tools in supporting European political and economic integration of the last century. Generally, the objectives of European competition rules fluctuate between two main categories: economic and noneconomic objectives.

1. Economic objective of European competition law

Most jurisdictions, including the EU's competition policy, recognise the economic objective in their competition policy as one of its most prominent objectives.[6]

Economic objectives have played an essential role in the last few decades, and have become the most prominent objectives of competition policy.[7]Some observers have pointed out that competition law is concerned fundamentally with the economic consequences of players' actions in the market.[8]In the2003 OECD (Organisation for Economic Co-operation and Development) survey in the affiliated countries, economic efficiency, after protection, appeared as the core objective of competition in those countries.[9] In addition, competition is seen as an important tool for solving economic dilemmas. However, competition cannot solve such dilemmas alone, even when the competition in the market operates perfectly.[10] The economic objective of competition policy is represented by its"economic efficiency".[11] Economic efficiency encompasses the following types of efficiency: productive efficiency, allocative efficiency and dynamic efficiency.[12]

a) Productive efficiency

Economic productive efficiency is realisedwhen the firm has the lowest possible costs through employing the most effective combination of resources in the production process. This level of productive efficiency reflects the amount consumed by society, wealth and the scarcity of resources.[13]The highest level of productive efficiency is realised when competition in the market is high. At this point, the marginal cost of production is equal to the price of the goods produced. The greater the competition in the market is, therefore, the greater the productive efficiency.[14]The reason for thisis that, under pressure from its market competitors, a given producer seeks to produce at the lowest possible cost so it can sell its product at a competitive price. By comparison, in a monopolised market, a producer is not under pressure from its rivals (as it tends to have none, or few), and thus no incentive to produce at the lowest possible cost; it sells its products at whatever price it determines.[15]

b) Allocative efficiency

Allocative efficiency or Pareto *efficiency* is achieved when the price of a given product reflects the cost of the product.[16] That is, the price equals the marginal cost of a given product.[17] Naturally, a firm produces in order to gain maximum profits. For this reason, a producer continues to produce as long it is profitable, or where the marginal cost (including profit) is less than or equal to the market price.[18] Resources must be allocated efficiently to the highest possible level, that is, the producer will continue to produce as long as the consumer demands that product. Thereafter, the producer will suspend producing (because producing extra units of the product would lead to 100% loss). In other words it

is the consumer demand alone that dictates when the provider must produce. However, any suspension of productiondoes not create a problem in terms of consumer demand of consumers,as other producers will compensate the shortage in demand.[19]When the market is monopolised, however,suspending production can create a problem. Nevertheless, in such case, the monopolist can limit production freely to gain high profits since demand would be greater than supply. Thus, monopoly prices are likely to be higher than the marginal cost, and thereforeresources are allocated inefficiently as consumers pay more than the real value of the product.[20]

c) Dynamic efficiency

Dynamic efficiency is achieved when a given supplier (producer), as a result of the pressures of market competition, strives to develop its products through innovations in scientific research and technology in order to satisfy consumer desires on the one hand and to maximise its profits on the other. The monopolist also innovates, uses technology, and conducts a scientific research to develop it products, of course.What, therefore, is the difference between the two cases of monopoly and competition in this context? Well, the achievement of continued dynamic efficiency requires both the ability and the incentive to innovate. In the absence of competitive market forces and the resultant pressure on the producer to achieve dynamic efficiency, the monopolist has the ability to innovate and develop its products,[21] but not necessarily the incentive to do so.[22]

2. Non-economic objectives of competition law

Despite their importance, economic objectives are not the only objectives in competition law; jurisdictions worldwide seek to achieve other objectives by adopting competition law. Competition law, for example, aims to redistribute wealth in a country by preventing big firms from excluding rivals from the market. In other jurisdictions, competition law aims to increase employment rates through adopting openness and liberalisation policies, and in other cases, the law aims to protect consumers.[23]

a) Consumer protection

Competition law might concentrate on protection and the interests of consumers as a priority in condemning anticompetitive practices.[24] Adoption of consumer interests as a main objective of competition policy can even lead to changes in how the law is applied by competition authorities, and where they lay their priorities.[25] Consumer interests have been a key consideration of European competition policy. For example, paragraph 3 of article 101 of

the Treaty on the Functioning of the European Union (TFEU) provides an exemption for the prohibition laid down in paragraph 1 of the same article, where consumer interest has been taken into account and prioritised.[26]The European Commission fights severely against cartels since such violationsare seen as the most dangerous infringement on the consumer interests rules.[27] In addition, the European Commission directly mentions consumer interests as a goal, and indirectly stresses their importance by focusing on the protectionof competition in markets.[28]

We might ask what is meant by the term "consumer,"i.e. does it refer to the customer, or the end user? The European Commission adoptsa wide sense of the term, and they refer toconsumersas all the customers in the market place including the end users.[29] Nonetheless, consumer interests might be measured either by consumer welfare[30] or total welfare in the market[31]. Consumer welfare refers to consumer surplus, which is the difference between the social valuation of product and the price actually paid by theconsumer (the price of a given product is less than the price final consumers are willing to pay).[32] The total welfare (known also as social welfare) is the combination of producer welfare[33] andconsumer welfare.[34] Competition authorities might refer to total welfare[35] or consumer welfare as a standard by which they can assess market competition. In practice, if competition policy is determined by consumer welfare rather than total welfare, competition authorities would take into account the effect of the alleged practice by measuring the benefits transmitted from consumer surplus to producer surplus, and vice versa. Thus, unreasonable increases in price will be prohibited since consumer benefits go to the producer. On the other hand, if the competition policy targets total welfare, then competition authorities assess any alleged practice according to the benefits obtained by the producer and the consumer collectively.[36]

b) Protection of small and medium-sized firms

It is understood that the protection of small and medium-sized firms, particularly in infant industries, must be acknowledged in order to establish healthy competition in the market, especially in emerging economies and new competition polices. The more effective the enterprises in the marketplace are, the higher the level of competition will be in that market. The existence of several firms in the market leads to innovation and maintains equal opportunities for players in that market.[37] Some jurisdictions, such as the US antitrust policy, do not consider this objective.[38]

The European competition policy gives some attention to the protection of small and medium-sized firms. It is believed that the protection of such businesses leads to the competitiveness process being enhanced[39] European policy makes not of this objective inthe European Commission Notice on Agreements of Minor Importance.[40] Accordingly, arrangements and agreements reached by small and medium firms are exempted from falling in the scope of prohibited agreements pursuant to paragraph 1 of article 101 TFEU Treaty.[41]

3. Other objectives

The above-mentioned objectives are mere examples; competition policy through the law might seek to achieve other objectives. For example, in some jurisdictions, especially in developing countries and emerging economies, competition laws seek to promote investment for the sake of enhancing economic growth by attracting foreign investment. Such laws also seek to fight against poverty and increase employment rates.[42]

In the EU, competition has been seen to be a vital instrument in achieving political objectives, especially in the early years of the European Economic Community.[43] The political objective has become integral to European policy.[44] European treatiesconcentrate European integration, in which competition is an important tool of support.[45] The importance of competition in this regard appears through the abolishment of any barriers between Member States by prohibiting boundaries being made by public or private undertakings.[46] The EU has also used competition as an instrument to overcome financial and sovereign debt crises. In this regard, the Vice-President of the European Commission responsible for Competition Policy, Joaquin Almunia, addressed the need to face financial crises by adopting suitable policies towards competition, namely the merger policy.[47]Furthermore, the European Commission relies on competition to achieve the objective of the European Union of 'Europe 2020 strategy' aiming at supporting growth, creating more jobs, and realising the competitiveness of the EU economy.[48]

The objectives of the Palestinian Draft Law of Competition:

The above discussion shows that there is an endless list of objectives of competition law and policy (political and economic integration, freedom of competition, efficiency, consumer or social welfare, protection of small and medium-sized undertaking and solving financial crises).[49] Furthermore, the objectives of the policy are changeable even in the same jurisdiction according to the situation of the economy and the passage of time.

The adoption of several objectives and the changeable nature of competition policy objectives lead, therefore, to decreased legal certainty and a misleading assessing of anticompetitive practices, especially and most importantly where these objectives are inconsistent. For example, adopting the protection of 'small and medium-sized undertakings' as an objectivewill likely harm consumer interests.[50]

The Palestinian draft law has not regulated the objectives of the competition policy. Nevertheless, the draft law has adopted some objectives indirectly, such as the protection of small and medium-sized firms. The draft has dealt with the protection of small and medium-sized firms as a tool in the establishment of a competitive environment. It has adopted this implicitly as it has exempted mergers where the market share of merging companies is lower than 10%.[51]

The Explanatory Note attached to the draft law has also been adopted. Accordingly, the law aims to achieve the following objectives: protecting market factors (consumer, tradersand small businesses); creating a healthy investment environment to attract foreign investors; promoting competitiveness of local products in local and international markets; and realisingthe economic efficiency of the market.

The above-mentioned stance of the Palestinian legislature can beencriticised for several reasons. Firstly, the draft law has not adopted particular objective(s), and instead the objectives have been provided by the Explanatory Note, which is not binding. Secondly, the objectives laid down in Explanatory Note contradict each other.For example, the objective of protecting the consumer contradicts the objective of protecting competitors in specific cases, such as predatory pricing. Because adopting contradicted objectives confuses the assessment of anticompetitive practices, legislature should only provide one end-objective of the Palestinian competition policy, that is, long-term consumer interests. This objective can berealisedby protecting market competition rather than the competitors themselves. Market competitiveness is realisedby encouraging competitors to achieve economic efficiency. Thus, any alleged practice is procompetitive as long as it leads to realise efficiency. Thirdly, despitethe clear importance of consumer interests in the European context, Palestinian draft law has not regulated this objective of competition law, and this must be reconsidered in the draft law.

For the above-mentioned reasons, competition policy-makers should define the objective(s) of competition law at the political level in the actual text of the law. Furthermore, the objective must be cited in the law itself in order to clarify the priorities of a competition authority during the enforcement phase in the future. The objective must be an end-objective, and clear enough to lead any

assessment of abusive practices to the right results. The paper proposes the protection of the consumer as an end objective through the maintenance of acute competition in markets. Accordingly, acute competition is found as long as alleged abusive practices lead to economic efficiency.

The researcher points out that policy makers should take into account: first, the necessity to define the objectives of competition law at the political level;[52] second, the vitality to only include direct objectives during the selection process; third, the necessity to distinguish between the end objectives and the means of achieving them (for example, total welfare is an objective, while protection of freedom to operate in the market is a means to achievingit);[53] andfourth, the importance of taking into account the overlap between competition policies and other relevant policies, such as consumer policy. Accordingly, the focal point of competition law should be effective competition in the market while a concentration of consumer policy should be the protection of the consumer.[54]

Conclusion

The study has also shown that there are endless objectives sought through adopting competition law. Those objectives differ from one jurisdiction to another. Objectives may be categorised into economic and non-economic ones. The economic objective is represented by economic efficiency, which is dominant and widely adopted. However, the non-economic objectives are various and derived from the domestic needs of each country. A non-economic objective might be a political objective, for example, competition policy in the EU aimed (at least at the time of erecting the European community) to enhance the integration of the internal market of the EU. In some cases, the objective is social. For example, Palestinian draft law of competition considers protecting small and medium-sized firms from big ones. Despite the importance of defining the objectives of the law as guidance to competent authorities and courts, it should be noted that the European competition law and the Palestinian Draft Law have avoided explicitly expressing objectives of the competition policy. However, the European courts have bridged the legislative gap (ambiguity of the objectives) during their practice the last sixty years. Bridging such a gap by the Palestinian courts would be very far-reaching, as the courts have not experienced such matters yet. Therefore, the proper way to solve such a dilemma would be legislative.

Notes

* This paper is a part of the author's doctoral dissertation submitted at the Free University of Brussels in 2013.

1. J. Law and E. A. Martin, *Black's Law Dictionary*, 7thedn (Oxford: Oxford University Press, 2009). See (in Arabic) Y. Al-Hadedi, *The Legal System for the Franchising in the Economic and Legal Thought* (Manshaet Al-Maaref: Alexandria, 2007), p.319, p.320.

2. See UNCTAD, *Model Law on Competition: Substantive Possible Elements for a Competition* (UNCTAD, Geneva 2004) 1. See also R. Van den Bergh, P. Camesasca: *European Competition Law and Economics: a Comparative Perspective* (Intersentia: Hart; Antwerpen: Groningen, Oxford, 2001) p.1. See also M. M. Dabbah, *International and Comparative Competition Law* (Cambridge: Cambridge University Press, 2010), p.17. See E. Buttigieg, *Competition Law: Safeguarding the Consumer Interest: A Comparative Analysis of US Antitrust Law and EC Competition Law* (Netherlands: Kluwer Law International, 2009) 1. See also R. Bork, *The Antitrust Paradox: A Policy at War with itself* (New York: Basic Books, 1978), p.50. See K. Maskus and M. Lahouel, "Competition Policy and Intellectual Property Rights in Developing Countries" *The World Economy* 23 (2000): 595-611 (p.595, p.598).

3. See R. Whish, *Competition Law* 6thedn, (Oxford: Oxford University Press, 2009), p.201. See also J. T. Lang & R. O'Donghue, 'The Concept of an Exclusionary Abuse under Article 82 EC' in D. Geradin (ed), *GCLC Research Papers On Article 82 EC* (Bruges: Global Competition Law Centre, 2005), p. 38. See G. Monti, *The EC Competition Law* (Cambridge: Cambridge University Press, 2007) 213. See also J. T. Lang, 'The Requirements for a Commission Notice of the Concept of Abuse under Article 8' *Centre for European Policy Studies* (2008), p.4.

4. See J. T. Lang and R. O'Donoghu, 'Defining Legitimate Competition: How to Clarify Pricing Abuses under Article 82 EC', *Fordham International Law Journal*, 26 (2003), 83-185 (p.83, p.84). See also D. Geradin, *GCLC Research Papers On Article 82 EC*, (Bruges: Global Competition Law Centre, 2005), p.148.

5. Case T-203/01 *Manufacture française des pneumatiques Michelin v Commission of the European Communities* [2003] ECR II-3275, para. 235, 246. C-95/04 *British airways v Commission* [2007] ECR I-2331. See P. Lowe, 'Consumer Welfare and Efficiency – New Guiding Principles of Competition Policy?' (13th international conference on competition 13th International Conference on Competition and 14th European Competition Day, Munich 2007). See also P. Oliver, 'The Concept of "Abuse" of a Dominant Position under Article 82 EC: Recent Developments in Relation to Pricing' *European Competition Journal*, 1 (2005): 315-339 (p.315, p.316).

6. See European Commission, 'Report on Competition Policy 2009', p.4. See also A. Jones and B. Sufrin, *EC Competition Law: Text, Cases, and Materials*, 3rd edn (Oxford: Oxford University Press, 2008), p.2, p.4. See also S. F. Ross, *Principles of Antitrust law* (New York: Westbury, 1993), p.3. See also H. Hovenkamp, *Federal Antitrust Policy* (St. Paul: West Publishing, 1994) p.49.

7. See Jones and Sufrin (2008), p.3. See R. J. Van den Bergh and P. D. Camesasca, *European Competition Law and Economics: a Comparative Perspective* (Oxford: Hart; Antwerpen: Intersentia, 2001) 1. See also G. Monti, *The EC Competition Law* (Cambridge: Cambridge University Press, 2007), p.63.

8. G. A. Hay, 'Market Power in Antitrust', *Antitrust Law Journal*, 60 (1991), p.807. KoenT'Syen, 'Market Power in Bidding Markets: An Economic Overview,' *World Competition*, 31 (2008), p.37, p.38.

9. OECD, 'The Objectives of Competition Law and Policy and the Optimal Design of a Compfetition Agency,' *OECD Journal of Competition Law and Policy*, 5 (2003), pp. 8-9. E. Arezzo, 'Is There a Role for Market Definition and Dominance in an Effect-Based Approach,' in M. Mackenrodt, B. C. Gallego and S. Enchelmaier (eds), *Abuse of Dominant: New Interpretation, New Enforcement Mechanism?* (Berlin: Heidelberg, 2008), p.35

10. J. Fejo, *Monopoly Law and Market* (Netherlands:Deventer, 1990), p.29.

11. The opposite term is x-inefficiency; it indicates that the undertaking has no incentives to reduce the cost of production or to produce new developed products. See Monti(2007), p.55.

12. A. Jones and B. Sufrin, *EC Competition Law: Text, Cases, and Materials*, 3rdedn (Oxford: Oxford University Press, 2008), p.13. See Monti(2007), p.44, p.45.

13. Whish (2009), p.5. See also E. Gellhorn, *Antitrust Law and Economics* (West Publishing Co., 1976), p.41. See also Jones and Sufrin (2008), p.3.

14. See, for example, J. Vickers 'Concepts of Competition' *Oxford Economic Papers*, 47 (1995).

15. Whish (2009), p.5; Jones and Sufrin (2008), p.3.

16. See Whish (2009), p.5; Vickers (1995), p.4.

17. Whish (2009), p.5; Jones and Sufrin (2008), p.3.

18. Monti (2007), p.54.

19. Whish (2009), p.5; Jones and Sufrin (2008), p.3; Monti (2007), p.54.

20. Whish (2009), p.5; Jones and Sufrin (2008), p.3.

21. See L. Peeperkorn and E. Paulis, 'Competition and Innovation: Two Horses Pulling the Same Cart,' in P. Lugard and L. Hancher (eds), *On the Merits: Current Issues in Competition Law and Policy* (Antwerpen: Intersentia, 2005), p.21, p.22.

22. Gellhorn (1976), p.41; Jones and Sufrin (2008) p.3; D. G. Goyder, *EEC Competition Law* (Oxford: Clarendon Press, 1988), p.9; Whish (2009), p.6, p.7.

23. Ibid.

24. M. Cini and L. McGowan, *Competition Policy in the European Union* (London: Macmillan, 1998), p.4. See also R. W. Crandall and C. Winston 'Does Antitrust Policy Improve Consumer Welfare? Assessing the Evidence,' *The Journal of Economic Perspective*, 17 (2003): 3-26 (p.3).

25. See Commission, 'Report from the Commission (Report on Competition Policy)' COM (2011) 328 final, 2, where the European Commission considers the consumer interest is the goal beyond building the single market; Commission Communication, Guidance on its Enforcement Priorities in Applying Article 82 of the EC Treaty to Abusive Exclusionary Conduct by Dominant Undertakings [2009] OJ C45/7, para.5. See also Van den Bergh and Camesasca (2001), p.2.

26. It states: "1. The following shall be prohibited as incompatible with the internal market: all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market, and in particular those which…2… 3. The provisions of paragraph 1 may, however, be declared inapplicable in the case of: - any agreement or category of agreements between undertakings; - any decision or category of decisions by associations of undertakings; - any concerted practice or category of concerted practices, which contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not".

27. The European Commission has allocated a chapter to explain the effect of cartels and the consequences on consumer interests. See European Commission 'Report from the Commission (Report on competition policy 2008)' COM (2009) 374 Final, 3. See also A. C. Witt 'Public Policy Goals under EU Competition Law-Now is the Time to Set the House in Order,' *European Competition Journal*, 3 (2012), p.443.

28. The European Commission stressed this by stating, "[t]he objective of Article 81 is to protect competition on the market as a means of enhancing consumer welfare and of ensuring an efficient allocation of resources. Competition and market integration serve these ends since the creation and preservation of an open single market promotes an efficient allocation of resources throughout the Community for the benefit of consumers"; Communication from the Commission - Notice - Guidelines on the application of Article 81(3) of the Treaty [2004] OJ C101/97, para.13. See L. Parret, 'Shouldn't We Know What We Are Protecting? Yes We Should! A Plea for a Solid and Comprehensive Debate about the Objectives of the EU Competition Law and Policy' *European Competition Journal*, 6 (2010), p.339, p.346, p.347.

29. See D. Zimmer, 'The Basic Goals of Competition Law: to Protect the Opposite of the Market,' in D. Zimmer (ed), *The Goals of Competition Law* (Cheltenham; Northampton, MA: Edward Elgar, 2012), p.491.

30. In the forward of the annual report of competition of 2007, NeelieKroes (Member of the Commission in charge of competition policy) stressed the importance of consumer welfare as an important objective of the European Competition law. See European Commission, 'Report on competition policy› COM (2007). See also Bork (1978), p.66; and Zimmer (2012), p.490.

31. See L. Kaplow, 'On the Choice of Welfare Standards in Competition Law,' in D. Zimmer (ed), *The Goals of Competition Law* (Cheltenham; Northampton, MA: Edward Elgar, 2012). See also P. Lowe, 'Consumer Welfare and Efficiency – New Guiding Principles of Competition Policy?' (13th International Conference on Competition and 14th European Competition Day, Munich 2007).

32. See Arezzo (2008), p.34.

33. The producer surplus indicates the excess of the price received by producer over the normal price (the supposed the competitive price).

34. Zimmer (2012), p.493; Jones and Sufrin (2008), p.13; Van den Bergh and Camesasca (2001), p.63, p.64; Kaplow (2012), p.4.

35. The Vice-President of the European Commission responsible for Competition Policy *JoaquinAlmunia* in the Foreword of the Commission of 2009 stressed that, competition policy aims to achieve total welfare as he said: '[a]s Competition Commissioner, I am here to ensure that competition policy delivers for consumers and for businesses'. See European Commission, 'Report on Competition Policy 2009', p.4.

36. Jones and Sufrin (2008), p.13; Van den Bergh and Camesasca (2001), p.5, 63, p.64. See also P. S. Crampton, 'Alternative Approaches to Competition Law: Consumers' Surplus, Total Surplus, Total Welfare and Non-Efficiency Goals', World Competition, 17 (1994), p.55, p.58.

37. Van den Bergh and Camesasca (2001), p.3; Cini and McGowan (1998), p.4.

38. The US policy adopted this objective in the Robinson-Patman in 1936. The act imposed restrictions on big firms in the favour of small firms as said at that time "[s]mall is beautiful"; However, US antitrust policy is no longer interested in this objective. See Fejo (1990), p.30. See also W. J. Kolasky, 'What is Competition? A Comparison of U.S. and European Perspectives,' *The Antitrust Bulletin*, 49 (2004), p.29, p. 31.

39. See Van den Bergh and Camesasca (2001), pp. 2-4; C. Bright 'EU Policy: Rules, Objectives and Deregulation', *Oxford Journal of Legal Studies*, 16 (1996), p.535, p.540; Parret (2010) p.339, p.353.

40. Commission Notice on Agreements of Minor Importance [2001] OJ C368/13. Van den Bergh and Camesasca (2001), p. 5.

41. There are three scenarios in terms of the market share. First: if the agreement is between the competitors (actual or potential), the threshold of the market share hold by all parties should not exceed 10% of the relevant market. Second, if the agreement is between non-competitors, the threshold of the market share hold by all parties should not exceed 15% of the relevant market. Third, if the agreement is between several different suppliers and distributors, and these agreements have a cumulative effect on restricting the competition on the market, the threshold becomes 5% and the aggregate threshold less than 30% of the relevant market. See Jones and Sufrin (2008), pp.184-185. Van den Bergh and Camesasca (2001), pp.1-2.

42. See M. M. Dabbah, *Competition Law and Policy in the Middle East* (Cambridge: Cambridge University Press, 2007), p.168; M. F. Elshunaq,*Monopolisation and Anticompetitive Practices* (Amman: Dar Elthaqafa), p.52.

43. See Van den Bergh and Camesasca (2001), p.4. See also Crampton (1994), pp.56-57.

44. See Van den Bergh and Camesasca (2001), p.2; Cini and McGowan (1998), p.4.

45. Monti (2007), p.50, p.51. See also A. Schaub, 'Objectives of Competition Policy,' in C. D. Ehlermann and L. L. Laudati (eds), *European Competition Law Annual* (Oxford: Hart Publishing, 1998), p.120.

46. The boundaries may be governmental or designed by private firms. The competition rules have

supported European integration through prohibition of artificial boundaries. They also prohibit the firms' practices and the Member State's actions. Cini and McGowan (1998), p.4. See also Commission, 'Report from the Commission (Report on competition policy)' COM (2011) 328 Final, p.4. See Van den Bergh and Camesasca (2001), p.55.

47. J. Almunia, 'Policy Objectives in Merger Control,' in B E. Hawk (ed), *International Antitrust Law and Policy* (Fordham:Juris Publishing, 2012), p.317.

48. European Commission, 'Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions (Report on Competition Policy 2011)' COM (2012) 253 Final, p.2.

49. See Schaub (1998), p.119. See also Jones and Sufrin (2008), p.13. See also Van den Bergh and Camesasca (2001).

50. Jacques H. J. Bourgeois, 'The Objectives of Competition Policy,' in C. D. Ehlermann and L. L. Laudati (eds), *European Competition Law Annual* (Oxford: Hart Publishing, 1998), p. 173. See PeeperkornPaulis (2005), p.21.

51. Article 15 of the Draft Law.

52. See Schaub (1998), p.119. See also L. L. Gormsen, 'Article 82 EC: Where Are We Coming from and Where We Going to?', *The European Law Review*, 2 (2006), p.6.

53. See Parret (2010), p.339, p.340.

54. See Peeperkorn and Paulis (2005), p.25.

Chapter Six

Market Measures in the European Union: How do Consumers Get an Advantage?

Chapter Six

Internal Market Measures in the European Union: How do Consumers Get an Advantage?

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Introduction

The general frame of the policy of consumer protection in the European Community (EC) treaty is outlined in articles (4/f) and (169) of the EC treaty.[1] This policy provides the following rights to consumers:[2] the freedom of choice and decision,protection of their legitimate expectations of the suppliers of goods and services and protection of their particular legal interests (such as health and safety of products and services, judicial protection and access to justice including collective legal protection and alternative dispute resolution mechanisms).[3] To attain the above rights, there must be an internal market between member states so as to allow consumers free access to goods and services across the EU borders.[4] The movement of goods and services across the borderprovides consumers with choice in terms of the products and services offered, and the bargaining power with which to purchase them.[5] This free movement enriches the competitive practices of the internal market and promotes the efficient supply of goods and services efficiently (negative measures).[6] The aim of this paper is to examine how the internal market enhances the legal and economic position of consumers when they make market transactions. The first part of this paper approaches the notion and the requirements of the internal market according to the European legal system, while the second explains how this market enhances the legal and economic interests of consumers.

1- The notion of the internal market in the EC Treaty

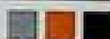
The internal market refers to an area that is established without internal frontiers between the member states, in which the free movement of goods,

persons, services and capital are ensured, and the legal organisation of this area is harmonised.[7] It necessitates that the restrictions and rules that currently hamper the creation of a single market are brought down.[8] This provides consumers with more purchasing opportunities as there are allowed direct access to the EC markets.[9] The cornerstones of the internal market are often said to be the 'four freedoms': the free movement of people, goods, services and capital.[10] The EC treaty highlights the establishment of the internal market and progressive approximation of the economic policies of the member states as a main focus for the community.[11] This objective requires the free movement of people, goods, services and capital (the negative integration actions), in addition to generating a status of legal integration between the member states (the positive integration actions).[12]It is these actions that form the main interest of this part of the study.

1.1- Negative integration actions

Negative integration actions the free movement of persons, goods, services and capital between the member states. These free movements are essentialfor the maintenance of the internal market objectives.[13]The European Court of Justice (ECJ) adopted this orientation somewhat comprehensively when it decided that member states must not only establish relations of international law when trading amongst each other, but also create an independent legal system, impacting directly on the relations of private citizens.[14] This impact will ensure *the free movement of persons, goods, services and capital between them.*[15]

In order to ensure the free movement of goods between the member states, a variety of obstacles or barriers to inter-member states trade must be removed. The EC treaty recognises the following main obstacles to intra-community trade and therefore the creation of the internal market:[16] customs duties (tariffs) on imports and exports (or other charges with a similar effect), quantitative restrictions (quotes) on imports and exports (or measures to the same effect),[17]the discriminatory internal taxation of imports, state monopolies of a commercial character and state aids to national industries or undertakings.[18] The elimination of these restrictions would enable consumers to compare and the products on offer in all member states markets, and therefore the power to bargain amongst them.[19] To ensure the best practice of this measure, the EU legislator has expanded upon the above-mentioned interpretation of negative integration actions, providing that the free movement of goods *is also applied to neutral measures*, therefore catching domestic and imported products. The authorities of the national courts therefore have the option of testing the composition and content of the products in order to rule out national measures



that may restrict the free movement of products between the member states.[20]

In order to ensure the free provision of services between the member states, discrimination on grounds of nationality must be prohibited(found in article (18) of the EC treaty). Articles (56-62) of the EC treaty deal with the provisions of services of an industrial, commercial or professional character. In particular, services shall include: activities of an industrial character, activities of a commercial character, activities of craftsmen and activities of the professions. Such services are these normally require remuneration.[21]Under the community law, services can be provided in three different ways: either the provider, without becoming established, moves to the place or country of the recipient; the recipient moves to the provider's country to obtain a service;or the services move across bordersas tangible products.[22]

Eliminating discrimination on the grounds of nationality between the member states has an important function in attaining the above-mentioned freedoms,[23] and does not require any positive legal action by the member states.[24] This obligation has a direct effect on the national courts, as they must apply it directly.[25] The ECJ considered this obligation to be a main indicator in determining the scope of the application of the treaty. It decided that union citizenship should be the fundamental status of the nationals of the member states.[26] It enables those who find themselves in the same situation to enjoy the same legal treatment irrespective of their nationality.[27]

1.2- Positive integration actions

Positive integration actions refer to the direct support of consumer interests through the adoption of independent consumer policieswithin the community.[28] It attempts to provide independent information and to pursue autonomous protection objectives, which can be attained by harmonising the regulations of these member states in the area of consumer protection. It is based on the direct legislative activities to create a unified legal framework that protects consumers within the member states. This action, in its aim ofunifying the legal measures ruling the legal relations between consumers and sellers, is considered to be afundamental element of the establishment of a single market in the EC.[29] A unified legal framework means that consumers will face the same, or similar, provisions controlling their transactions with sellers in all markets of the member states.[30] Measures taken by the community do not serve just to promote and supplement, but also to monitor the policies of the member states. This monitoring can be used to examine whether the member states actually secure an optimal scale of protection for their citizens and whether they meet the obligations of their consumer protection directives.[31]

The EU regulations and directives, along with the jurisprudences of the ECJ form the necessary tools for implementing this action.[32] The power of the community with regard to consumer protection is not exclusive; it is bound by the principles of subsidiarity and proportionality, as set out in article (5) of the EC treaty.[33] In areas that do not fall within its exclusive competence, therefore, the community is allowed to take action in accordance with the principle of subsidiarity.It can only do this, however, if and when the objectives of the proposed action cannot be sufficiently achieved by the member states and can therefore, by reason of the scale or effects of the proposed action, be better achieved by the community.[34] The community in itself lacks enough power to ensure its objectives and policies in the area of consumer protection, and this is known as the principle of subsidiarity.[35] Paragraph (1) of article (169) of the ECtreaty illustrates unarguably that consumer protection constitutes an area of autonomous policy within the community.[36] The community is neither the holder of a monopoly, nor does it have exclusive jurisdiction (the principle of subsidiarity) as it merely "makes a contribution" as exemplified in article (4/t) of the (EC) treaty.[37] The objective of the contribution is to promote the interests of the consumers. It concerns the joining of responsibilities that are to be taken by the community and the member states in the area of consumer protection.[38] For this reason, the principle of subsidiarity is generally only applicable to the area of consumer policy because the community lacks exclusive jurisdiction (article 5 of the EC treaty). This matter justifies the role of national measures in promoting and enhancing the requirements of consumer protection.

Various harmonisation methods can be detected in the (EU) legal system in this context.[39] These include: total (maximum) harmonisation, which allows no derogation in the preempted area, except what is permitted in the directive; optional harmonisation, which refers to how producers are allowed to apply national or community norms; partial harmonisation,which refers to the re gulation of some aspects of the subject matter (i.e. rules which only applied to certain cross-border transactions); minimum harmonisation,which allows member states to provide more stringent rules; and alternative harmonisation, which enables MS to choose between alternative methods of harmonisation.[40] Both minimum and maximum harmonisation techniques are used in the area of consumer protection.

It is important to understand the distinction that is madein the field of consumer protection between the techniques of maximum and minimum harmonisation, and how the (EU) legislator harmonises the member states legal systems in this field.[41]

As part of the technique of maximum harmonisation, the EC appoints a ceiling of protection that member states have to maintain, and must not exceed, in their legal systems. This ensures that uniform rules are applied in all member states legal systems and that consumers obtain the same level of protection in all member states.[42] This represents a compromise both between the aims of market integration and the achievement of wider policy objectives, and the imperatives of market integration and respect for national identities as suppliers are no longer confronted with different legislations.[43] Member states would then lack the power to establish a "higher standard of protection" in favour of consumers.[44] Thus, this sort of harmonisation can be considered the optimal way of establishing an internal market.[45]

The technique of minimum harmonisation overcomes contradictions that arise between the following three important objectives:[46] the objective of the internal market, the objective of consumer protection and the balancing the legal relations between the member states and the EC with "the sovereignty of the member states".[47]This occurs where the community legislator lays down a "floor" of common rules, which authorises the member states to retain or introduce measures that can be considered more stringent.[48]Through this technique of harmonisation, the member states are allowed to include within their legal systems a higher level of protection than is provided by the directive. Thus, we are referring to a minimum ceiling of protection, which the member states have to adopt in their legal systems.[49]

2- How Do Consumers Get Advantages?

The drafters of the EC treaty realised that consumers can benefit from the creation of an internal market;[50] increased supply of products and greater competition would drive prices down and improve the consumers' range of choice and their confidence in the EU markets. Promotion of economic integration and the free movement of goods therefore became a principal motivation for community institutions to improve consumer protection.[51]Thus, the policy of consumer protection under the EC treaty is divided into economic and social aspects; both objectives are provided in article (3) of the EC treaty, which stipulates that,"this objective was primarily to be achieved by implementing production-related measures". In other words, promoting the right ofconsumer choice is based mainly on the promotion of European policy, which focuses on improving the measures of production and distribution.[52]

The real impact of an internal market on consumer interests can be explained

clearly with reference to the 1975 program.[53]This program failed to carry out its objectives because it did not adopt the internal market objectives in its policy. On this, Bourgoignie said "in order to implant the measures set out in the action plans and in the absence of provisions of the treaty, specifically referring to consumers, the legal basis of any commute action in the field of consumer protection has to come from articles providing for the creation of the internal market".[54]

The role of market integration, therefore, is to ensure economic benefits for consumers, and to provide greater choice of goods and services, competition on merit, lower prices and a higher standard of living for consumers. Thus, the internal market policies must ensure that these benefits,including maintaining the quality of goods and services, are realised. In addition, the internal market cannot function properly without consumer confidence. Adequate consumer protection is necessary for growth and competition.[55] In short, the impact of the internal market on consumer interests can be explained through the application of two principles: the principle of competition and the principle of consumer confidence. These two principles are the main focus of this part of the study.

2.1- *Competition measures and consumer protection*

Competition means prohibiting all agreements between undertakings that may affect free trade between member states and which distort the fair competitive advantages in the common market. It also means prohibiting any abusive behavior by one or more undertakings of a dominant position in the common market or in a substantial part of the common market. Examples of anti-competitive behaviors are provided in article (101/1) of the EC treaty. According to this article, any behavior that directly or indirectly fixes purchase or selling prices or any other trading conditions, limits or control production, markets, technical development or investment is forbidden. Article (102) also determines that the abuse of a market-dominating position, which may directly or indirectly impose unfair purchase or selling prices or other unfair trading conditions, limit production, markets or technical development to the prejudice of consumers, is also forbidden.

Fair competitive measures between undertakings may enhance consumer interests via three main factors.[56] One factor is price: consumers buy products at the cheapest price available to them. Another is appropriateness: consumers buy the products that most suitably satisfy their tastes and preferences. Finally, there is the quality factor: consumers purchase products of the quality that they are looking for. However, consumers tend to only pay attention to the price factor,

and this may have negative consequences. For example, consumers may lose out on access, quality, information, reduced choice and less innovation in the products that they choose.[57]When consumers are not paying enough attention to the appropriateness and quality factors, the competitive market will naturally promote these two factors, and thus overcoming these disadvantages.[58]The impact of free competition policy on consumer interests also has an economic base. Competition law operates at the structural levelof the market, and controls and prohibits any agreements between undertakings that may have a negative affect on consumer interests. Further, it analyses the agreement economically in order to determine whether it has an anti-competitive effect, and whether such an effect is significant.[59]Accordingly, it may indirectly improve consumer interests by stimulating firms to innovate, decrease pressure on costs, provide incentives for the economic efficient and organise elements of production and distribution.[60]

It is worth noting that the mechanism of competition policy towards consumer interests does not derive from direct regulations that protect consumers, but rather depends upon the margin of consumer choices. The mechanism also improves the competitive activities undertaken between traders in order to ensure that there are many options for consumers within the same market. This cannot be achieved, however, without adopting a legal framework to control national rules, and breaking free trade.[61]This framework indirectly influences consumer interests by increasing the amount of products on offer in one market. Three elements must be considered to ensure the success of this legal framework.[62] Firstly, thatintensive regulatory activity against restrictions of market access must be adopted, and that these activities have a direct impact on the behaviors of undertakings and consequently have an indirect impact on consumer freedom of choice. Secondly,that the member states be allowed to retain reasonably restrictive rules on entry and marketing if they can be justified by genuine consumer concerns. Thirdly, under community law, it should be checked that these restrictions are adequate forattracting consumer interest. In short, the free market policy attracts high levels of consumer interest by maintaining free competitive measures between undertakings.[63]

2.2- Consumer confidence and consumer right of information

This principle deals withmarket transactions of the consumer outside his/her frontiers, and is there to ensure that consumers are notseriously disadvantaged by the legal systems of other member states. The positivity of the consumer stimulates him to shop around within the different markets of the member states. This sense of positivity can be attained by creating confidence between

consumer and the markets, which can be achieved by making this consumer believe that the legal system applied in his/her own state with regards to trading relations is the same, or similar, to the legal systems applied in other member states.[64]To be sure that he/she is not disadvantaged when making market decisions, the consumer must be aware of the legal system organising the market that he/she is dealing with.[65]This is not possible when the applied legal systems of these member states differ from the consumer's own legal system. This is also made difficult through language barriers: if these legal systems are not unified, the differences in language also impede consumer awareness, and, in turn, consumer confidence[66]The explanatory memorandum of the Directive (93/13) underlined that it cannot be assumed that consumers who cross frontiers to buy goods or services, or to invest, have understood and agreed to the terms of a contract they have made, if they do not speak the local language and have no understanding of local law, unless there is some assurance that they will not be seriously disadvantaged by unfair terms. Thus, creating a base of unified rules to organise the activities of consumers in all member states is will ensure consumer confidence.[67]

It is important to note also that this principle also extends to the activities of businesses in other member states markets. In the absence of this principle, fair competition between the undertakings of the member states is restricted. The rules of fair competition may be breached where: (a) the law of the member states organising the relations between sellers and consumers shows significant disparities, and (b) foreign sellers are not familiar with other national rules toorganise their activities.[68]

The consumer's right to information meets the needs of the consumer by making sure that no internal failures affect the consumer's ability to make the appropriate choice. European consumer protection measures necessitate that certain information be given in a manner that is "comprehensible" to the consumer. The ECJ expressly mention the importance of this right: the provision of information to the consumer is considered to be one of the principle requirements under the community law of consumer protection.[69]It is important to illustrate the role of the consumer's right to information as it will improve and enhance his/her legal interests by determining the extent to which the use of Safer Future Communities (SFC) may damage a consumer's legal interests.

The EC consumer policy has, of course, relied heavily on rules on the necessity of providing information to consumers. These rules have played an important role in improving the consumer's bargaining position in the internal market. The ECJ considers the provision of information to consumers central to consumer protection policy, and that improving the former will improve the latter.[70]

Informational measures play an important role in reducing the negative impacts of using SFC terms. In many cases, this right is considered to be sufficient for protecting consumers. For this reason, the British Office of Fair Trading (OFT) classifies the consumer's right to information as integral to the test of fairness.[71] According to the OFT, the unfairness in market transactions arises as a result of "the consumer's lack of information which consequently affects his right of choice".[72]This clarifies how these contracts restrict the consumer's right to information and therefore his right of choice.[73]

The main aim of this right is to secure and enhance legal position of the consumer in the market. For this reason, this right will only be satisfied if the information is made available in a comprehensible and accessible language, so the average consumer can understand its meaning and consequences.[74] Sufficient information should be made available to the purchaser of goods and services to enable him to:[75] assess the goods and services, make rational choices between competing products and services, use these products and services safely satisfactorily and to claim redress from any injury or damage resulting from the product supplied or services received.

This improves the bargaining position of a consumer in three main ways.[76] Firstly, a consumer may refuse to make a contract that seems unfair to him, and, as a result, choose not to acquire the offered goods or services, as they appear incompatible with their needs, or are offered without fair contract terms.[77]Secondly, a consumer can use this right when negotiating a better position with the business party.Thirdly, a consumer may have the opportunity to shop around within market place for other offers, which are more suitable and acceptable than the original one.

The criticisms of the information paradigm are also well known. Criticisms include: necessary information may not reach the consumers, consumers find the information provided difficult to use or understanding, andconsumers may not find it worthwhile to gather the necessary information, considering the relatively small advantages that it may bring.[78] These kinds of problems seem to affect most the more disadvantaged groups of consumers. For example, studies concerning truth-in-lending regulation show clearly that the improvement, if any, of interest awareness due to such regulation seems to apply more to higher-income groups. The regulation of information also lacks relevance if the consumer does not have any practical alternatives. Information that a cheap product is of inferior quality to a corresponding more expensive product does not help a consumer who cannot afford this alternative. In other words, well-off consumers tend to gain more from a transparency strategy than less advantaged ones.[79]

Notes

1. J. Stuyck, 'European Consumer Law After the Treaty of Amsterdam: Consumer Policy in or Beyond the Internal Market?'*Commercial Law Review Journal* (2000), p.378; A. P. Reindll, 'Consumer Contracts and European Community Law,'*Washington University Law Quarterly*, 75 (1997), p. 628. (

2. See N. Reich, *Understanding EU Consumer Law* (Brussels: Centro de FormacaoJuridica e Judiciaria, 2009), p.21; H. W. Micklitz, 'The Principles of European Contract law and the Protection of the Weaker Party', *Journal of Consumer Protection* (2004), p.339; N Reich, 'A European Contract Law or an EU Contract Law Regulation for Consumers,'*Journal of Consumer Protection* (2005), p.383.

3. E. Houndous, 'The Reception of the Directive on Unfair Terms in Consumer Contracts by Member States,' *European Review of Private Law*, 3 (1995), p.241.

4. See: E. P. Exter, 'Legal Consequence of EU Accession for Central and Eastern European Health Care System,'*Electronic Law Journal* (2002), p.556; C D Ehlermann, 'The International Market Following the Single European Act,'*Common Market Law Review* (1987); N Reich, *Understanding the EU Law*, 2nd edn (Antwerp: Intersentia Publishers: 2005).

5. It is defined by the commission as: "the cross border movement of goods and services that allows consumers to search out bargains and innovative products and services and thus ensures that they optimize their consumption decisions. This cross-border demand increases competitive pressure within the internal market and allows for a more efficient and competitively priced supply of goods and services. This virtuous circle can only be achieved if the regulatory framework in place encourages consumers and businesses to engage in cross-border trade. Different national laws on commercial practices relating to business–Consumer relations can hinder this evolution". See the Commission green paper on European Union Consumer Protection 2001, COM (2001) 531 final, Brussels, 2.10.2001, para. 2-1.

6. The green paper on European Union consumer protection introduced by the commission of the European union of the European community, Brussels, 20.10.2001, p.3; available at: http://ec.europa.eu/Consumers/policy/developments/fair_comm_pract/fair_comm_greenpap_en.pdf, visited on 12-11-2007; see also: http://www.csd.bg/artShow.php?id=13715 visited on 16-10-2007.

7. Article (14/2) of the (EC) treaty; T Hartley, 'Article 13: Consumer Contracts,'*European Law Review Journal*, 19 (1994), pp.537-538.

8. For more details see P Nebbia, 'Internal Market and the Harmonization of European Contract Law,' in T Tridimas and P Nebbia, *EU Law for the 21st Century: Rethinking the New Legal Order* (Oxford: Hart, 2004), p. 96

9. See the green paper of the commission of the European community COM (2001) 531 final, Brussels, 2.10.2001, p.3; and O Arowolo, 'Application of the Concept of Barriers to Entry Under Article 82 of the EC Treaty: Is There A Case For Review?,'*European Commercial Law Review Journal*, 26 (2005), p.251.

10. See Ehlermann (1987); Exter (2002), p.556; see also the following link:

    http://ec.europa.eu/internal_market/top_layer/index_1_en.htm, visited on 17-11-2007.

11. Article (3) of the (EC) treaty; see also C Joerges, translated from German by L Fraser and P Wilkins, 'The Europeanization of Private law as a Rationalization process and the contest of Disciplines: An Analysis of the Directive on Unfair Terms in Consumer Contracts,' *European Review of Private Law* (1995), p.175.

12. For more details about the internal market policy in the (EU) law, see: G Howells, H Micklitz and T Wilhelmsson, *European Fair Trading Law*, 3rdedn (London: Ashgate Publishing, 2006); R Barents, 'The Internal Market Unlimited: Some Observations of the Legal Basis of Community Legislation,' *Common*

Market Law Review (1995); M Doughan, 'MinimumHarmonization and the Internal Market,'*Common Market Law Review* (2000), p.835.

13. See: S Weatherill, 'Free Movement of Goods,'The International and Comparative Law Quarterly, 43 (1994), p.207; see also The (ECJ) opinion No. (1/91), (1991) ECR 1-6079, 6102.

14. See G. Scott, 'Unfair Terms in Consumer Contracts in the European Community,'*Products Liability Law Journal*, 4 (1993), p.90; N Bamforth, 'The Limits of European Union Consumer Contract Law,' *European Law Review*, 24 (1999), p.410.

15. See the opinion No. (1/91), (1991) ECR 1-6079, 6102; see also O. Arowolo, 'Application of the Concept of Barriers to Entry Under Article 82 of the EC Treaty: Is There a Case for Review?',*European Commercial Law Review Journal*, 26 (2005), p.251.

16. See J. Tillotson, *European Community Law, Text, Cases and Materials*, 2nd edn (London: Cavendish Publishing Limited, 1996), p.235; K J Alter, 'Judicial Politics in the European Community: European Integration and the Path Breaking (Cassis de Dijon),'*Comparative Political Studies*, 26 (1994), p.535; H Micklitz and N Reich, *Understanding EU Consumer Law* (Brussels: Centro de FormacaoJuridica e Judiciaria: 2009), p.9.

17. P. Koutrakos, 'On Groceries, Alcohol and Olive Oil: More on Free Movement of Goods After Keck,' *European Law Review*, 26 (2001), p.391; S Weatherill, 'Consumer Safety Legislation in the United Kingdom and Article 30 EEC,' *European Law Review Journal*, 13 (1988), p.87.

18. See also: M. W. Hesselink, 'Consumer Protection, Citizenship or Justice,' *European Review of Private Law Journal* (2007), 323-348; E. Hondius, 'The Protection of the Weak Party in a Harmonized European Contract Law,' *Consumer Protection Law Journal* (2004), p.245; G Howells and T Wilhelmsson, 'EC Consumer Law: Has it Come of Age?', *European Review of Private Law Journal* (2003), p.370.

19. N. Reich and G. Woodroffe, European Consumer Policy After "Maastricht" (Netherlands: Kluwer Acadamic Publisher, 1999), p.293; Koutrakos(2001), p.391. The same situation can be applied in article 49 of the (EC) treaty relating to services sectors and article (56) relating to the free movement of capital. See Weatherill(1994), p.207; Micklitz, Reich and Weatherill, 'EU Treaty Revision and Consumer Protection,' Journal of Consumer Policy (2004), p.367.

20. In this context, the (ECJ) decided that, the concept of the (MEE) is to be understood to mean that, the fixing of minimum alcohol content for alcohol beverage, which is intended for human consumption by the national measures of the member states, also falls within the prohibition that is laid down in that provision. The .ECJ 120/78(1979) ECR 649; see also Koutrakos (2001), p.401.

21. See article (50) of the (EC) treaty; see also J Stuyck, 'European Consumer Law After the Treaty of Amsterdam: Consumer Policy In or Beyond the Internal Market?', *Commercial Law Review Journal* (2000), p.392; G. Hadfield, R. Howse and M. Trebilcock, 'Information-Based Principles for Rethinking Consumer Protection Policy,' *Journal of Consumer Policy* (1998), p.131; J Fairhurst and C Vincenzi, *Law of the European Community*, 4th edn (London: Pearson Longman, 2003), p.273.

22. See C Barnard, 'Fitting the Remaining Pieces into the Goods and Persons,' *European Law Review*, 26(2006), p.35.

23. Barnard(2006), p.36; P Oliver, 'Some Further Reflections on the Scope of Article28-30 EC,' *Common Market Law Review*, 36 (1999).

24. P Akman, To Abuse, or Not to Abuse, Discrimination Between Consumers,'*European Law Review*, 32 (2007), p. 492.

25. Micklitz and Reich (2009), p.48; Nebbia (2004), p.96.

26. See C. T. Flesner, *Consumer Product Guarantees* (USA and England: Ashgate Publishing Limited, 2003), p.157; C Quigley, *European Community Contract Law: The Effect of EC Legislation on Contractual Rights, Obligations and Remedies* (London-the-Hague, Boston: Kluwer law international, 1996), p.261.

27. For more details, see the following link; http://en.wikipedia.org/wiki/Citizenship_of_the_European_Union. Accessed on 16-5-2007

28. Micklitz and Reich (2009), p.11; Exter (2002), p.556; Ehlermann, (1987); Howells (2003), p.373.

29. See the Council directive on the approximation of the laws, regulations and administrative provisions of the member states concerning liability for defective products («Product Liability Directive»), 1985 O.J. (L 210) 29 (recital 1 provides that, different liability standards for defective products distorts competition, restricts intra-community trade and results in different levels of consumer protection); see also: G. Davies, 'Can Selling Arrangements be Harmonized?,' *European Review Law Journal* (2005), p.374; N. Reich, 'A European Contract Law, or an EU Contract Law Regulation for Consumers?,' *Journal of Consumer Policy*, 28 (2005), p.385.

30. See the Commission green paper on European Union consumer protection 2001, COM (2001) 531 final, Brussels, 2.10.2001, para 2-1.

31. S. Drak, 'Twenty Years After Von Colson: The Impact of «Indirect Effect» on the Protection of the Individual›s Community Rights,' *European Law Review*, 30 (2005), p.329.

32. See Davies (2005), p.371; A P Reindll, 'Consumer Contracts and European Community Law,' *Washington University Law Quarterly*, 75 (1997), p.627; M P Maduro, *We, the Court: The European Court of Justice and the European Economic Constitution* (Oxford: Hart, 1998), p.99; see also article 249 of the (EC) treaty; N Reich, 'The Constitutional Relevance of Citizenship and Free Movement in an Enlarged Union,' *European Review Law Journal* (2005), p.675.

33. See L. Gormley, 'The Legal Basis of Directive 92/59 on General Product Safety,' *European Law Review Journal*, 21 (1996), p.59; Reich (2005), 383; Davies (2005), p.381; Bamforth (1999), p.410.

34. See K. Ioannou, 'Recent Developments in the Application of Community Law in Greece,' *European Law Review*, 14 (1989), p.461; Weatherill (2005), p.23; and P Rott, 'Consumers and Services of General Interests: Is EC consumer Law the Future?,' *Consumer Law Journal*, 49 (2007).

35. Micklitz Reich (2009), p.20; Davies (2005), p.382.

36. Flesner (2003), p.156; T Wilhelmsson, 'The Abuse of the Confidant Consumer as Justification for EC Consumer Law', *Journal of Consumer Policy* (2004), p.321.

37. This paragraph stipulates that, "[f]or the purposes set out in Article 2, the activities of the Community shall include, as provided in this Treaty and in accordance with the timetable set out therein: (a contribution to the strengthening of consumer protection)."

38. Ioannou (1989), p.461; Micklitz and Reich (2009), p.21.

39. W. Gerven, 'Harmonization of Private Law: Do We Need It?,' *Common Market Law Review*, 41 (2004) p.508; see also I. Maselis, 'Legislative Harmonization and the Integration of Harmonized Legislation into the National Legal System within the European Community,' *European Review of Private Law*(1993), p.139.

40. For more details, see Joerges (1995), p.177.

41. It has to be noted that these two techniques are the main rules of harmonization that the (EU) legislator adopts when dealing with consumer protection directives.

42. The aim of the high common level of consumer protection has also been expressed in the Community

consumer policy strategy 2002: 2006 (Council resolution on Community consumer policy strategy 2002: 2006, OJ 2003, C 11/1) with further details in the related communication by the Commission (Commission's Communication on Consumer policy strategy 2002: 2006, OJ 2002, C 127/2)

43. M. Kenny, 'The 2003 Action Plan on European Contract Law: Is the Commission Running Wild?' *European Law Review Journal*, 28 (2003), p.540.

44. Micklitz and Reich (2009), p.41.

45. For more details about the advantages of the maximum harmonization way, see: P Rott, 'Minimum Harmonization for the Compellation of the Internal Market? The Example of Consumer Sales Law' *Common Market Law Review*, 40 (2003), p.1109.

46. See R. M. D-Sa and T. Krummel, 'Sale of Consumer Goods and Associated Guarantees: A Minimalist Approach to Harmonized European Union Consumer Protection,' *European Law Review Journal*, 26 (2001), p. 319; A. D. Moor, 'Common and Civil Law Conceptions of Contract and European Law of Contract: The Case of the Directive on Unfair Terms in Consumer Contracts,' *European Review of private Law*, 3, (1995), p.257; T. Wilhelmsson, 'European Contract Law Harmonization, Aims and Tools,' *Tulan Journal of International and Comparative Law*, 23 (1993), p.23.

47. See Reindll (1997), p.633; U Bernitz, 'The Commission's Communications and Standard Contract Terms,' in S. Vogenauer and S. Weatherill (eds), *The Harmonization of European Contract Law* (USA : Hart Publishing, 2006), p.185; E. Truilhé-Marengo, 'Towards a European law of Contract,' *European Review law Journal*, 10 (2004), p.471.

48. D-Sa and Krummel (2001), p314; F Cecco, 'Roomto Move? Minimum Harmonization and Fundamental Rights,' *Common Market Law Review*, 43 (2006), p.9.

49. ECJ 168/05 (2006) ECR I-10421; N Reich, 'European Consumer Law and its Relationship to Private Law,' *European Review of Private Law*, 3 (1995), p.295.

50. See the Commission green paper. 'Consumer Guarantee and After Sales Services,' COM (93) 509 final; Micklitz and Reich (2009), p.24.

51. See S. Mahajan and G. Ryzin, 'Inventory Competition Under Dynamic Consumer Choice,' *Operation Research*, 49(2001), p.646; I Ramsay, J Salloun, N Harrox and G Mowatt, *Risk and Choice in Consumer Society* (Brussels: Bruylant, 2007).

52. Micklitz and Reich (2009), p.11; the communication from the Commission to the European Parliament, the Economic and social committee and the committee of regions, consumer policy strategy 2002-6 COM (2002) 208 Final; see also Recital 6 of the directive.

53. The program of the (EEC) for the consumer protection and information policy: OJ C 92\1975.

54. T. Bourgoignie, 'European Community Consumer Law and Policy: From Rome to Amsterdam,' *Consumer Law Journal*, 4 (1998), p. 443.

55. Wilhelmsson (2004), p.317.

56. See the OFT publications: 'Consumer Detriment' (2000, HMSO); S. Davies and A. Majumdar, *The Development of Targets for Consumer Savings Arising from Competition Policy* (2004), The OFT Publications; Arowolo (2005), p.251; L Eagles, 'Of Ports, Pilots and Predation: New Zealand Courts Reassess Some Competition Fundamentals' *European Commercial Law Review Journal*, 17 (1996), p.462.

57. See R. Smith and S. King, 'Does Competition Law Protect Consumers,' *European Court Law Review*, 28 (2007), p.Search T412.

58. See P. Evans, 'Assessment Consumer Detriment', *European Competition Law Review*, 28 (2007), p.26.

59. The Commission green paper, "Consumer Guarantee and After Sales Services", COM (93) 509 final; Wagner, 'The Economics of Harmonization: The Case of Contract Law', *Common Market Law Review*, 39 (1995), p.1014; M. Tenreiro, 'Guarantee and After Sales Services: Brief Analysis of the Green Paper Presented by the European Commission', *Consumer Law Journal*, 81 (1995); P. Rott, 'Minimum Harmonization for the Compellation of the Internal Market? The Example of Consumer Sales Law,' *Common Market Law Review*, 40 (2003), p.1121.

60. P. Nebbia, 'Standard Form Contracts Between Unfair Terms Control and Competition Law' *European Law Review*, 31 (2006), p.103; F. Dethmers and N. Dodoo, 'The Abuse of Hoffmann-La Roche: The Meaning of Dominance Under EC Competition Law,' *European Competition Law Review*, 27 (2006) p.537.

61. Joerges (1995), p.179.

62. The communication from the Commission to the European Parliament, the Economic and social committee and the committee of regions, consumer policy strategy 2002-6 COM (2002) 208 Final; Micklitz and Reich (2009), p.46.

63. See also R. Korobkin, 'Behavioral Economics, Contract Formation and Contract Law,' in *Behavioral Law & Economics* (Cambridge: Cambridge University Press, 2000), p.116; T. Wilhelmsson, 'Cooperation and Competition Regarding Standard Contract Terms in Consumer Contracts', *European Business Law Review*, 54 (2006); Wilhelmsson (2004), p.317; T. Wilhelmsson, 'Private Law in the EU: Harmonized or Fragmented Europeanization,' *European Review of Private Law*, 77 (2002); J. Klick, 'The Micro Foundations of Standard Form Contracts: Price Discrimination vs. Behavioral Bias.' (2004). Available at: http://www.mason.gmu/~jklick/form.pdf. Accessed on 25-11-2007.

64. See Wilhelmsson(2004), p.325; M. J. Bonell, 'The CIGS, European Contract Law and the Development of a World Contract Law', *The American Journal of Comparative Law*, 56 (2008), p.6.

65. R. Whish, 'The Commission's New Style Block Exemption for Vertical Agreements,' *Common Market Law Review*, 37 (2000), p.887; V. Korah and D. O'Sullivan, 'Distribution Agreements Under the EC Competition Rules,' *Common Market Law Review* (2002); P. Taylor, Vertical Agreements:The New Regulation in Context, *Common Market Law Review* (2000).

66. The explanatory mandatory of the proposal (1990) of the Directive (93/13), COM (90) 322 final 2, clearly refers to the challenge of language affecting the consumer confidence.

67. In addition, recital 10 of the Directive 93/13 remarked tha, more effective protection of the consumer can be achieved by adopting uniform rules of law in the matter of unfair terms.

68. See J. Basedow, 'A Common Market Law for the Common Market,' *Common Market Law Review*, 33 (1996), p.1182; Recital (2) of the directive (93/13); N. Reich, *Understanding the EU Law*, 2nd edn (Antwerp: Intersentia Publishers, 2005), p.384; Nebbia, (2006), p.103; H. Micklitz, 'The Concept of Competitive Contract Law,' *Penn State International Law Review* (2005), p.561.

69. ECJ 362/88 (1990) ECR 667, 689; for a comprehensive discussion, see S. Grundman, W. Kerber and S. Weatherill, *Party Autonomy and the Role of Information in the Internal Market* (Berlin: Walter de Gruyter, 2001); M. Radeideh, *Fair Trading in EC Law - Information and Consumer Choice in the Internal Market* (Netherlands: European Law Publications, 2005); S. Grundmann, 'Information, Party Autonomy and Economic Agents in European Contract Law', *Common Market Law Review* (2002), p.269; G. Howells, A. Janssen and R. Schulze, *Information Rights and Obligations* (Aldershot: Ashgate, 2004); Wilhelmsson, (2006), p.51.

70. ECJ 362/88 (1990) ECR 667.

71. The OFT in its unfair contract terms guidelines lays down the criteria of the test of fairness as: "the term has the potential to upset the original balance of the contract; it leaves Consumers open to not getting what they were promised; it renders the Consumens position unforeseeable or exposes him to unexpected disbursement." See the OFT publications, *Unfair Contract Terms Guidance* (London, 2001).

72. For more details, see R. Bradgate, 'Unreasonable Standard Terms,' *The Modern Law Review Limited*, 60(1997), p.582; Hondius (1997), p.5; R Plaistowe, 'Models for Business-University Collaboration - The Lambert Agreements' *European Intellectual Property Review*, 27 (2005), pp.121-123.

73. I. Klauss and L. Rathje, 'Germany: Anti-Competitive Agreements - Sports Rights,' *European Competition Law Review Journal*, 29 (2008), p.180.

74. Y Farah, 'Allocation of Jurisdiction and the Internet in EU Law', *European Law Review Journal*, 33 (2008), pp.257-270; Micklitz and Reich (2009), p.23; S. M. Maniatis and A. K. Sanders, 'A Consumer Trade Mark: Protection Based on Origin and Quality', *European Intellectual Property Review Journal*, 15 (1993), p.406; Weiler and Lockhart, 'Taking Rights Seriously: The European Court and its Fundamental Rights Jurisprudences', *Commercial Law Review Journal*, 51 (1995).

75. Micklitz and Reich (2009), p.24.

76. Wilhelmsson (2006), p.52.

77. Wilhelmsson (2004), p.325; A. Gorrie, 'Competition Between Branded and Private Label Goods. Do Competition Concerns Arise When a Customer is also a Competitor?', *European Competition Law Review Journal*, 27 (2006), pp.217-227; Plaistowe (2005), pp.121-123.

78. P. Kirch, 'The French Paradox and the New Means to Fight Against Fraudulent Cases of Cooperation Commercial', *European Commercial Law Review Journal*, 27 (2006), pp.519-523.

79. 'The European Consumer Law Group in its Response to the Communication on European Contract Law', available at: http://europa.eu.int/comm/consumers/po..lnts/contr_law/comments/index_en.html visited on 22-3-2010; see also: Howells (2003), p.375; Whitford, 'The Functions of Disclosure Regulation in Consumer Transactions', Wisconsin Law Review, 2 (1973), p.414.

Chapter Seven

Transparency Norms, the World Trade Systems and Free Trade Agreements

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Introduction

Transparency is one of the fundamental standards of the trading system and is increasingly seen as an essential tool in the governance of international trade. Transparency, furthermore, has received significant attention and its importance continues to be recognised by international, regional and national legal regimes. More importantly, it is believed that without transparency, trade agreements would be ineffective. Transparency, moreover, allows trader actors and trading partners to see how rules are established: transparency in decision-making ensures fairness.

The central aim of this paper, therefore, is to highlight how the principle of transparency is integrated within the World Trade system and in Free trade agreements (FTAs). The paper firstly illustrates the meaning and importance of transparency in the global trade system. It should be noted that the global trade system is monitored and observed by the General Agreement on Trade and Tariffs (GATT) and its successor, the World Trade Organisation (WTO), which is considered to be the most important organisation in regulating International trade. The importance of transparency was stipulated in the 1947 GATT agreement, and these provisions have been implemented by the WTO. This paper will deal with how the concept of transparency is dealt with firstly in the GATT, and secondly in the WTO.

Moreover, the paper glances briefly at the provisions and articles of some FTAs (in particular the European Union (EU) Free Trade Agreements) that contained transparency provisions. Recently, many and various free trade agreements have been signed between states. Such agreements became the centerpiece of world trade as states sought to improve access to foreign markets for their

exporters, products and investors. In light of this, this paper will then outlinethe provisions of transparency that have been stipulated in different FTAs.

The last section of this paper suggests some articles and provisions to be included in any future Palestinian trade agreements in respect of transparency, based on the different FTAs that have been mentioned in the paper.

1. Transparency

Transparency is one of the fundamental norms of the world trading system and constitutes a cornerstone of the multilateral system.[1] Without transparency, trade rules and the value of Members' liberalisation commitments are just theoretical. Some scholars define transparency as:

> the availability and accessibility of knowledge and information about: (1) the meaning of norms, rules, and procedures established by the treaty and practice of the regime, and (2) the policies and activities of parties to the treaty and of any central organs of the regime as to matters relevant to treaty compliance and regime efficacy.[2]

It is noteworthy that the importance of transparency in the world trade is embodied by the collection of information by states either to evaluate their own performance, or the performance of their trade partners.[3] Furthermore, at a practical level, traders need all the information related to the trade rules and practices of other member states in order to take full advantage of the trade benefits that are presented in the agreement commitments.[4]

Since transparency is regarded as a legitimate and essential instrument to the rule of law and as a key element of good and modern governance, much academic debate surrounds the lack of transparency tools and methods in international trade agreements. Critics point out that the lack of transparency in the WTO and FTAs make such treaties less accessible to the public and less accountable to domestic democratic institutions.[5]

Adding to the academic debate, civil society and NGOs emphasise that transparency must include the right to be informed about the process of negotiations between the members and the final text of the agreement.[6]They also include the right of the civil society and the NGOs to be consulted on the issues being negotiated, particularly in terms of human rights, health,

environment and development.[7] As the number of FTAs, by both developed and developing states, is increasing, there are concerns in civil society about the lack of transparency in these trade agreements.[8] Nevertheless, the WTO and various FTAs have solved such civil society concerns, and these will be discussed in the following sections of this paper.[9]

2. Transparency in the World Trade Regime

It is important to note that the World Trade Organisation (WTO) is the guardian of the global trade regime.[10] Integral to the WTO is the reduction in trade barriers and restrictions between the WTO members (according to the principles of Most-Favoured-Nation (MFN)[11] and National Treatment (NT)).[12] To illustrate, no WTO member should be discriminated against by another member's trade regime. Nevertheless, Regional Trade Agreements (RTAs) between WTO members are an exception to the earlier mentioned principles. Under RTAs, the reduction in trade barriers applies only to the parties of the agreement and does not extend to the other WTO members. This exception is allowed under Article XXIV of the GATT for trade in goods, under Article V on General Agreement on Trade and Services (GATS) and under the Enabling Clause for developing countries.[13]

Returning to transparency, the GATT Agreement obliges members to set up a transparent method of regulation by requesting of the members certain minimum standards of transparency in their domestic administrative systems. To demonstrate, the GATT Agreement requires that members publishpromptly their regulations, laws, judicial decisions and administrative rulings before they are enforced so that interested parties are familiar of the changes.[14] Also, the members are required to administer their laws in a uniform, reasonable and impartial manner and must have or institute tribunals or procedures so that administrative actions can be subject to review and amendment.[15]

The objective of transparency in the WTO members' trade system is nevertheless to strengthen the effectiveness of the WTO agreements.[16] In general, trading partners and economic actors require information about a wide range of domestic policies that may affect the flow of trade and transactions across borders, and particularly between members.[17] The aim of transparency is to provide clarity for other WTO Members, and the predictability of economic factors. In addition, discussing the new measures prior to their being adopted can reduce the risk of conflict between states, as it provides both an opportunity to modify the measures to accommodate the interests of partners, and time for members to adjust.[18]

The WTO regime distinguishes between two types of Transparency: external and internal.[19]

2.1. Internal Transparency

The basic provision on Transparency is found in Article X of the GATT. The article calls members to publish in their domestic Gazette any measure, including any laws, regulations, judicial decisions or administrative rulings that relate to GATT measures, as well as any agreement affecting international trade policy.[20]

States are therefore obliged to make any information on their relevant laws, regulations and other policies available, and to notify interested parties of the relevant laws and regulations (and of any changes to them).[21]Members are also obliged to publish their international obligations that are mentioned in the 'schedule' attached to the general obligations of the WTO Agreements. The reason for such publications is that firms cannot navigate global markets without knowing what domestic tariffs and rules apply.[22]

Similar requirements for transparency are found in the other WTO agreements,23 namely, the Agreement on services (GATS) and the Agreement of Intellectual Property Rights (TRIPs).[24] The GATS in its Preamble outlines the concept of transparency: "[w]ishing to establish a multilateral framework of principles and rules for trade in services with a view to the expansion of such trade under conditions of transparency and progressive liberalization". Moreover, GATS Article III states that members are obligated to notify changes in laws, regulations, and administrative procedures for all measures affecting service trade that apply to committed sectors.[25]Furthermore, the GATS promotes transparency in services trade via several articles that contain publication and notification requirements.[26]

TRIPs article 63 insists that domestic intellectual property laws and decisions publicly be made available to the right owners, laws be notified to the Council for TRIPs for review,[27] and members be provided with information on certain cases of interest.[28]

The WTO Agreements require governments to notify new or modified trade measures fist at the national level first and second to the WTO Secretariat before implementing them. New anti-dumping or countervailing legislation, new technical standards affecting trade, changes to regulations affecting trade in services, and laws or regulations concerning intellectual property agreements all have to be notified to the appropriate body of the WTO.[29]

As a result of a number of proposals by several delegations,[30] the Council for Trade in Goods is looking to review Article X of the GATT 1994, covering "various means to improve transparency such as the installation of enquiry points, the introduction of an advanced ruling system, the more systematic consultation between customs administrations and traders and the establishment of effective appeal procedures".[31]

It is worth noting that various obstacles in a member market may occur, and thus that economic actors may in turn make alternative decisions, which might encourage the government to change its policies.[32] Therefore, the WTO monitors the notifications of its members through different WTO bodies before and after the measure takes effect. Monitoring and surveillance take place through The Policy Review Mechanism (TPRM), which aims to" achiev[e] greater transparency in, and understanding of, the trade policies and practices of Members".[33]

2.2. External Transparency

The importance of external transparency was realised after the Seattle Ministerial Conference Meeting (MCM), in which the NGOs inability to participate in and access information regarding the WTO's activities and negotiations was criticised and demonstrated against. Discussions took place after this at the WTO headquarters in Geneva, which have been praised for the series of improvements to WTO's practices for external transparency that took place.[34]

The General Council decided in 1996 to launch a WTO website so as to make more information about WTO activities publicly available and to ensure that public information, including WTO documents, was accessible on-line. Since the General Council Decision of 2002 on the Procedures for the Circulation and De-restriction of WTO Documents, more documents have been made available to the public at their time of circulation, and the small numbers of documents that are restricted are now made public more quickly.[35] All notifications by WTO Members are now posted on the WTO's website and are accessible to all.[36]

The WTO website therefore plays an important role in ensuring the transparency of WTO activities. With its regular postings of news, items, official documentsand videos, it acts as the best source of accessible information on the WTO.[37] In fact, such online access, has benefited governments of member states that are considered"developing" and "least-developed"as they are oftenunable to send large delegations to WTO meetings in Geneva, and do not have resident delegations there. The organisation is more open to the public than it has ever been and great efforts have been made to improve the participation of all members in the work of the organisation.[38]

2.3. Regional Trade Agreements in the GATT

As mentioned previously, Most-Favoured-Nation (MFN) treatment is a key principle of the multilateral trading system.[39] Nevertheless, if a member signed an FTA, this would violate the WTO's principle of equal treatment for all trading partners, pursuant to the (MFN) principle. To illustrate, a country entering into an FTA [40] or CU[41] might grant more favourable treatment to the participating states than to the other WTO members. However, GATT's Article XXIV allows regional trading arrangements to be set up as a special exception, provided certain strict criteria are met.[42] These conditions are subject to some degree of interpretation. Therefore, the WTO's consent to new free trade agreements is usually an issue of debate until a decision is made.

Similarly, Article V of the GATS provides for economic integration agreements in services. Other provisions in the WTO agreements allow developing countries to enter into regional or global agreements that include the reduction or elimination of tariffs and non-tariff barriers on trade among themselves.[43]

In terms of Transparency and FTA or CU agreements, Article XXIV, paragraph 7(a) requires any parties deciding entering into a CU or FTA to notify the other members of the WTO and provide them with details of the proposed arrangements. This would include plans and schedules for removing internal barriers and establishing common external barriers in the case of a customs union, within a reasonable time.

In the GATT years, these examinations were conducted by individual working parties.[44] On 6th of February 1996, the WTO General Council established the Regional Trade Agreements Committee (CRTA) following the Uruguay Round whose purpose is to examine regional groups and to assess whether they are consistent with the GATT rules.[45] The committee is also responsible for examining how regional arrangements might affect the multilateral trading system, and what the relationship between regional and multilateral arrangements might be.[46] The CRTA plays an important role in ensuring that regional agreements do not undermine the multilateral system. This mechanism improves the accuracy of notification requirements under article XXIV, the enabling Clause and Article V of the GATS.[47]

Furthermore, in 2006 the General Council also established a new transparency mechanism for Regional Trade Agreements (RTAs).[48] It has been noted that the adoption of the Transparency mechanism in December 2006 has improved the notification examination procedures of all RTAs, including those between developing countries.

Finally, once the WTO has been notified of an agreement, the WTO Secretariat prepares a detailed analysis of the RTA (called a Factual Presentation), which is used by other WTO members to examine and inspect the agreement according to WTO rules.

3. Transparency Provision in Various Free Trade Agreements

There are large and increasing numbers of Free Trade Agreements (FTAs) being negotiated that cover a variety of trade issues, most commonly occurring of which is the issue oftariffs on goods.[49] These agreements also cover tradeissues such as investment, services, intellectual property and competition. Trade Agreements areoften particularly important in the context of creating and establishing larger, more effective and more attractive markets. The WTO only permits member countries to enter into FTAs under certain conditions.[50]

Free Trade Agreements are tending increasingly to include transparency provision. An overview of existing provisions indicates that there is a clear trend towards expanding more transparency provisions in FTAs.[51] It has been argued that there is an increasing trend by parties in FTAs of including World Trade Organisation articles on transparency (WTO Plus clauses).[52] Moreover, parties might include some articles related to the transparency principle that might exceed the obligations contained in the WTO agreements (WTO-X clauses).[53]

Thus, these agreements (hereunder) highlight and illustrate some FTAs that contained transparency provisions,including FTAs in the European Union (EU), the United States of America (US) and Canada. The purpose of demonstrating such provisions is to provide Palestine with useful references for negotiating transparency provisions that might be included in any future Palestinian trade agreement.

3.1. European Union Free Trade Agreements

In the post-war period, the European Union (EU), which is an FTA in itself, developed the largest group of FTAs in the world.[54] The EU has signed various Free Trade Agreements with most countries and trade blocks.[55] It is believed that the EU has the largest number of FTAs of any major power, accounting for nearly half of those notified to the WTO and in force.

The European Commission adopted the 2006 Communication 'Global Europe:

Competing in the World', whichproposed a new generation of bilateral free trade agreements in Europe as a stepping stone for future trade liberalisation.[56] The aim of this Global Europe strategy is to promote Europe's commercial interests in a world market.

Furthermore, the EU has not used one singular model of FTA with all its trade partners. The agreements wereamended in each specific case to suit the EU and its partners.[57] Based on their success within Europe, the EU considers FTAs a means for promoting economic and political stability.[58] We can assume, by extension therefore, that the EU's desire is to promote regional integration in other regions of the world.[59]

EU arrangements in the EU's agreements with developed states, in terms of external and internal transparency, have (due to the similarities in the common domestic transparency mechanisms of the developed state partners) been rather flexible. Yet, the EU has used more elaborate political and economic conditionality in negotiating bilateral trade agreements with developing countries in order to promote the EU's own transparency rules. Such developing counties would otherwise have to harmonise their regulatory policies with EU standards.[60] Recently, the EU recommended a 'best endeavor' type of obligations with respect to the duty to publish legislative proposals in advance, and to provide information on and respond to questions pertaining to any existing or proposed measures.[61] A case in point, the FTA between the EU and Chilecontains a general reference to transparency, but specific details are to be developed by the parties in the course of the agreement.[62]

Coming back to the developed states, it has been noted that transparency provisions in the EU FTAs with developed states are limited to one general provision, following the GATT Article X requirements. For example, Canada is negotiating an FTA with the EU, but the proposed FTA contains provisions that are in line with Article X of the GATT. There is an emphasis within these provisions on the obligations of each party to inform the other of relevant legislative proposals and to allow the other party's interested persons to comment on such proposals.[63] Furthermore, the EU signed an FTA with South Korea[64] that is considered to be the first of the EU's new generation of FTAs, and is regarded as the most comprehensive FTA of the EU already in force.[65]

From a different perspective, more tough provisions of EU FTAs are included in more specific areas, such as those related to the Technical Barriers to Trade (TBT) and Sanitary and Phyto-sanitary Measures (SPS) obligations of the parties.[66] Subjects such as TBT are a priority for EU negotiators as TBT measures

can be used as barriers to market access for EU exporters to the partner's market. In this context, the EU requires greater clarity from its partners, and better administration of the various measures and standards set forth in the FTA.[67]Transparency can be improved through an effective notification system, as the public and private sectors of each party are informed of forthcoming changes in technical and SPS standards, and parties are given the opportunity responding to each other'squestions and concerns.This will therefore raise awareness among each party's public agencies and private parties of the rights and obligations of TBT and SPS.

In terms of civil society concerns, the EU has developed its own rules on the engagement and participation of the civil society in trade negotiations between the EU and other state parties. The EU requests that the other trade party work out their own ways of promoting and presenting the trade arrangements to their populations.[68]

3.2. United States Free Trade Agreements

The United States of America (USA) has signed a number of free trade agreements in the past few years. Transparency provisions have been a major component of all these agreements, reflecting the USA's commitment to this notion. To illustrate an example, the US- Bahrain FTA followed suit with most other US FTAs, where transparency commitments are required of both sides. Most importantly, this free trade agreement has brought transparency to the service sector.

Furthermore, Morocco has no previous regulatory transparency history. The US-Morocco FTA was therefore an enormous step for Morocco. General Transparency requirements are mentioned, as well as provisions for transparency in services, including financial, cross border and investment services. The basic transparency provisions require: the designation of a contact point for inquires, prompt publication, measures that each party proposes to adopt are published in advance "to the extent possible", and persons of both parties to have an opportunity to comment during the process. Interested persons are to be notified of any proceedings that take place during the drawing up of the regulations, and are to be allowed to have their cases presented before final administrative actions. The parties are also required to establish independent tribunals or procedures in order to guarantee prompt reviews of administrative actions.[69]

3.3. Canada Free Trade Agreements

Canada's FTAs with developing countries contain wide provisions and articles that relate to transparency. The Canada-Colombia FTA, for example, contains broad general regulatory transparency provisions,[70] as well as more detailed specific regulatory transparency provisions on telecommunications,[71] financial services,[72]e-commerce,[73] government procurement,[74]TBT and SPS measures.[75]

Nevertheless, Canada's FTAs with developed countries contain flexible provisions in terms of transparency. As a case in point, Canada – The European Free Trade Agreement (EFTA)[76] FTA has modest general transparency provisions related to the availability of information, the disclosure of information to authorities[77] and trade in services.[78] The Agreement establishes a 'best endeavor' type of obligation to provide information on any measure that might have an impact on trade in service or investment.[79]

The Canada-Jordan FTA stipulated the transparency process.[80] The agreement mentioned the process of publication, notification and administration of laws.[81] Furthermore, the Canada-Peru FTA mentioned (in Chapter 19) the procedures of transparency related to publications, notification and information.[82]

4. Transparency Chapters in Future Palestinian Trade Agreements

This section intends to highlight the best practice for any future Palestinian trade agreements in the area of transparency standards. It intends to encourage a coherent and consistent approach to the content of such agreements. The model is based on previous FTAs and on article X of GATT. These examples provide Palestine with useful references for negotiating an FTA transparency chapter. They are guidelines for the kind of provisions that might be included in such an agreement.

By illustrating the transparency provisions in the WTO and in various FTAs, the researcher believes that the Palestinians should add provisions related to transparency in any future bilateral trade agreements. To illustrate, the trade agreement should contain a few articles in a section that could be titled **Transparency**. Such a section should contain few provisions regarding: Enquiry Points, Publications, Notifications and the Provision of Information, the Review, Cooperation on Promoting Increased Transparency and finally, Specific Provisions.

To exemplify, in terms of Enquiry points it might be mentioned that each party designate one or more enquiry points to address enquires from interested persons, and each party shall make available on the internet and/or in print form information concerning procedures for making such enquiries.

The second article in the section could be titled Publications. Such an article could mention that each party shall ensure that its laws, regulations, procedures and administrative rulings covered by the agreement are promptly published or made available in such a manner that enables interested persons and the other Party to become acquainted with them. In addition, each party shall publish in advance, where possible, any measures that it proposes to adopt, and provide interested persons and the other party with a reasonable opportunity to comment on these proposed measures.

It is imperative to add an articlein the transparency section regarding the notification of information. For example, it could conclude that each party shall, to the best of their ability, notify the other party of any proposed or actual measure that the Party considers might affect the operation of this agreement or otherwise substantially affect the other Party's interests under this agreement. In addition, on the request of the other party, a party shall promptly provide information and respond to questions regarding any actual or proposed measure.

In addition, each party shall establish or maintain judicial, quasi-judicial or administrative tribunals or procedures for prompt review and correction of final administration actions regarding matters covered by the agreement. Every party, further, shall ensure that the parties of the proceedings are provided with the right to support or defend their positions.

Adding to this, a concluding article might state that the parties agree to cooperate, as much as possible, in bilateral, regional and multilateral aspects to promote international trade transparency. Finally, it should mention that in the case of conflict between the provisions in the transparency chapter and the specific provisions of other chapters, the latter should prevail.

5. Conclusion

To sum up, the core issues of the paper are the principle of transparency in world trade and in Free Trade Agreements, and how to promote the concept of transparency provisions in multilateral and bilateral trade agreements.

The objective of transparency is that individuals, traders, and companies involved in trade know as much as possible about the conditions of trade. It is therefore fundamentally important that regulations and policies be transparent. In the WTO, this is achieved in two ways: governments have to inform the WTO and the members of specific measures, policies or laws through regular notification; and the WTO conducts regular review of individual countries' trade policies through the Trade Policy Review.

In the context of bilateral trade agreements, transparency is an important factor for facilitating the efficient regulation of the issues negotiated under the FTA, and for providing public details of shared trade liberalisation commitments between the two parties. Transparency is an important condition of free market efficiency.

As the domestic level, transparency is where each party ensures that its laws, regulations, procedures, and administrative rulings of general application respecting any matter covered in the agreement are published or otherwise made available in such a manner as to enable interested persons and the other party of the agreement to become acquainted with them. Individuals and companies have the right to know as much as possible about the conditions of trade. It is therefore fundamentally important that regulations and policies are transparent and based on WTO transparent articles; mainly article X of the GATT.

Finally, using the various FTAs mentioned, this paper outlined some recommendations for transparency provisions that might strengthen any future Palestinian trade agreements.

Notes

1. Maria Perez-Esteve, 'WTO Rules and Practices for Transparency and Engagement with Civil Society Organizations,' World Trade Organization, Economic Research and Statistic Division, Staff Working Paper, ERSD-2012-14, 18th September 2012, p.4.
2. Carl-Sebastian Zoellner, 'Transparency: An Analysis of An Evolving Fundamental Principle in International Economic Law', *Michigan Journal of International Law*, 27 (2006): 579-628 (p.583).
3. Transparency in world trade refers to a number of acts, including how: a rule or a policy is developed domestically; the rule is enforced or a policy is implemented; the rule is published; the other Members of the WTO are notified of the new rule or a policy action; a notification is discussed in Geneva (the WTO headquarter); and the results of Geneva process are published. Transparency entails greater access to information as well as greater awareness on issues or policies.
4. WTO negotiations produce general rules that apply to all Members, and specific commitments made by individual members governments. The specific commitments are listed in documents called 'Schedules of Concessions', which reflect tariff concessions and other commitments that they have given in the context of trade negotiations.
5. LjiljanaBiukovic, 'Transparency Norms, The World Trade System and Free Trade Agreements: The Case of CETA,' *Legal Issues of Economic Integration*, 39 (2012) 93-107 (p.99).
6. Peter Van den Bossche, *The Law and Policy of the World Trade Organization: Text, Cases and Materials* (Cambridge: Cambridge University Press, 2005), p.154.
7. Jill JohnstoneNajaFelter and MarusLenzen, "Consumer Interests in Regulatory and Trade Policies", in *Trade and Regulatory Reform: Insights from Country Experience*, (Paris: Organization for Economic Co-Operation and Development (OECD), 2001) pp.47-50 (p.49).
8. Biukovic, supra, p.95.
9. Section 2.2 and 3.1.
10. On September 20, 1986, the contracting parties of the General Agreement on Tariffs and Trade of 1947 (GATT 1947) agreed to launch an eight round multilateral trade negotiation known as the Uruguay Round. More than seven years later they concluded the round with an entirely new treaty, without an amended version of the GATT 1974, the Agreement Establishing the World Trade Organization. The World Trade Organization (WTO) was established in 1 January 1995 and deals with the rules of trade between states at an international level. The WTO is an organization of governments that negotiate trade agreements for liberalising trade. http://www.wto.org/english/thewto_e/whatis_e/tif_e/fact1_e.htm (Accessed on 10, June 2013). The GATT agreement is now the WTO's principle agreement for trade in goods. Furthermore, the Uruguay Round also created new rules for dealing with trade in services, relevant aspects of intellectual property, dispute settlement, and trade policy reviews. See http://www.wto.org/english/thewto_e/whatis_e/inbrief_e/inbr03_e.htm. (Accessed on 10, June 2013).
11. Article 1 of the General Agreement on Trade and Tariffs (GATT), and Article 2 of the General Agreement on Trade in Service (GATS), Article 4 of the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs).
12. Article 3 of the GATT, Article 17 of GATS, and Article 3 of the TRIPs.
13. There are two major types of RTAs under the WTO, Free Trade Areas (FTA) and Customs Union (CU). Some countries may also sign interim agreements, which operate during a transition period, ultimately leading to the creation of CU or Free Trade Area. See article XXIV of the GATT. See LorandBartels, "'Interim agreements' Under Article XXIV GATT," *World Trade Review*, 8 (2009): 339-350 (p.339.)
14. Article X of the GATT.
15. Kevin Kennedy, "GATT 1994", in *The World Trade Organization: Legal, Economic and Political Analysis*, Volume I, Edited by Patric F.J. Macrory, Arthur E. Appleton and Michael G. Plummer, Springer Science and Business Media, Inc., New York, USA, 2005, pp.89-186 (p.132).

16. PadidehAla'I, "The WTO and the Anti-Corruption Movement," *Loyola University Chicago International Law Review*, 6 (2008): 259-278 (p.261). Mark Halle and Robert Wolfe, *A New Approach to Transparency and Accountability in the WTO*, Issue brief 06. Entwined Publisher, Stockholm, Sweden, 16/09/2010, p.3.

17. Robert Wolfe, "Regulatory Transparency, Developing Countries and the WTO", *World Trade Review*, 2 (2003): 157-182 (p.161).

18. Mark Halle and Robert Wolfe, supra, p.3.

19. External transparency enables citizens and civil society to notice and observe what international trade regulators, such as the WTO, are doing. In general the aim is to keep the public informed of the WTO's work and activities, including negotiations. Internal transparency refers to the practices for transparency between Member governments, whereby governments have to inform the WTO and Members of specific measures, policies or laws through domestic publication obligations and regular 'notification' to the WTO.

20. The WTO Transparency practice and principle that are impose at the WTO members are mentioned in Article X of the GATT 'Publication and Administration of Trade Regulations'. Article X states: "laws, regulations, judicial decisions and administrative rulings of general application … shall be published promptly" and that they be administered "in a uniform, impartial and reasonable manner" notably by independent administrative tribunals or procedures. Transparency, predictability and uniformity are the principle elements that are stipulated in the Article. See Article X of the GATT 1947. When Article X was drafted, it applied to the administration of customs rules at the border. Nowadays, these requirements have been extended to domestic policy. Peter Van den Bossche, supra, p.152.

21. For Internal Transparency see Peter Norgaard Pedersen, "The WTO Decision-Making Process and Internal Transparency", *World Trade Review*, 5 (2005): 103-131.

22. Mark Halle and Robert Wolfe, supra, p.4.

23. WTO Agreements mandate at least four levels of transparency: a) publication of laws and regulations; b) notification of new measures to trading partners; c) enquiry points for trading partners; and d) independent administration and adjudication. The Agreements require publication of all legal requirements affecting trade in sufficient time for anyone one affected by the rules to know about them before they come into force, both to allow time to comment and time to prepare to take advantage of the new opportunities created. See Wolfe (2003), p.3.

24. Sherry M. Stephenson, "Regional Versus Multilateral Liberalization of Services", *World Trade Review*, 1 (2002): 187-209 (p.190). Terry Collins-Williams and Robert Wolfe, "Transparency as a Trade Policy Tool: The WTO's Cloudy Windows," *World Trade Review*, 9 (2010): 551-581 (p.556).

25. Article III of the GATS.

26. Articles V, VI, VII, VIII, and IX of the GATS.

27. The Council of TRIPs is charged with monitoring members' compliance with TRIPS obligations. Articles 68 of TRIPs.

28. Articles 63(1-3) of the TRIPs. See Thomas E. Volper, "TRIPS Enforcement in China: A Case for Judicial Transparency", *Brooklyn Journal of International Law*, 33 (2007): 309-346 (p.319).

29. Understanding the WTO, Fifth Edition, Geneva: WTO, 2010a, p.53.

30. Canada (G/C/W/379), the European Communities (G/C/W/363), Japan (G/C/W/376), and Korea (G/C/W/377). The United States (G/C/W/384) contributed an overview of mechanisms used by its authorities in ensuring transparency.

31. WTO, 'Report (2002) of the Council for Trade in Goods,' World Trade Organization:

G/C/W/433, 12 November 2002. WTO, 'Review, Clarification and Improvement of GATT Articles V, VIII and X – Proposals Made by Delegations,' World Trade Organization: G/C/W/434, 15 November 2002.

32. Mark Halle and Robert Wolfe, supra, p.4.

33. The creation in 1989 of the Trade Policy Review Mechanism (TPRM) as a means of monitoring compliance with the GATT Article X. See Trade Policy Review Mechanism (TPRM), WTO website. Also see Terry Collins-Williams and Robert Wolfe, supra, p.565.

34. See Simon A.B. Schropp, *Trade Policy Flexibility and Enforcement in the WTO: A Law and Economic Analysis*, (Cambridge: Cambridge University Press, 2009) p.95. Maria Perez-Esteve, supra, p.7.

35. WTO document WT/L/452 of 16 May, 2002.

36. Maria Perez-Esteve, supra, p.8. The notifications contain information about Members' trade policies and practices. It assists and provides the private sector enterprises with the stability and predictability needed for them to conduct their day-to-day activities. It also provides NGO's and the general public with information that can used to hold governments accountable for their actions.

37. Ibid. Recent figures on visits to the WTO website (14 million visits in 2011, averaging about 1.1 million per month) and feedback from users illustrate the website's importance as a tool for promoting openness about the WTO's activities to the wider public. However, the continuous efforts made by the Secretariat to make improvements to the website, through greater use of webcasts, podcasts, videos, and discussion forums, attests to the WTO's desire to enhance its communication with the wider public. By the end of 2011, approximately 149,000 individuals had registered with the contacts database to obtain regular email announcements on WTO news. This contact list is made up of academics, consultants, government officials and students with a particular interest in trade issues. The general public, companies, NGOs, and the academic community are able to keep up-to-date with the WTO's activities through the website and its email alert system which has 150,000 subscribers to date. See WTO website Survey.

38. Steve Charnovitz, "Transparency and Participation in the World Trade Organization," *Rutgers Law Review*, 56 (2004): 927-959 (p.939). See Florentino P. Feliciano, "The Order Public Dimensions of Confidentiality and Transparency in International Arbitration", in *Transparency in International Trade and Investment Dispute Settlement*, ed. by Junji Nakagawa (UK: Routledge, 2013) pp.15-29 (p.23). Maria Perez-Esteve, supra, p.4.

39. MFN treatment means that a lower customs duty offered by one member of the WTO to another country must be extended to all other members of the WTO.

40. A Free Trade Area is defined in Article XXIV, paragraph 8(b):"[a] free tradearea shall be understood to mean a group of two or more customs territories in which duties and other restrictive regulations of commerce [...] are eliminated on substantially all the trade between the constituent territories in products originating in such territories".

41. A Customs Union is defined in Article XXIV, paragraph 8(a):"[a] customs union shall be understood to mean the substitution of a single customs territory for two or more customs territories, so that Duties and other restrictive regulations of commerce [...] are eliminated with respect to substantially all the trade between the constituent territories of the union or at least with respect to substantially all the trade in products originating in such territories, and, [...] substantially the same duties and other regulations of commerce are applied by each of the members of the union to the trade of territories not included in the union".

42. Understanding the WTO, supra, p.64. In order for FTA or CU to be compatible with the WTO norms, the FTAs must meet four basic conditions.

    a. They should eliminate, rather than just lower, trade barriers on 'substantially all trade' between the signatories. Trade agreements, on other words, should not exclude too many sensitive products from liberalization. In particular this condition requires that no major sector be excluded from free trade.

    b. Implementation of the free trade agreements may well be gradual but liberalization must take place 'within a reasonable period of time'. This is now understood to mean that a transitional period 'should exceed ten years only in exceptional cases'.

    c. The agreement should exhibit reciprocal trade concessions among all the involved parties. This condition is implicit in the nature of free-trade agreements in that they are not one-sided

preferential concessions.

d. The free-trade agreement should not result in raising tariff towards the outside countries, and must be approved unanimously by all WTO members.

43. WTO members, in the Doha Round of Negotiations, have agreed that some of the existing WTO rules governing RTAs need clarification. WTO members formally adopted a new Transparency Mechanism for RTAs on 14 December, 2006. The mechanism established a standardised review process for all RTAs. See Maria Perez-Esteve, supra, p.64.

44. Paul J. Davidson, *The Legal Framework for RTAS/FTAS in the Asia-Pacific Region*, APEC study Centre Consortium Conference; Building an Asia-Pacific Economic Community, Jeju, Korea, May 22-25, 2005.

45. Ibid.

46. Understanding the WTO, supra, p.64.

47. Pursuant to the RTA transparency mechanism, members participating in new negotiations aimed at concluding an RTA, and those parties to a newly signed RTA, shall inform the WTO and provide the WTO with information about the agreement in the form of an "early announcement" (including the official name, scope, date of signature, foreseen timetable for the entry into force, etc.). Following entry into force and notification of the Agreement, the parties are required to provide substantial information about the agreement (such as tariff concessions under the agreement and MFN duty rates-for goods, trade or balance of payment statistics, GDP data or production statistics, etc.), so as to enable the Secretariat to prepare a factual presentation of the Agreement. Another important feature is the requirement that Members notify the Secretariat every time there is a change in their agreement and also provide a summary of implementation once the agreement is fully implemented. The mechanism also contains other modalities to facilitate the notification and transparency such as database on RTAs which makes publicly available information on all RTAs notified to the WTO. See Maria Perez-Esteve, supra, p.5.

48. WTO document WT/L/671, 18 December 2006. Ralph H. Folsom, Bilateral *Free Trade Agreements: A Critical Assessment and WTO Regulatory Reform Proposal*, Legal Studies Research Paper Series, Research Paper No. 08-070, University of San Diego, School of Law, USA, September 2008, p.11.

49. The Term *'Free Trade Agreement'* is often used to present both bilateral and regional trade deals. FTAs can be negotiated between two or more countries. However, for the purpose of the paper, the researcher focuses only on the FTAs that are signed between two countries. Under FTA, two or more countries minimally agree to eliminate tariffs, quotas, and preferences on most traded goods. Most of FTAs today also seek to liberalise trade in services, investment, and numerous other regulated areas of economic activity. At the same time, members of an FTA maintain their own tariffs, quotas and other non-tariff barriers vis-avis non-members. Raymond J. Ahearn, *Europe's Preferential Trade Agreements: Status, Content, and Implications*, Congressional Research Service 7-5700, R41143, March 3, 2011, p.1.

50. The specific conditions for satisfying consistency with the General Agreement on Tariffs and Trade (GATT)/WTO rules that are contained in Article XXIV of the GATT (now part of the WTO), or Article V of GATT's agreement that covers services (the WTO's General Agreement on Trade in Services (GATS)).

51. These provisions can be classified into three categories: a) general transparency provisions that call for the transparent administration of laws and regulations covered by the agreement; b) specific transparency provisions on goods-related requirements, mainly TBT-type requirements, but also SPS-type requirements in some agreements, and c) specific transparency provisions regarding domestic regulation affecting services trade. EvdokiaMoise, *Transparency Mechanisms and Non-Tariff Measures: Case Studies*, OECD Trade Policy Working Paper No. 111, Working Party of the Trade Committee, TAD/TC/WP(2010)4/FINAL, Organization for Economic Co-operation and Development (OECD), Paris, France, 18 March, 2011, p.9.

52. The 'WTO Plus' refers to a PTA that includes enhanced obligations relating to policy areas that are already covered by the WTO agreements, where parties undertake commitments that build on commitments they have already made at the multilateral lever (such as obligations concerning customs administration, Technical Barriers to Trade (TBT), sanitary and phyto-sanitary (SPS), trade remedies 'countervailing duty

and anti-dumping' services which fall under GATS Agreement, government procurement, state trading enterprises, state aid, and Intellectual Property Rights (IPR) that fall under TRIPs Agreement). Henrich Horn, Petros C. Mavroidis, and Andre Sapir, *Beyond the WTO? An Anatomy of EU and US Preferential Trade Agreements*,Bruegel Blueprint 7, 2009, p.12.

53. The 'WTO-X' designation indicates that the RTAs also establish obligations for its members in policy areas that are not included in the current WTO agreements (human rights, competition, labour market regulations, environmental laws, etc.). Henrich Horn, Petros C. Mavroidis, and Andre Sapir, Ibid, p.17.

54. The EU itself, initially established in 1957 as the European Economic Community, is the world's largest preferential agreement (the 28 members of the EU are: Austria, Belgium, Bulgaria, Croatia, Cyprus, the Czech Republic, Denmark, Estonia, Finland, France, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden, and the United Kingdom). http://europa.eu/legislation_summaries/institutional_affairs/treaties/treaties_eec_en.htm. (Accessed on 2 July 2013).

55. Europe's recently completed FTA with South Korea, and ongoing negotiations between EU and Canada over a comprehensive FTA. However, there are only a few remaining major developed countries that fall outside the EU's network of PTAs, including the USA, China, Japan and Australia. The reason for the delay to sign FTA is that these states would likely demand liberalisation of European agriculture and services, to which there is widespread opposition in Europe. See Raymond J. Ahearn, Supra, pp.4-12.

56. See http://trade.ec.europa.eu/doclib/docs/2006/october/tradoc_130376.pdf. (Accessed on 14 June 2013). The European Commission (EC) has the exclusive right to initiate trade policy proposals and is the EU's sole representative in trade negotiations. The EC takes instruction from its member states via the Council (The Council comprises ministers from the capitals of member states and is the formal body representing member states on European foreign and trade policy).

57. Stephen Woolcock, *European Union Policy towards Free Trade Agreements*, European Centre For International Political Economy (ECIPE) Working Paper, No. 03/2007, p.4.

58. Ibid.

59. As a result of the EU process for signing FTAs, the United States business community sector have created a more activist United States FTA policy, out of fear of losing export sales and market share to EU competitors who may be gaining more favourable access to larger foreign markets as a result of new FTAs. To illustrate an example, the EU signed an FTA with South Korea and Colombia while the US has not. It was believed that the implementation of these FTA might jurisprudence the US exporters to the Korean and Colombian Markets. U.S. Chamber of Commerce, *Trade Action-or Inaction: The Cost for American Workers and Companies*; September 15, 2009, p.2.

60. LjiljanaBiukovic, supra, p.98.

61. The 2006 Communication, 'Global Europe: Competing in the World,' from the European Commission proposed a new generation of bilateral free trade agreements as a stepping stone for future trade liberalization. See http://trade.ec.europa.eu/doclib/docs/2006/october/tradoc_130376.pdf. (Accessed on 14 June 2013).

62. See European Union-Chile Free Trade Agreement.

63. LjiljanaBiukovic, supra, p.101.

64. European Union-Korea Free Trade Agreement, Ch. XII "Transparency".

65. The Agreement contains chapters on trade and sustainable developments with substantive commitments on labour and environmental standards, a monitoring mechanism and a clause on enhancement of the dialogue with the civil society. See the European Union-Korea Free Trade Agreement.

66. Terry Collins-Williams and Robert Wolfe, supra, p.571.

67. For example, Article 4.4: technical regulations of the EU-Korea FTA obligating the regulators of the parties or standard-making bodies to give written reasoned response to these parties' submissions

or comments on the rules and requiring that each party shall ensure that economic actors and other interested persons of the other party are allowed to participate in any formal public consultative process concerning the development of technical regulations, on terms no less favourable than those accorded to is own legal or natural persons. See EU-Korea FTA (2002/979/EC) O.J. L/127, 14 May 2011.

68. A working document of the Committee on Civil Liberties, Justice and Home Affairs of the European Parliament (EP) pointed out the EP views the implementation of the principle of transparency in the EU institutions as a general principle of the EU legal order, particularly after the entry into force of Regulation No. 1049/2001 and the Lisbon Treaty. The Committee finds that the Lisbon Treaty transparency principle is also linked with the principles of civic participation and of good administration (EP, Council, Commission, the European Council, the European Central Bank and the Court of Justice). In addition, the Committee requests the EU institutions, particularly the Council and Commission, to establish a balance between transparency and effectiveness through an indirect transparency set-up for EU citizens through their parliamentary representatives. See EP Committee on Civil Liberties, Justice and Home Affairs, Working Document (1) on the Annual Report on public access to documents, 24 Jan. 2011, DT/854597EN.doc, at 2. Yves Bonzon, *Comparative Analysis of Transparency and Public Participation Mechanisms in Regional Trade Agreements and Other International Regimes*, EGDE Workshop, March 2008.

69. Also, see the US-Singapore and the US-Chile FTA. These agreements contain provisions similar to the US-Morocco Free Trade Agreements. Nevertheless, the Jordan-US FTA lacks the regular transparency measures that were sought in most other FTAs with the United States.

70. Canada-Columbia Free Trade Agreement, Chapter 19.

71. Ibid, article 1010.

72. Ibid, article 1111.

73. Ibid, article 1502.

74. Ibid, article 1407.

75. Ibid, articles 601-608, and 504, respectively.

76. The European Free Trade Agreement (EFTA) is an intergovernmental organisation set up for the promotion of free trade and economic integration to the benefit of its four Member States: Iceland, Liechtenstein, Norway and Switzerland. See http://www.efta.int/. (Accessed on 29 June, 2013).

77. Canada – European Free Trade Agreement (EFTA) Free Trade Agreement, article 37.

78. Ibid, article 12.

79. Ibid.

80. Canada-Jordan Free Trade Agreement, chapter 12.

81. Ibid, chapter 12 (Transparency), Articles 12.1-12.10.

82. Section A (Transparency), Articles 1901-1910 of the Canada-Peru FTA.

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