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A CLOSER LOOK AT THE DOCTRINE OF SEPARABILITY IN ARBITRATION

Ilijana Todorović*

Abstract

In the ever-growing business world impacted by globalization, many commercial contracts nowadays contain an arbitration clause. This article focuses on the history behind arbitration as an alternative method of dispute resolution and its penetration to the forefront of mechanisms for resolving commercial disputes—with focus on England, France, and the United States. The article also delves into some of the key questions related to the relationship between an arbitration clause and the underlying contract in which it is contained. And those are the infamous separability and competence-competence doctrines. The author's conclusion is that the efficiency of an arbitration clause is feasible only if its autonomy is entrenched and safeguarded from preventative and baseless court intervention. In that regard, the author addresses the consequences, current challenges, judicial and academic discourse, and the need for improvement when it comes to these two arbitral principles—all with the goal to provide contracting parties with forethought as to what to consider when drafting their contracts as to avoid unwelcome consequences.

Keywords

International Arbitration · Separability Doctrine · Competence-Competence Doctrine · Historic Overview · Issues of Jurisdiction.

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1. Introduction

An international arbitration agreement is, nearly unfailingly, handled as "separable" or "autonomous" from the underlying contract in which it is included.[1] The consequence of this supposal is conventionally known as the "separability doctrine" or, more precisely, the "separability presumption"—which is one of the conceptual and pragmatic bedrocks of international arbitration.[2] Various jurisdictions, be it common or civil law, have given the doctrine different definitions. Yet, its aim is constant within the context of international arbitration—to provide for the autonomy and judicial independence from the main contract in which it is contained.[3]

Whatever its definition, the separability presumption unquestionably carries crucial importance in international commercial arbitration. Namely, the same is, as mentioned above,[4] one of the underpinnings of the current legal regimes relevant to international arbitration agreements. Nevertheless, despite its pragmatic and expository significance, the separability presumption gives rise to many heated debates, particularly when it comes to the questions relating to the choice of law, contractual validity, and competence-competence.[5] Even more to the point, the issues—all of which will be given a closer consideration—encompass:

(1) the potential application of a different national law, or substantive legal rules, to the arbitration agreement other than to the underlying agreement;
(2) the potential legality of an arbitration agreement, regardless of the non-existence, illegality, or invalidity of the underlying contract;
(3) the potential validity of the underlying contract, notwithstanding the issues related to an associated arbitration clause; *and*
(4) the analytical groundwork for the competence-competence doctrine, which recognizes the jurisdiction of an arbitral tribunal to rule on its own jurisdiction.[6]

[1] Gary Born, *International Commercial Arbitration*, vol. 1 (Kluwer Law International, 2009), 311-312.
[2] Ibid.
[3] *Final Award in ICC Case No.* 8938, XXIVa Y.B. Comm. Arb. 174, 176 (1999).
[4] *See* Abstract, *supra* p. 3, para. 1.
[5] Born, *International Commercial Arbitration*, 312 (n. 3).
[6] Ibid., 313.

2. The Doctrine of *"Separability"* or *"Autonomy?"*

However undeterred by the aforementioned worth of the separability presumption, substantial ambiguities as to its basis, content, and impact still exist. Thus, for instance, the appropriate name of the separability doctrine is an ongoing puzzlement and varies across different legal systems.[7] Common law jurisdictions, on one hand, have talked about the "separability" or "severability" doctrine, emphasizing its *contractual origin* and the perspective of arbitration agreement being *severable* from the underlying contract.[8]On the other hand, civil law jurisdictions have spoken of the "autonomy" and "independence" of the arbitration clause, arguably pointing out the role of the *outer legal regime* applicable to international arbitration agreements. This distinction in nomenclature in the civilian tradition also suggests a greater degree of *legal distance* between an arbitration agreement and the underlying contract, than the one that is proposed by the separability doctrine.[9]

The debate over the adequate label—"autonomy" or "separability"—does not, however, result in any considerable gain, particularly because both characterizations can be subjected to inexactitude.[10] Yet, though the distinction is one of degree rather than nature, many would agree that "separability" would be a more appropriate epithet, for the following reasons:

(1) it would be wrong to describe an arbitration clause as either wholly or necessarily "autonomous" or "independent" from the underlying contract when the former prevails to exercise the supportive function to the latter and is, thus, still closely related to it;
(2) it correctly places the focus on the *parties' intentions*, as a contractual manner, in forming the arbitration agreement rather than on *external legal rules* imposing a specific understanding of an arbitration agreement upon the parties; *and*
(3) the term "autonomy" is vague and indecisive as it can be used to express the independence of the arbitration clause from *any national law*, whereas the "separability" nomenclature denotes solely the separability of the arbitration agreement from *the underlying contract*, without indicating any autonomy that the arbitration clause may have in relation with national legal systems.[11]

[7] Ibid.
[8] Ibid., 313-314.
[9] *See* Judgment of 7 May, 1963, Ets Raymond Gosset v. Carapelli, JCP G 1963, II, 13, ¶405 (French Cour de cassation civ. 1c), 354-404.
[10] Born, *International Commercial Arbitration*, 314 (n. 3).
[11] Ibid., 315-316.

3. Historic Origins and Evolution of the Separability Doctrine

Historically, some jurisdictions were reluctant to fully recognize agreements to arbitrate future disputes. But even the Roman law, written 1,500 years ago, provided that the arbitration clause was a separate contract (*promisum*) which could not be enforced unless conglomerated with another contract—to produce a *com-promisum.*[12] This position remained in force until the early twentieth century, particularly in England, France, and the United States.[13]Despite the fact that the public policy of each of these three countries resembles the aspiration to encourage arbitration as a form of alternative dispute resolution, each nation has established a distinct legal framework in response to this objective. The course and measure of growth and the status of arbitration law within each country goes hand-in-hand with the goal to incentivize the use of arbitration agreements and to augment that nation's rank and prominence as a favorable center for arbitration.[14] Hence, though the doctrine of separability is now an accepted principle in almost all advanced arbitral jurisdictions, its application still continues to vary—even within jurisdictions—under circumstances in which the container agreement is argued never to have come into existence at all.[15]

3.1 England

In English law, the doctrine of separability was established in the 1698 Arbitration Act which provided that arbitration clauses can be made rules of court if the parties had so chosen.[16] Violating contractual terms would not, at the time, bring about the contempt of court.[17] However, this was to be very short-lived as it was dismissed by the cataclysmic decision in *Kill* v. *Hollister*[18] in 1746, where it was found that the parties' agreement to arbitrate cannot "oust this Court" of its jurisdiction.[19] The courts' jealousy regarding their own jurisdiction resulted in a major setback as the arbitral clause was reduced to a "standard contractual term" which the courts were stubbornly refusing to enforce.[20] The reason behind the refusal of the only so-reduced contractual term (other contractual terms were not approached in the identical manner) was exactly its jurisdictional nature—"a form of separability in itself."[21]

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[12] Ibid., 321.
[13] Ibid.
[14] Janet A. Rosen, "Arbitration under Private International Law: The Doctrines of Separability and Competence de La Competence," *Fordham Int'l LJ* 17 (1993): 616-617.
[15] Alan Redfern and Martin Hunter, *Law and Practice of International Commercial Arbitration* (Sweet & Maxwell, 2004), 164.
[16] Adam Samuel, "Separability of Arbitration Clauses-Some Awkward Questions about the Law on Contracts, Conflict of Laws and the Administration of Justice," *Arbitration and Dispute Resolution Law Journal* 36 (2000), http://www.adamsamuel.com/separabi.pdf.
[17] Ibid.
[18] Kill v. Hollister, 1 Wils. K.B. 129, 95 Eng. Rep. 532 (1746).
[19] Samuel, "Separability of Arbitration Clauses," (n. 18).
[20] Ibid.
[21] Ibid.

Still, in 1942, the decision reached by the House of Lords[22] in *Heyman*[23] re-instated the doctrine of separability by holding that an arbitration agreement included in a written contract may survive the termination of the contract. The question whether the discharge by a fundamental breach of the container agreement simultaneously discharged the arbitration clause as well was unanimously answered in the negative.[24] Half a century later, in the famous 1992 *Harbour Assurance*[25] decision, English judges expressly recognized the separability principle as part of English law. They stated, *inter alia*, that the said doctrine gives an arbitral tribunal the jurisdiction "to determine the validity or invalidity of the relevant contract provided that the arbitration clause itself was not directly impeached."[26] In that regard, even a successful attack on the contract's validity would not—in and of itself—negate the arbitral tribunal's jurisdiction unless the arbitral clause is thereby impugned.[27] This scheme eliminated the conundrum (not to say the absurdity) of the process as arbitrators were allowed to examine the issues of legality and were empowered to render the container agreement void for illegality without thereby eradicating their own jurisdiction so to render. The doctrine was subsequently enacted by Section 7 of the Arbitration Act 1996.[28]

3.2 France

England was not the only country facing anti-arbitration developments. Following a boom of the excitement in the revolutionary aftermath, the 1804 Napoleonic Code outlawed the enforcement of arbitral clauses.[29] This judicial hostility toward arbitration clauses had been impacting French domestic arbitration law for two centuries.[30] However, in the landmark 1963 *Gosset*[31] decision, the *Cour de Cassation*[32]

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[22] "House of Lords History," UK Parliament, 2021, https://www.parliament.uk/business/lords/lords-history/.
[23] Heyman v. Darwins, [1942] 1 All ER 337.
[24] Samuel, "Separability of Arbitration Clauses," (n. 18).
[25] Harbour Assurance Co. Ltd. v. Kansa General International Insurance Co. Ltd., [1992] 1 Lloyd's L.Rep. 81.
[26] *"Separability of Arbitration Agreements,"Arbitration Law Monthly,* October 2005, https://www.i-law.com/ilaw/ doc/view.htm?id=35136.
[27] Ibid.
[28] Ibid.
[29] Samuel, "Separability of Arbitration Clauses," (n. 18).
[30] Philippe Leboulanger, "The Arbitration Agreement: Still Autonomous?," in *International Arbitration 2006: Back to Basics?,* ICCA Congress Series, no. 13 (International Arbitration Congress, Alphen aan den Rijn: Kluwer Law International, 2007), 3–31.
[31] Cour de Cassation, 7 May 1963 (Ets. Raymond Gosset v. Carapelli), Juris Classeur Périodique, Ed. G., Pt. II, No. 13405 (1963).
[32] "Présentation," Cour de cassation, n.d., https://www.courdecassation.fr/#:~:text=La%20Cour%20de%20cassation%20est,interpr%C3%A9tation%20uniforme%20de%20la%20loi. As noted on the website of the *Cour de Cassation*,

re-introduced the doctrine of separability by ruling that the arbitration agreement, in international disputes, is separable from the main contract and judicially autonomous.[33] More precisely, the Court reasoned that, in cases of international arbitration, an arbitration agreement—be it in a separate document or as a part of the underlying contract—is always, absent exceptional circumstances, completely autonomous.[34] The Court went on to declare that the autonomy of the arbitral clause in an international contract (*Gosset* involved a contract between a French and an Italian company) is not affected even when the underlying contract may be invalid.[35]

The *Cour de Cassation* upheld this ruling in the subsequent cases shortly after *Gosset*, in 1968 and 1971.[36] About a decade later, in response to two executive degrees[37] of 1980 and 1981, the French Parliament promulgated the Nouveau Code de Procédure Civile,[38] Book IV of which expressly regulates all aspects of domestic and international arbitration. This was an indication that the French Parliament worked towards incentivizing settlement of disputes in international trade. As a fruit of combined efforts by the legislature and the judiciary—where French judges opted to restrict their dominion over international arbitration matters—France emerged as an occupier of a highly prominent position in the realm of international commercial arbitration.[39] What is more, not only was international arbitration afforded great deference in France, but the arbitration was generally encouraged, and it emerged as the most dynamic aspect of the French contract law.[40]

Be that as it may, it is still worth mentioning that this great advantage afforded to arbitration in France was by no means absolute or all-encompassing. Namely, despite the *in dubio pro arbitrarium*[41] approach that the French legal system has adopted in terms of honoring arbitral clauses, the same could—albeit on rare occasions—invoke the application of the French law. And the substantive provisions of the French domestic law provided for the non-arbitrability of a contractual subject matter in

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> La Cour de cassation est la plus haute juridiction de l'ordre judiciaire français. Siégeant dans l'enceinte du palais de justice de Paris, la juridiction suprême a pour mission de contrôler l'exacte application du droit par les tribunaux et les cours d'appel, garantissant ainsi une interprétation uniforme de la loi.

[33] Leboulanger, "The Arbitration Agreement: Still Autonomous?" (n. 32).
[34] Rosen, "Arbitration under Private International Law," 639-640 (n. 16).
[35] Ibid.
[36] Ibid., 641-642.
[37] Decree No. 80-354 of May 14, 1980, (1980) Journal Officiel de la RépubliqueFrançaise ("J.O.") 1238, (1980) D.S.L. 207 (Fr.) - established the extensive review of domestic arbitration law, while Decree No. 81-500 of May 12, 1981, (1981) J.O. 1380, (1981) D.S.L. 222 (Fr.) – set in motion a change in international arbitration rules. *See* Rosen, "Arbitration under Private International Law" (n. 16).
[38] Rosen, "Arbitration under Private International Law," 643-644 (n. 16).
[39] Ibid., 637-638.
[40] Ibid., 637.
[41] "When in doubt, for the [favor] arbitration."

instances when "court intervention is regarded as indispensable."[42] Those instances are mostly the ones that entail public policy matters, such as issues related to naturalization, immigration, tax, and administrative concerns.[43] Non-arbitrable cases also involve political legislation, such as laws regarding price controls, freedom of commerce, or economic organization of society.[44]

3.3 The United States

While the judiciary in the United Stated had been treating arbitration with a certain degree of hostility prior to the enactment of the Federal Arbitration Act (FAA) (9 U.S.C. §§ 1-16) in 1925, the development of federal public pro-arbitration policy supervened the passing of the FAA.[45] The assurance that the private contracts will be enforced seems to have been the main stimulus behind the approval of and support for the arbitration process. That is why the United States Congress, in its attempt to surmount judicial resistance to arbitration, passed the FAA. The FAA, however, was silent on the issue of separability.[46] The FAA provisions are said to apply to the U.S. interstate and transnational commerce, meaning that the international commercial arbitration agreements may very well fall under the scope of the FAA.[47] Still, the international commercial arbitration agreements may also invoke the application of the New York Convention, discussed *infra,*[48] which was codified into the U.S. law almost 50 years after the FAA.[49] In any event, the FAA provides for the enforcement of written arbitral clauses by incorporating instruments with which courts may rule on issues involving both the arbitrability and validity of the arbitral clause.[50] Hence, pursuant to the FAA, a written agreement contained in a commercial contract is a "valid, irrevocable and enforceable agreement."[51]

A pro-arbitration initiative in the United States became notable in subsequent case law discussed by the U.S. courts. Specifically, the initial *favor arbitrandum* principle was established in the 1967 *Prima Paint*[52] case, a landmark decision credited with making the separability doctrine a part of the U.S. law by holding that separability was a principle of federal law applicable in state courts. The case involved a Maryland corporation, Prima Paint, which purchased a paint manufacturing business from a New

[42] Rosen, "Arbitration under Private International Law," 647 (n. 16).
[43] Ibid., 647-48.
[44] Ibid., 648.
[45] Ibid., 617-18.
[46] Leboulanger, "The Arbitration Agreement: Still Autonomous?" (n. 32).
[47] Rosen, "Arbitration under Private International Law," 619 (n. 16).
[48] *See* Sec. IV(2) The New York Convention and the FAA: Gap and Overlap.
[49] Rosen, "Arbitration under Private International Law," 619, 625 (n. 16).
[50] Ibid., 619.
[51] 9U.S.C. §2 – *Validity, irrevocability, and enforcement of agreements to arbitrate:*"[A] written [arbitration] provision in ... a contract evidencing a transaction involving commerce ... shall be valid, irrevocable, and enforceable."
[52] Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 U.S. 395 (87 S.Ct. 1801, 18 L.Ed.2d 1270).

Jersey corporation, Flood & Conklin. The parties signed a Consulting Agreement which stated that Flood & Conklin were to advise Prima Paint on the questions of production, manufacturing, sales, and service of paint products over a period of six years.[53] Prima Paint, the plaintiff, subsequently claimed that the execution of the Consulting Agreement, in which the arbitration clause was incorporated, was fraudulently induced by false representations related to the defendant's financial condition.[54]

The U.S. Supreme Court found that the agreement in question involved interstate commerce and it, accordingly, applied the FAA (federal law) to hold that arbitration clauses can be *separable* from the contracts in which they are included.[55] Since the plaintiff here challenged the contract *generally* and not the arbitration clause *specifically*, the fact that the underlying agreement was fraudulently induced did not, without more, invalidate the arbitration clause.[56]However, the Court did point out that the outcome might have been different had the arbitration clause itself been claimed to be fraudulently induced. So, because the fraudulent inducement claim challenged the entire contract, rather than the arbitration clause itself, the Court concluded that the claim should be adjudicated by the arbitrators.[57] Nonetheless, it should be noted that the doctrine of separability as laid down by the U.S. Supreme Court in *Prima Paint* is a "rule of national substantive law" and was decided only with reference to the FAA, thereby giving force to the U.S. public policy of favoring arbitration agreement subject to the FAA.[58]

The FAA, now a ninety-plus-year-old statute, has been attacked by many legal scholars who think it is time for a complete reformulation of federal arbitration law, whether on interstate or international level.[59] In support of their claim, these legal experts allege that the FAA has been constantly disregarded by the U.S. Supreme Court, "which has recast arbitration in an activist set of cases that largely ignore careful legislative history and even the explicit wording of the FAA."[60] Notably, most of the critics are of the opinion that the Supreme Court has generally been unsuccessful in its pursuit to clarify and perfect the arbitration doctrine by employing the practice of setting forth rules in individual cases.[61] Legal experts also hold the Congress at fault for failing to address the issues of "age, fragmentation, and omission" that influenced the

53 Ibid., 397.
54 Ibid.
55 Ibid., 400.
56 Rosen, "Arbitration under Private International Law,"623-624, 627 (n. 16).
57 Paul T. Milligan, "Who Decides the Arbitrability of Construction Disputes," *Constr. Law.* 31 (2011): 24.
58 Edward Brunet et al., *Arbitration Law in America: A Critical Assessment* (Cambridge University Press, 2006), 92-93.
59 Ibid., 1.
60 Ibid.
61 Ibid.

implementation of federal arbitration law.[62] Put briefly, scholars argue for a new and improved FAA to take a form of legislation instead of a set of federal judicial cases.

4. The New York Convention and the Separability Doctrine

4.1 Overview

The *Convention* on the Recognition and Enforcement of Foreign Arbitral Awards, also known as the New York Convention, is the most momentous international treaty concerning international commercial arbitration.[63] Despite the fact that it may be very well regarded as a major step in the progress of arbitration as a method for resolving international disputes, the application of the Convention has not gone without functional complications and hardships.[64] This is not solely a result of a lack of coherent interpretation of the Convention by the courts of diverse signatory states, but also a consequence of reality that the Convention—adopted about six decades ago—is now starting to reveal its dotage.[65-66] Once again, in spite of that, it is still pivotal to remark that no other convention post 1958 has had the same impact in the shaping of modern commercial arbitration.[67]

For present concerns, what becomes relevant is that the 1958 New York Convention makes no direct reference to the principle of separability.[68] To begin with, Articles II(1)[69] and (2)[70] of the Convention merely grant the arbitration clause a title of an "agreement" but do not pose the requirement that such agreements be considered "separable." Conversely, arbitration agreements are understood to be "separate" agreements by virtue of the said Articles primarily because they introduce certain legal

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[62] Ibid.
[63] Redfern and Hunter, *Law and Practice of International Commercial Arbitration*, 69 (n. 17).
[64] Ibid.
[65] *See* Sec. III(3) The United States, at p. 13.
[66] Redfern and Hunter, *Law and Practice of International Commercial Arbitration*, 69 (n. 17).
[67] Ibid.
[68] Aiste Sklenyte, "International Arbitration: The Doctrine of Separability and Competence-Competence Principle," *The Aarhus School of Business*, 2003, 1–3.
[69] The New York Convention, Article II(1):

> Each Contracting State shall recognize an agreement in writing under which the parties undertake to submit to arbitration all or any differences which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not, concerning a subject matter capable of settlement by arbitration.

[70] The New York Convention, Article II(2):

> The term 'agreement in writing' shall include an arbitral clause in a contract or an arbitration agreement, signed by the parties or contained in an exchange of letters or telegrams.

rules which do not relate to the underlying agreement (e.g. the requirement for the agreement to be in writing, to have substantive validity, and so on).

Additionally, Article V(1)(a)[71] of the Convention speaks of the separable nature of the arbitration agreement by providing an exception to the enforceability of arbitral awards in cases when the arbitration agreement is invalid under "the law to which the parties have subjected it" or "where the award was made." The said clause transparently envisages the application of particular national law to the arbitration agreement itself. Moreover, it stands on the contention that international arbitration agreements are understandably separate from the main contract and are, therefore, open to be dealt with by different national laws and legal rules than the underlying contract.[72]

The question thus arises as to whether the stated Articles acknowledge the separability doctrine. Conclusions, needless to say, deviate to a great extent. While some legal scholars are of the opinion that the Convention is *silent* as to the subsistence of the separability doctrine, others share the belief that the doctrine is *impliedly* adopted by the Convention.[73] As revealed by Born, both of these thoughts are mistaken, for the Convention is neither silent nor does it adopt the said doctrine. Rather, it accepts that arbitration agreements can be—and usually are—separate agreements which, accordingly, call for application of different rules (of validity and choice-of-law rules) than the main contract.[74]

Treating arbitration clause and container agreement as presumptively separate from one another is not, as elaborated by Born, *required* by the Convention.[75] Instead, the drafters of the Convention accepted this presumption of separability in order to reflect what they understood commercial parties' intentions and expectations to be.[76] More precisely, the drafting of the Convention was guided by the thought that parties may, and usually do, intend their arbitration agreements to be separable. Hence, the Convention was designed to offer specialized legal rules applicable only to arbitration agreements. So, even though the Convention, pursuant to the requirement laid down in

[71] The New York Convention, Article V(1)(a):

> Recognition and enforcement of the award may be refused, at the request of the party against whom it is invoked, only if that party furnishes to the competent authority where the recognition and enforcement is sought, proof that the parties to the agreement referred to in article II were, under the law applicable to them, under some incapacity, or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of the country where the award was made.

[72] Born, *International Commercial Arbitration*, 318 (n. 3).
[73] Ibid.
[74] Ibid., 319.
[75] Ibid.
[76] Ibid.

Article II(1), does not *demand* separability of arbitration agreements, it *stipulates recognition* of agreements to treat arbitration clauses as separable.[77]

4.2 The New York Convention and the FAA: Gap and Overlap

Establishing homogenous standards for judicial review of arbitral awards bolsters the predictability, uniformity, and adeptness of the international arbitration regime. The New York Convention sets forth a systematic revision for enforcement proceedings in signatory jurisdictions, but it fails to devote effort to instituting standards for vacatur.[78] In instances when both vacating and enforcing an arbitral award are at issue before the rendering jurisdiction, the solidity and compactness of the relevant legal tools are exceptionally significant as they relate to the gravity of vacatur.[79] When setting aside and enforcing proceedings within the United States, there is an interplay between the FAA and the New York Convention in a sense that the grounds for vacatur provided by the former are in no way identical with the enforcement exceptions under the latter.[80]

According to the decisions reached in *Rent-A-Center*[81] and *Hall Street*,[82] discussed *infra*,[83] Sections 4[84] and 10(a)[85] of the FAA have been interpreted to suggest that the arbitrator's decision on jurisdiction is not reviewable if so chosen by the

[77] Ibid.
[78] Graves and Davydan, "Competence-Competence and Separability-American Style," 168 (n. 2).
[79] Ibid.
[80] Ibid.
[81] Rent-A-Center, Est, Inc. v. Jackson, 130 S.Ct. 2772 (2010).
[82] Hall Street Assoc v. Mattel, Inc., 552 U.S. 576 (2008).
[83] *See* Sec. V(1) Overview, *infra* p. 26, para. 2.
[84] 9 U.S.C. § 4 - *Failure to arbitrate under agreement; petition to United States court having jurisdiction for order to compel arbitration; notice and service thereof; hearing and determination:*

> A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any United States district court which, save for such agreement, would have jurisdiction under title 28, in a civil action or in admiralty of the subject matter of a suit arising out of the controversy between the parties, for an order directing that such arbitration proceed in the manner provided for in such agreement [...]

[85] 9 U.S.C. § 10(a) – *Same; vacation; grounds; rehearing:*

> (a) In any of the following cases the United States court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration—
> (1) where the award was procured by corruption, fraud, or undue means;
> (2) where there was evident partiality or corruption in the arbitrators, or either of them;a
> (3) where the arbitrators were guilty of misconduct in refusing to postpone the hearing,upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced; or
> (4) where the arbitrators exceeded their powers, or so imperfectly executed them that amutual, final, and definite award upon the subject matter submitted was not made.

parties.[86] If we suppose that a U.S. court has to decide whether or not to enforce and vacate a non-domestic award challenged on the ground of invalidity of the arbitration agreement containing such parties' choice, the problem becomes self-evident.[87] While on one hand Article V(1)(a) of the New York Convention unambiguously provides for a judicial review of such a challenge, Section 10 of the FAA—on the other hand—does not.[88] Even more to the point, bearing in mind that the FAA Section 10 provisions are *exclusive*, the courts are apparently not allowed to enforce the exceptions to vacate the award provided by the New York Convention.[89] Consequently, in cases when the validity of the arbitration agreement is disputed, an award cannot be vacated *but* the courts may refuse to enforce it.[90] Therefore, at least when it comes to challenging the arbitrators' jurisdiction, the FAA and the New York Convention leave a substantial lacuna which gives rise to quixotic outcomes. This is so because, with no vacatur apparatus, a party challenging arbitral jurisdiction must conceivably fight enforcement in more than one jurisdiction.[91]

The existence of any efficacious "fill in the gap" practices that could be employed for remedying or avoiding this issue remains an open question as reconciling these two instruments—the FAA and the New York Convention—may open the archetypal "Pandora's box" to arbitral awards' review on the merits.[92] Nonetheless, at first glance, it seems like the parties themselves could be able to avoid this issue by expressly choosing *state* arbitration law since eight states in the U.S. have adopted the UNCITRAL Model Law as their international arbitration statutes (California, Connecticut, Florida, Georgia, Illinois, Louisiana, Oregon, and Texas).[93] But, since Chapter VII Article 34 of the Model Law on Recourse Against Award is identical to the New York Convention enforcement exceptions—and thus provides the same standard of review—*and* since only four out of these eight states adopted the Model Law in its entirety (while others opted out of the Chapter VII which deals with the vacatur), state law is highly unlikely to be able to productively fill the gap.[94]

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[86] Graves and Davydan, "Competence-Competence and Separability-American Style," 170 (n. 2).
[87] Note: If a party alleges that the dispute is not arbitrable, the courts—rather than the arbitrator—would determine the issue of arbitrability; *i.e.,* unless the parties *clearly and unmistakably* provide otherwise, the question of whether the parties had agreed to arbitrate is to be decided by the court, not the arbitrator. For more information, *see* B.M. Harges, *The Handbook on Louisiana Alternative Dispute Resolution Laws* (Esquire Books, 2011), 375. Citing *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938 (1995).
[88] Graves and Davydan, "Competence-Competence and Separability-American Style," 170 (n. 2).
[89] Ibid., 170-71.
[90] Ibid.
[91] Ibid.
[92] *Status: UNICTRAL Model Law on International Commercial Arbitration (1985), with amendments as adopted in 2006.* United Nations Commission on International Trade Law, https://uncitral.un.org/en/texts/arbitration/ modellaw/commercial_arbitration/status.
[93] Graves and Davydan, "Competence-Competence and Separability-American Style,"at 172.
[94] Ibid.

Moreover, pursuant to the statutory interpretation of Chapter 2 Section 202[95] of the FAA and Article I(1)[96] of the New York Convention, U.S. courts would usually apply the latter to disputes of international nature arbitrated in the United States.[97] While Section 10 of the FAA, as previously mentioned,[98] has exclusive application for setting aside a proceeding, Article V of the New York Convention still applies to the enforcement—even in cases when the same is sought in the United States.[99] Unlike the UNCITRAL Model law which mirrors the non-enforcement grounds under the New York Convention, the FAA grounds for vacatur do not. Therefore, supposing, as before, that a U.S. court would have to decide whether or not to enforce and vacate a non-domestic award, before making such a determination—the court would have to mitigate the FAA Section 10 vacatur provisions with the non-enforcement provisions of the New York Convention.[100] The way in which the courts have opted to rectify the discrepancies between these two arbitral instruments is to interpret the FAA and the New York Convention as having an *"overlapping coverage"* to the extent they are not in conflict with one another.[101]

When it comes to this "overlap," after examining the legislative histories of both the FAA and the New York Convention, the court in *Lander v. MMP*[102] reached the conclusion that there is nothing to suggest that the New York Convention was meant to have exclusive application.[103] On the contrary, since Article VII(1)[104] of the New York

[95] 9 U.S.C. § 202 – *Agreement or award falling under the Convention:*

> An arbitration agreement or arbitral award arising out of a legal relationship, whether contractual or not, which is considered as commercial, including a transaction, contract, or agreement described in section 2 of this title, falls under the Convention. An agreement or award arising out of such a relationship which is entirely between citizens of the United States shall be deemed not to fall under the Convention unless that relationship involves property located abroad, envisages performance or enforcement abroad, or has some other reasonable relation with one or more foreign states. For the purpose of this section a corporation is a citizen of the United States if it is incorporated or has its principal place of business in the United States.

[96] The New York Convention, Article I(1):

> This Convention shall apply to the recognition and enforcement of arbitral awards made in the territory of a State other than the State where the recognition and enforcement of such awards are sought, and arising out of differences between persons, whether physical or legal. It shall also apply to arbitral awards not considered as domestic awards in the State where their recognition and enforcement are sought [...]

[97] Graves and Davydan, "Competence-Competence and Separability-American Style," 169 (n. 2).
[98] *See* Sec. IV(2) The New York Convention and the FAA: Gap and Overlap, *supra* p. 19.
[99] Graves and Davydan, "Competence-Competence and Separability-American Style," 169 (n. 2).
[100] Ibid., 169, 170.
[101] Ibid.
[102] Lander Co. v. MMP Invs, Inc. (Lander II), 107 F.3d at 476, 478 (7th Cir. 1997).
[103] Lander II, 107 F. 3d at 481.
[104] The New York Convention, Article VII(1):

Convention provides that it will not deprive any interested party of any right to avail himself of an arbitral award as long as that is permitted by the law of the country where the award is sought to be relied upon, parties are essentially at liberty to choose either Article I of the New York Convention, Section 202 of the FAA, or both in seeking to have their arbitral awards enforced.[105]

The application of the New York Convention to a wider range of non-domestic awards brings about several advantages, including those related to a more pliable and efficacious enforcement. Three of such advantages stand out. First, the New York Convention invokes independent federal jurisdiction.[106] Second, whereas under the FAA[107] the enforcement proceedings should be initiated within a one-year period, the New York Convention allots the parties a three-year statute of limitations within which to act.[108] And third, while the FAA restricted the courts to compel arbitration only "within a district," the New York Convention permits the courts to order parties to arbitrate either in or outside of the United States' territory.[109] Therefore, in summary, by assigning the New York Convention a broader application, American parties will be given broader legal possibilities (both in local and foreign jurisdictions), which will in turn make the United States a more prominent arbitration forum. Foreign parties, of course, would find this appealing and would opt to arbitrate their disputes in the United States.[110]

> The provisions of the present Convention shall not affect the validity of multilateral or bilateral agreements concerning the recognition and enforcement of arbitral awards entered into by the Contracting States nor deprive any interested party of any right he may have to avail himself of an arbitral award in the manner and to the extent allowed by the law or the treaties of the country where such award is sought to be relied upon.

[105] Lander II, 107 F.3d at 481-82.

[106] Christina Cheung, "The Enforcement Methodology of Non-Domestic Arbitral Awards Rendered in the United States & Foreign-Related Arbitral Awards Rendered in the People's Republic of China Pursuant to Domestic Law and the New York Convention," *Santa Clara Journal of International Law* 11, no. 1 (December 30, 2012): 246.

[107] 9 U.S.C. § 9 – *Award of arbitrators; confirmation; jurisdiction; procedure:*

> If the parties in their agreement have agreed that a judgment of the court shall be entered upon the award made pursuant to the arbitration ... then at any time within one year after the award is made any party to the arbitration may apply to the court ... for an order confirming the award, and thereupon the court must grant such an order [...]

However, in Sverdrup Corp. v. WHC Constructors, Inc.,989 F.2d 148 (4th Cir. 1993), the court held that this time period was permissive rather than mandatory. *See* Harges, *The Handbook on Louisiana Alternative Dispute Resolution Laws*, 387 (n. 89).

[108] Cheung, "The Enforcement Methodology of Non-Domestic Arbitral Awards," 246 (n. 108).

[109] Ibid.

[110] Ibid., 246-247.

5. The Competence-Competence Doctrine in a Nutshell

5.1 Overview

The principle of competence-competence equips an arbitral tribunal with the power to decide its own jurisdiction (which, however, is subject to a judicial review of competent jurisdiction in almost all legal systems). In light of this principle, the parties can circumvent waiting on a court's determination on the issue as the tribunal is allowed to act promptly and rule on the merits of the parties' broader contract challenge.[111] Thus, the competence-competence principle allows the arbitrators to discuss and rule on the existence of the arbitral clause, its scope and validity, without having to go through a national court. Though acknowledged in most modern legal systems in charge of arbitration, the doctrines of both competence-competence and separability are statutorily codified in a vast majority of countries, but neither one is expressly given mention anywhere in the FAA.[112] And, while the U.S. Supreme Court recognized the separability doctrine some five decades ago, any type of progress of the competence-competence doctrine has been incomparably more lethargic and has only started to take shape in recent years.[113]

Even though the jurisdictional decision of an arbitral tribunal is almost always subject to judicial review, the current U.S. law does not provide for such review on occasions when the parties had chosen to delegate the issue of jurisdiction to the arbitral tribunal.[114] The conclusions that the U.S. Supreme Court reached in *Rent-A-Center, West, Inc. v. Jackson,*[115] and *Hall Street Assoc. v. Mattel, Inc.*[116] clearly indicate that an arbitral tribunal does not only have the authority to rule on its own jurisdiction, but it also has the "final" word on the matter—without any posterior revision by the court.[117] This novel obstinate conflux seems to be the very picture of the German form of Kompetenz-Kompetenz that had existed in Germany before its adoption of the UNCITRAL Model Law in 1998.[118] The extreme scheme of Kompetenz-Kompetenz in Germany, which has since been abandoned, actually implied that if the parties entered into a second arbitral agreement allowing the arbitral tribunal to rule on its own jurisdiction in the first matter, the issue of the arbitral tribunal's jurisdiction could not come under the scrutiny of state courts so long as the second arbitral clause so providing

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[111] Graves and Davydan, "Competence-Competence and Separability-American Style," 157 (n. 2).
[112] Ibid., 158.
[113] Ibid.
[114] Ibid., 157.
[115] Rent-A-Center, Est, Inc. v. Jackson, 130 S.Ct. 2772 (2010). This decision, when read in combination with the *Hall Street Assoc.* decision, not only grants an arbitration tribunal the power to decide its own jurisdiction, but also gives the tribunal the "final" word on the issue, without any subsequent judicial review.
[116] Hall Street Assoc v. Mattel, Inc., 552 U.S. 576 (2008).
[117] Graves and Davydan, "Competence-Competence and Separability-American Style," 158 (n. 2).
[118] Ibid., 158-159.

was valid.[119] Stated differently, the parties had the power to efficiently forbid the state courts from deciding on the arbitral tribunal's jurisdiction and not merely until the tribunal itself had decided on its own jurisdiction.[120] Therefore, Germany was never bothered with the issue of whether the arbitral tribunal has the authority to rule on its own jurisdiction as the same was implied whenever there was a valid and binding arbitration agreement between the parties so providing.

5.2 Doctrinal Variations

Investing the arbitrator or arbitration tribunal with the power to rule on their own jurisdiction is, as it is widely asserted, one of the absolutely indispensable ramifications arising out of the nature of the autonomous and independent arbitral agreement. The source of this power that became known as the "competence-competence" doctrine is not to be found in the arbitral agreement itself or in the *pacta sunt servanda*[121] approach to the arbitral agreement (which mandates its binding character and enforceable prerogative). With that being taken into consideration, the principle of competence-competence has grown to have a few different adaptations varying across jurisdictions to the extent to which they opted to embrace and honor this principle in their respective legal regimes. In that regard, we can today speak of roughly four distinctive alterations of the competence-competence doctrine. What follows are the overviews of all four of them.

5.2.1 A party's challenge of the arbitral clause alone does not, in and of itself, preclude the arbitrator's power to move forward with the arbitration proceedings.[122]

Even in cases when one of the parties disputes the validity or the existence of the arbitration agreement, the core modicum of the idea behind the competence-competence principle still entitles the arbitrator or the arbitration panel to proceed with the process. This is so regardless of whether the party challenging the arbitration clause does so on the grounds related to the arbitration clause itself or on the grounds of voidability, ineffectiveness, or unenforceability of the underlying agreement. The reason behind that lies in the very purpose of the separability doctrine which, as previously established, provides for the autonomy of the arbitral agreement from the container agreement in which it is included and is insofar sufficient to fight off these allegations raised by one of the parties. However, the doctrine of separability allows only so much, so the capacity of the arbitrator or the arbitration panel to move forward with the arbitration process even when the disputed invalidity is directed at the arbitration agreement itself, stems from the competence-competence principle alone.

[119] Suyash Paliwal, "The More Favorable Regime within the 'Overlapping Coverage' of FAA Chapters One and Two," *American Review of International Arbitration* 23, no. 2 (2011), 47.
[120] Ibid.
[121] "Agreements must be kept."
[122] Paliwal, "The More Favorable Regime," 45-46.

5.2.2 Despite the fact that the arbitrator or arbitration panel is empowered to decide the disputes regarding the arbitration agreement, any such decision is subject to postliminary judicial review. In that sense, the arbitrator's power is concurrent with that of the judiciary.[123]

Generally speaking, the doctrine of competence-competence allows the arbitrators to rule on the claims raised regarding their jurisdiction in the arbitration proceeding. In other words, arbitrators or arbitration panels are allowed to determine and issue award on the formation, validity, and scope of the arbitral agreement concluded among the parties. The point to be made is that there is no law ordering arbitrators to suspend their action in cases when their jurisdiction is being disputed until such time when their authority to hear a case is determined by the court of competent jurisdiction.[124] Nor is there any law mandating that arbitrators proceed with ruling upon the merits of the dispute at hand without considering challenges concerning their jurisdiction, thus removing the jurisdictional issue from their agenda until the same is ruled upon by the relevant judiciary.[125] While one preference may lead to a substantial waste of time and resources, the other may prove itself as impracticable and subversive to the arbitration process itself. That exactly may be the reason behind the lack of any regulation providing for either course to be taken, allowing the arbitrators to look into the jurisdictional issue—not with the objective to render a final decision that would be binding on the parties (for that they cannot do under this variation of the competence-competence principle), but with the goal to serve as preliminary judges on whether or not to proceed with the arbitration. Nevertheless, the parties in jurisdictions embracing this doctrinal approach are entitled to seek either immediate or *ex post facto* judicial review on the issue or arbitrators' jurisdiction.

5.2.3 In certain instances, arbitrators are given the exclusive authority to be the preliminary decision-makers on challenges relating to the arbitral clause, but such decisions are still subject to review of the court with competent jurisdiction.[126]

The competence-competence principle, as invigorated by some legal systems, could equip the arbitrator or arbitration panel with exclusive power to preliminarily inquire and determine the claims raised with respect to their jurisdiction. According to this configuration, national courts are not permitted to consider the disputes concerning the arbitral clause until the arbitrator or relevant arbitration panel or tribunal makes such determination.[127] So, once the arbitrators had decided on the jurisdictional issue and rendered an award (either interim or final), the decision is subject to judicial review

[123] Ibid., 46.
[124] Ibid.
[125] Ibid.
[126] Ibid.
[127] Ibid.

under otherwise applicable standards of review.[128] Therefore, the only distinction between this and the previous doctrinal approach lies in the fact that the parties are not entitled to petition the courts and the courts are not allowed to engage in the arbitration process *concurrently* with the arbitrators or arbitration panels, and can only do so *ex post facto.*

5.2.4 Arbitrators and arbitration panels or tribunals have the exclusive power to rule on the challenges raised concerning the arbitral agreement.

Certain jurisdictions have interpreted the competence-competence principle in a way that provides for the exclusive authority of the arbitral body to inquire into and determine challenges to its jurisdiction, subject to little or no judicial review. More precisely, national courts would be prevented from examining the claims made in regard to the arbitral agreement until the arbitral body itself issues an award on the claims.[129] Once that occurs, a review by a court of competent jurisdiction would be made available only on the "highly-deferential grounds" that many legal mechanisms made applicable to non-jurisdictional arbitral awards.[130] The substructure for such effect of the competence-competence doctrine does not come from the arbitration agreement, but from the arbitration laws of the country where the arbitration proceeding is taking place as well as—more broadly—from laws of all jurisdictions inclined to recognize an award rendered by arbitrators or arbitration panels on the issue of their own jurisdiction.

5.3 Upsides and Drawbacks

Nowadays, it is vital to acknowledge the dual function of the competence-competence principle as it carries with itself both beneficial and unfavorable aspects. One of the upsides of this doctrine, as universally accepted by contemporary statutory codifications on international arbitration and international conventions, is to empower the arbitral tribunal to decide on its own jurisdiction. However, this is not to be achieved by empowering the arbitrators to act as *sole* judges, but simply by entitling them to act as *first* judges on the issue of their jurisdiction. More precisely, the advantage lies in granting them the right to reach a decision on their jurisdiction prior to any judicial authority, thus restricting the function that the judiciary has in reviewing the award. Hence, the competence-competence doctrine makes it mandatory for any judiciary dealing with a challenge of an arbitral tribunal's jurisdiction to desist hearing substantive argument as to the arbitrators' jurisdiction until the arbitrators themselves have had the opportunity to do so.[131] In that sense, the competence-competence doctrine is a principle of "chronological priority,"[132] and being of such legal nature where the

[128] Ibid.
[129] Ibid., 46-47.
[130] Ibid., 47.
[131] Ibid., 55.
[132] Ibid.

autonomy of the arbitral agreement amounts to the issue of *procedure*, it can be differentiated from the separability doctrine which amounts to the issue of *substance.* The purpose behind this principle seems to be to prevent a party from attempting to postpone arbitral proceedings by claiming invalidity or non-existence of the arbitral clause.

The paradox of the competence-competence doctrine could be noted in that its perks could also simultaneously be perceived as its defects, which is one of the reasons why its drawbacks have still not been fully acknowledged and why the topic has faced contentious debates. Namely, owing to the fact that the arbitral tribunal has the right to be the first in ruling on its own jurisdiction, the courts would get a chance to review such decision only in circumstances when an action is brought to set aside or enforce the arbitral award.[133] The act of challenging the validity or existence of the arbitral clause will not, however, preclude the arbitral tribunal from moving forward with the arbitration proceeding, determining its own jurisdiction, and—if it decides to retain jurisdiction—rendering an award on the substance of the issue at hand. And the arbitrators could perform all of these tasks without expecting to hear the outcome of any judicial action that may set aside the award on the jurisdictional issue.[134]

There is, of course, an exception. And that exception comes in the form of anti-arbitration injunctions—a tool that parties employ to prevent either the initiation or continuation of the arbitration proceedings. But because anti-arbitration injunctions attack the very essence of the competence-competence doctrine, the courts sitting in those countries that strictly adhere to the doctrine refuse to issue them.[135] Conversely, other courts find anti-arbitration injunctions necessary and their issuance justified. This stance is supported by the argument that (1) the competence-competence principle is not, by any means, absolute,[136] and (2) because a challenge of an arbitrator's jurisdiction will ultimately have to reach the court anyway, it would be more prudent for the court to rule on it at the beginning of the process and save the parties some time and costs along the way.[137] So certain courts—both in common and civil law jurisdictions—have been inclined to issue anti-arbitration injunctions and restrain arbitration proceedings when, for instance, the parties entered into no agreement to arbitrate, they initiated the arbitration proceeding before the wrong institution, the issue subject to

[133] Paliwal, "The More Favorable Regime," 56.
[134] Ibid.
[135] Jennifer L.Gorskie, "US Courts and the Anti-Arbitration Injunction," (2012), 28 Arbitration International, 296.
[136] *See, e.g.,* Dallah Real Estate and Tourism Holding Co. v. Ministry of Religious Affairs of the Government of Pakistan [2010] 3 WLR 1472, at para. 84 ("So also the principle that a tribunal in an international commercial arbitration has the power to consider its own jurisdiction is no doubt a general principle of law. It is a principle which is connected with, but not dependent upon, the principle that the arbitration agreement is separate from the contract of which it normally forms a part. But it does not follow that the tribunal has the exclusive power to determine its own jurisdiction, nor does it follow that the court of the seat may not determine whether the tribunal has jurisdiction before the tribunal has ruled on it…").
[137] Romesh, Weeramantry, "Anti-Arbitration Injunctions: The Core Concepts," 2.

arbitration was outside the scope of the arbitration agreement or was *res judicata*, and so on.[138] The overall sentiment, however, is that anti-arbitration injunctions are disruptive of the parties' agreement to arbitrate as well as the competence-competence principle, and that—even if their issuance were supported by legal authority—these injunctions "should be exercised with the utmost circumspections and only in rare circumstances."[139]

6. Consequences of the Doctrine of Separability

The separability doctrine, *i.e.*, the conclusion that an arbitral agreement is separate and independent from the underlying contract, gives rise to certain consequences which could be characterized as direct and indirect. One of the two direct consequences brought by the separability doctrine is that the arbitral agreement does not fall under the effect of the status of the underlying agreement. Rather, it suggests that—according to the paramount idea behind the doctrine of separability—the arbitral agreement is out of the scope of the events impacting the container contract since the validity of the former is not dependent on the validity of the latter.[140] The second direct consequence is that the law applicable to the underlying contract is not necessarily applicable to the arbitration agreement as well; in other words, the arbitration agreement may be governed by a different law, if so chosen by the parties.[141]

Conversely, there are four indirect consequences of the separability doctrine. The first one relates to one of the fundamental elements of arbitration law known as the "competence-competence principle" which is deemed to be a corollary of the doctrine of separability. As elaborated in the preceding paragraphs, the competence-competence principle gives arbitrators the power to decide on their own jurisdiction.

The second indirect consequence lies in the doctrine departing from its original purpose (secluding the arbitral clause from the laws governing the underlying agreement) and progressively amassing new objectives aside its initial one**.** Hence, certain countries began to use the separability doctrine as the authority for invalidating principles of international arbitration agreements.[142] That is, the argument is that the separability principle provides for the separation from the underlying contract as well as from all national laws.[143]

The third indirect consequence is the ability of the arbitral agreement to survive the termination or expiry of the underlying contract in which it is contained. It is thus

[138] Ibid.
[139] Gary B. Born, International Commercial Arbitration (Kluwer 2009), Vol I, 1054.
[140] Paliwal, "The More Favorable Regime," 39.
[141] Ibid.
[142] Ibid.
[143] Ibid.

not infrequent for the parties to initiate arbitration after their main contract has expired or been terminated.[144] Most jurisdictions pose no barriers to such claims so long as the disputes arise from the conduct that occurred during the term of the agreement.[145]

And the fourth and final indirect consequence is that the invalidity of the underlying agreement cannot deprive an arbitral award of validity. Stated differently, if an arbitral panel (or the court) determines that the parties' main agreement is void, that determination will not automatically deprive the parties' arbitral clause, and the arbitrator's award, of validity.[146]

These corollaries of the separability doctrine play a crucial role in practice and in the realm of arbitration law where a substantial majority of arbitration proceedings arise exactly under the arbitral clauses whose autonomy is addressed by the doctrine. Simply put, allowing a party to claim the invalidity of the arbitral clause whenever the underlying contract was terminated through performance or some other act would run against the very purpose of the clause, jeopardize business activities conducted on national and international levels, and undermine the confidence in the institution of arbitration law in general.

In sum, regardless of whether they are direct or indirect, some of the most influential and significant corollaries of the separability doctrine are as follows:

(1) the status of the underlying agreement does not impact the arbitration agreement;
(2) the substantive law governing the formation or the validity of the arbitration agreement may be different from that governing the main contract;
(3) the principle of competence-competence, which entitles an arbitral tribunal to determine, among other things, its own jurisdiction; and
(4) the pro-arbitration principle, which compels the national courts to refer a case to arbitration if the arbitration clause is prima facie valid.[147]

7. Conclusion

Essentially, the doctrine of separability, severability, or autonomy can be summarized by encompassing two extremely elementary rules. One, the arbitral clause does not have to be governed by the same law as the underlying agreement, *i.e.*, the

[144] Ibid.
[145] Ibid.
[146] Ibid.
[147] Leboulanger, "The Arbitration Agreement: Still Autonomous?" (n. 32).

parties are free to choose which law will apply to their arbitral agreement (subject to certain exceptions). And two, the invalidity of the underlying agreement exercises no influence on the validity of the arbitral agreement included therein. Taking into consideration the deep impact these rudimentary rules have had within the sphere of arbitration law, it becomes apparent that the doctrine of separability is an interesting academic challenge and exceptional legal phenomenon. While observing its path of development from a mere novelty to one of the most important principles in international commercial arbitration, one cannot help but notice how the general conception of contracts and dispute resolution mechanism have served as gradual techniques for improving and molding laws as to bring them in conformity with the needs and ever-changing demands of the business world. Be that as it may, while the doctrine continues to prove itself pragmatically, academics are persistent in their efforts to discover why the same ought to be used and what its usage suggests regarding our universal comprehension of contracts, specifically, and the dispute resolution apparatus, generally.

Nowadays, the practical nature of the separability doctrine is one of its primal features making it a pillar of the whole international arbitration framework. As opposed to a few centuries ago, the current position is that entrusting the validity of the underlying contract to arbitration, instead of to the national courts, is indispensable in order to achieve the holism of arbitral decision-making and to ascertain a smooth, quick, and efficient process. As pointed out throughout this article, the fact is that the tussle between arbitral autonomy, on one hand, and judicial supervision of the arbitral body, on the other, has been prevalent since the doctrine's inception. Another fact is that discords in application of the separability doctrine are not completely eliminated. However, despite of these challenges, a rather robust inclination towards uniformity exists, convincing the international community to recognize the separable nature of the arbitration agreement.

The highlighted global importance of the position that the doctrine of separability assumes in both public and private affairs leaves no room for wondering about the autonomy of the arbitration agreement. The evidence of this significance can be found in the UNCITRAL Model Law on international commercial arbitration, adopted by the United Nations Commission on International Trade on June 21, 1985, which—as an embodiment of the current model of arbitration law—accepts the doctrine of separability.[148] Hence, scholars and national courts, acknowledging the doctrine of separability as a part of universal consensus among arbitration practitioners, ought to work on its further implementation by emphasizing its practical, legal, and procedural superiority.[149]

[148] Gerese, "Comparative Analysis of Scope of Jurisdiction of Arbitrators under the Ethiopian Civil Code of 1960," 14 (n. 1).
[149] Ibid., 10.

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THE WTO APPELLATE BODY CRISES: CAN THE CRISIS BE CURED?

Agata Zwolankiewicz

Abstract

The Appellate Body has played a major role in the dispute settlement system at the WTO. The future of it, and as a result, the future of the dispute settlement system remains unknown. That is due to the fact that the USA has been consistently blocking new appointments of the prospective members to the Appellate Body. The USA has been alleging that its strategy consisted in expressing its dissatisfaction with certain alleged irregularities concerning the functioning of the appellate process and the members of the Appellate Body. There has been a lot of discussions on the possibilities to avert the crisis both temporarily, as well as to pursue fundamental changes to the current dispute settlement system in order to address certain concerns that were raised since the beginning of the functioning of the Appellate Body. This paper explores possible scenarios of the cure of the stalemate in the Appellate Body in the WTO dispute settlement system.

Keywords
WTO · Dispute Settlement · Appellate Body · International Trade Law

1. Introduction

Dispute settlement system existing under the World Trade Organization ("WTO") regime was dubbed a "crown jewel" of the WTO and global trading system as such.[1] The legal framework for settling disputes under WTO auspices was set in the Understanding on Rules and Procedures Governing the Settlement of Disputes ("Dispute Settlement Understanding" or "DSU"). DSU constitutes a very unique set of rules – after all, the WTO was the first international organization to introduce a binding appeal process in 1995.[2] The system has been functional up to a certain point when the political tensions started coming into play. Despite the remarkable success of settling disputes among the WTO member states, in recent years we have been witnessing the process of the so-called "killing the WTO from the inside," as observed by Cecilia Malmstrom, the European Union's trade diplomat.[3] That is due to the fact that the USA has been consistently blocking new appointments of the prospective members to the Appellate Body. The USA has been alleging that it attempted to express its dissatisfaction with the functioning of the appellate process and with certain actions of the Appellate Body members. Even though the USA provided a detailed list of the concerns regarding malfunctioning of the system, it failed to make any proposals as to the Appellate Body amendments. Moreover, the recent proposals circulated by other WTO member states did not meet the United States' expectations. On 10 December 2019, terms of office of two out of three remaining members expired and the Appellate Body no longer holds the required quorum to operate in a functional manner.

This paper will address the reasons which led to the crises and present solutions which could once again cure the dispute settlement function of the WTO. One must bear in mind that even though December 2019 constituted a peak of the crisis, there has been a significant discontent with the appeal system in the WTO in the last decade.[4] Therefore, despite any temporary solutions to the stalemate, there is a need of a thorough redesign of the system. We are now witnessing a drift away from the multilateral trade cooperation with the simultaneous rise of the escalating national interests in politics. There is a risk that without maintaining a functioning dispute settlement system, we will be facing trading systems in which big players can once again dictate the rules of trade.[5]

2. The Importance of the Appellate Body in the Dispute Settlement in the WTO

2.1. The Structure and Functions of the Appellate Body

The Appellate Body constitutes one of the three institutions administering the WTO dispute settlement system. It was established in 1995 in DSU. The Dispute Settlement

[1] C. D. Creamer (2019), "From the WTO's Crown Jewel to Its Crown of Thorns," *AJIL Unbound*. No. 113.
[2] J. Waincymer (2002). WTO Litigation: Procedural Aspects of Formal Dispute Settlement. London: Cameron May Ltd. p. 693.
[3] E. Porter (2017). Trump's Trade Endgame Could Be the Undoing of Global Rules. N.Y. Times. Retrieved from: https://www.nytimes.com/2017/10/31/business/economy/trump-trade.html, [https://perma.cc/E85R-KWT4].
[4] Office of the US Trade Representative. (2018). 2018 Trade Policy Agenda and 2017 Annual Report of the President of the United States on the Trade Agreements Programme. pp. 22-28.
[5] A. Bahri (2019). "'Appellate Body Held Hostage': Is Judicial Activism at Fair Trial*?". J. World Trade.* 53(2). p. 295.

Understanding regulating the operation and proceedings before the Appellate Body is not the only legal act setting forth provisions regarding the appellate process. The Appellate Body is authorized to issue its own working procedures in consultation with the Chairman of the Dispute Settlement Body and the Director-General. Members of the Appellate Body, as the first task after the appointment, drew up Working Procedures for Appellate Review[6] which have been amended six times since 1995.[7]

Pursuant to Article 17 of DSU, the Appellate Body was created to rule on disputes heard by panels. It is generally composed (or given the current state of events - rather should be) of seven members – appointed for four year term; however, it sits in division of three members.[8] The members may be reappointed only once. The members of the Appellate Body are selected taking into account the principles of random selection which has not been shared with the public.[9] As provided for in Article 17.3 of DSU, the Appellate Body must be comprised of persons of a recognized authority who demonstrate expertise in law, international trade and the subject matter of the dispute. When it comes to membership, "a broad representation of membership in the WTO" is also taken into consideration.[10] There is no rule preventing the nationals from the Member State to sit on an appeal in a dispute concerning that member state, unlike at the panel stage. That is due to the limited number of members of the Appellate Body – since most disputes concern the USA, Japan and the European Union, it could have been virtually impossible to have the same rules as for the panel level.[11] The importance of the Appellate Body is even more significant given the number of appealed cases which far exceeds what was expected.[12] As of 2007, it has been estimated that almost 70 percent of cases were appealed.[13] This number has been increasing year by year and in 2016, the number of reports that were appealed amounted to nearly 90%.[14]

Essentially, disputing parties may file an appeal within 60 days after the panel's report has been circulated.[15] The Appellate Body hears appeals which are limited to the issues of law covered in the panel report and legal interpretation that was developed by the panel in a particular case.[16] Such a limitation has been subject to criticism in legal writing. An appeal can be brought only by the parties in a dispute before the panel, excluding any involved third

[6] P. Van den Bossche (2005). "The making of the 'World Trade Court': the origins and development of the Appellate Body of the World Trade Organization". Key Issues in WTO Dispute Settlement: The First Ten Years. Cambridge: Cambridge University Press. p. 69.
[7] WT/AB/WP/1; WT/AB/WP/2; WT/AB/WP/3; WT/AB/WP/4; WT/AB/WP/5; WT/AB/WP/6.
[8] Article 17.1 DSU.
[9] Waincymer, *supra* note 2, p. 706.
Rule 6 (2) of the Working Procedures for Appellate Review provides that: "*The Members constituting a division shall be selected on the basis of rotation, while taking into account the principles of random selection, unpredictability and opportunity for all Members to serve regardless of their national origin*".
[10] Article 17.3 DSU.
[11] Waincymer, *supra* note 2, p. 706.
[12] P. van der Bossche (2008). *The Law and Policy of the World Trade Organization*. Cambridge: Cambridge University Press. p. 73-74.
[13] Van der Bossche, *supra* note 13, p. 288.
[14] E. Fabry and E. Tate (2018). "Saving the WTO Appellate Body or Returning to the Wild West of Trade". Policy Paper. No25. p. 5.; Bahri, *supra* note 5, p. 294.
[15] Article 16.4 DSU.
[16] Article 17.6 DSU.

parties.[17] There are no limitations as to which party can file an appeal - both the complaining and responding party may wish to do so. Nonetheless, the parties will most likely file an appeal on different grounds.[18] Pursuant to the Working Procedures for Appellate Review, appellants must file a Notice of Appeal with Secretariat simultaneously with submitting a notification in writing to the Dispute Settlement Body.[19] A party to a dispute has 18 days thereafter to respond to the allegations raised in the appellant's submission.[20] After the written phase, the oral phase will begin. The procedural rules require the Appellate Body to hold a hearing between 30 and 45 days after the date of the filing of a Notice of Appeal, which means that the hearing is of a mandatory character and its conduct is not subject to the Appellate Body's discretion.[21] After the hearing, the members adjudicating the case meet with the remaining four members to exchange views on the case in order to ensure consistency in decision making.[22] After the exchange of views is completed, the Appellate Body deliberates and prepares a report, which is to be adopted by the Dispute Settlement Body and unconditionally accepted by the parties to the dispute unless there is a "negative" consensus not to adopt it within 30 days following its circulation to the Members.[23]

The Appellate Body does not give advisory opinions. Its report has no direct binding quasi-judicial power since its report has to be adopted by the Dispute Settlement Body[24] in any case. It can uphold, modify or reverse the legal interpretations adopted by the panel.[25] Modification of legal interpretations adopted by panels occurs where the Appellate Body upholds the final recommendations of the panel; however, it does so providing different reasoning.[26] Even though the reports do not have the *stare decisis* effect since 1995, the Appellate Body produced a significant international trade law jurisprudence of importance in its own future decisions which constitutes a relevant source of knowledge for legal scholars[27] as well.

2.2. The Law-Making Function of the Appellate Body

There is a general consensus that the Appellate Body's reports are not binding except between the parties in a dispute. It does not necessarily mean that subsequent panels have the liberty to disregard legal interpretations in the previous reports adopted by the Dispute Settlement Body.[28]

[17] Article 17.4 DSU.
[18] V. Hughes (2005). "Special Challenges at the Appellate Stage: A Case Study". Key Issues in WTO Dispute Settlement System. p. 80.
[19] Rule 20 (1) Working Procedures for Appellate Review.
[20] Rule 22 (1) Working Procedures for Appellate Review.
[21] Rule 27 (1) Working Procedures for Appellate Review.
[22] Rule 4 (1) Working Procedures for Appellate Review; *see* Hughes, 82 (n. 18).
[23] Article 17.14 DSU.
[24] Waincymer, 697 (n. 2).
[25] Article 17.13 DSU.
[26] Waincymer, 703 (n. 2).
[27] G. Shaffer, M. Elsig and S. Puig (2016). "The Extensive (but Fragile) Authority of the WTO Appellate Body". *Law & Contemp Probs.* 79(1). p. 244.
[28] J. Pauwelyn, A.T. Guzman and Hillman, J. A. (2016). *International Trade Law*. New York: Wolters Kluwer. p. 144.

Even though the Appellate Body does not operate under the stare decisis, its decisions have significantly impacted the operations of a dispute settlement system at the WTO.[29] As Van Grasstek states, "trade law is what the AB members say it is."[30] The Appellate Body constitutes a fundamental aspect of the law-making function at the WTO due to the fact that its decisions are likely to be most influential current interpretations on provisions in question.[31]

As indicated in Japan – Alcoholic Beverages II: "adopted panel reports are an important part of the GATT *acquis*. They are often considered by subsequent panels. They create legitimate expectations among WTO Members, and therefore, should be taken into account where they are relevant to any dispute."[32] The same view was expressed in the US Stainless Steel case: "The Panel's failure to follow previously adopted Appellate Body reports addressing the same issues undermines the development of a coherent and predictable body of jurisprudence […]."[33]

Since its existence, the Appellate Body has made significant rulings not only on the substantive issues but also concerning procedural and systematic issues relating to the WTO proceedings. They have had a significant impact on the functioning of the dispute settlement in the WTO – providing security and predictability of the system.[34] In general, stability of the line of its decisions was one of the advantages of the WTO dispute settlement system.

With this in mind, it must be underlined that there are certain mechanisms in the WTO dispute settlement system to prevent an excessive amount of "precedents" established by the Appellate Body. There has been some criticism that the Appellate Body expands its reach due to the use of *obiter dicta,* i.e. addressing the non-relevant issues for a resolution of the dispute by which it creates unnecessary precedents for future use. It has been argued by Pelc and Bush that in order to limit that scope, the Appellate Body should exercise its right to judicial economy to disregard the issues ambivalent to the scope of the dispute.[35] Judicial economy consists of a notion that the adjudicator does not have to enter into a complex analysis of each particular issue if a dispute has been resolved on other grounds.[36] Due to the wording of DSU provisions, it became unclear whether the Appellate Body may utilize judicial economy. Pursuant to Article 17.12 of DSU, the Appellate Body must address each of the issues raised in the appeal, which raised some doubts regarding such a possibility. However, despite the controversies surrounding this mechanism on the appellate level, the Appellate Body has taken advantage of the concept of judicial economy in the proceedings.[37] On the one hand, it has been argued that the language of

[29] A. Scully-Hill and H. Mahncke (2009). "The Emergence of the Doctrine of *Stare Decisis* in the World Trade Organization Dispute Settlement System". *Leg. Issues Econ. Integration*. 36(2). p. 143.
[30] C. Van Grasstek, (2013). *The History and Future of the World Trade Organization*. World Trade Organization. Geneva: World Trade Organization. p. 241.
[31] Waincymer, *supra* note 2, p. 705.
[32] *Japan — Taxes on Alcoholic Beverages*, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, 4 October 1996.
[33] *United States — Final Anti-Dumping Measures on Stainless Steel from Mexico*, WT/DS344/AB/R, 30 April 2008.
[34] D. Steger & S. Lester (2001). "WTO Dispute Settlement: Emerging Practice and Procedure in Decisions of the Appellate Body". *Due Process in WTO Dispute Settlement*. London : Cameron May. p. 199.
[35] M. Bush and K. Pelc (2010). "The Politics of Judicial Economy at the World Trade Organization". *International Organization*. 64 (2). p. 263.
[36] Waincymer, *supra* note 2, p. 368.
[37] R. Alvarez-Jimenez (2009). "The WTO Appellate Body's Exercise of Judicial Economy". *J. Int. Econ. Law*. 12 (2). p. 393.

the provisions is clear and leaves no room for interpretation.[38] On the other hand, the Appellate Body itself took a more liberal approach to that issue in the United States – Subsidies on Upland Cotton,[39] allowing for judicial economy. It has been argued that the ability to use this mechanism by the Appellate Body should be justified under the general principles embodied in Articles 3.4 and 3.7 of DSU.[40] There have been proposals to include an express provision allowing the Appellate Body to exercise the concept of judicial economy to clarify the ambiguity.[41] The main justification for such a proposal was that it would limit the obiter dicta rulings and ensure that a 90-day limit for deciding on an appeal is complied with.

2.3. Critique of the Appellate Body

Despite a remarkable success of the dispute settlement in the WTO, it is not a system without any flaws. As indicated by Pauwelyn, there has been a general satisfaction with the Appellate Body and none of the proposals as to its operation contain fundamental alterations.[42] Nonetheless, the United States constantly blocking the appointment of the members of the Appellate Body seems not to share that academic view. Moreover, there have been also dissenting voices in legal writing as to the functioning of the appeal process. It has been argued that the Appellate Body frequently oversteps its boundaries and instead of interpreting the law, takes a step further and creates it.[43] The criticism towards the Appellate Body revolves around the alleged failure to respect the procedural provisions by its members and progressive self-empowerment.[44] The so-called judicial activism and "the-law-making function" of the Appellate Body did not go unnoticed. Especially, the United States was negatively referring to the overreach of its rulings by underlining that this WTO body is not responsible for filling the gaps of the WTO agreements and creating new rights and obligations for the WTO members but solely for rectifying legal mistakes made by the panel in their reports.[45] Other allegations as to the malfunctioning of the Appellate Body concerned violation of the procedures. Examples include lack of a 90-day notice in case of resignation of Hyun Chong Kim who became South Korea's Trade Minister and violating time limits set forth for appellate proceedings (60 days or 90 days in complex cases).[46]

On the one hand, as described in the preceding paragraph, it has been argued that the Appellate Body has been trespassing its mandate. On the other hand, Pauwelyn points out that there are certain mechanisms the Appellate Body is lacking. One of the so-called "design flaws" of the Appellate Body is the lack of a remand procedure. As already mentioned, the Appellate Body has the power to uphold, modify or reverse the legal interpretations adopted by the panel.[47]

[38] Ibid., 394.
[39] Ibid.
[40] Waincymer, 702 (n. 2).
[41] Communication from the EU, China, Canada, India, Norway, New Zealand, Switzerland, Australia, Republic of Korea, Iceland, Singapore, and Mexico to the General Council. Retrieved from: https://trade.ec.europa.eu /doclib/docs/2018/november/tradoc_157514.pdf.
[42] Pauwelyn, Guzman and Hillman, 136 (n. 28).
[43] Matsushita, M., Schoenbaum, T. J., Mavroidis, P. C., & Hahn, M. J. (2017). The World Trade Organization: Law, Practice, and Policy. Oxford University Press. p. 131.
[44] Fabry and Tate, 8-9 (n. 14).
[45] Ibid,, 9.
[46] Bahri, 297 (n. 5).
[47] Article 17.13 DSU.

Due to the fact that the Appellate Body cannot make new factual findings as the review standard in not de novo, deciding on an appeal concerning panel's report may be a difficult task if it is not sufficiently exhaustive.[48] The review standard set forth in Article 11 of DSU requires an "objective assessment of the facts."[49] The possible scenarios to resolve that issue would be either to introduce a remand procedure or expand the powers of the Appellate Body to make new factual findings. As for now, the Appellate Body's only option under the current legal framework is to leave certain issues unresolved. In particular cases, not completing the analysis left the entire case unresolved, e.g. EC – LAN Equipment, Canada – Dairy (Article 21.5 – I) and US – Softwood Lumber VI (Article 21.5).[50]

Although there are no provisions that would clearly evaluate the position of the Appellate Body in the WTO system, Howse claims that its rather broad power can be deduced from the very nature of DSU provisions. Between the lines, they do describe the status and authority of the Appellate Body. Drafters demonstrated in a clear manner that it was not their intention to impose limitations on the Appellate Body – by including provisions solely relating to what the Appellate can and must do. That approach would indicate that the issues not specified in DSU would therefore be considered as outside of the scope of its authority. At the end of the day, drafters included a significant share of provisions describing what the Appellate Body cannot do, leaving room for interpretation and empowering that WTO body with a significant scope of possibilities.[51] It seems that these loopholes are exactly that which led to the escalated conflict regarding the operation of the dispute settlement system.

3. Background of the Crisis in the WTO

Despite the general message created by the media, it was not Donald Trump who turned the United States' approach against the WTO. It has been more than a decade since the United States was seeking amendments to the dispute settlement system and has been making detailed complaints regarding its functioning.

The USA has been following the general line of negative views on the Appellate Body. It mainly expressed concerns on the quasi-precedents as well as the Appellate Body's failure to comply with procedural requirements. However, nowadays the USA went into a more detailed critique of the Appellate Body members. In "2018 Trade Policy Agenda and 2017 Annual Report of the President of the United States on the Trade Agreements Programme,"[52] the United States acknowledged that a dispute settlement mechanism is necessary to protect the underlying trading system. It also presented a list of its concerns regarding the operation of that body and the WTO dispute settlement system.

[48] J. Pauwelyn, (2007). Appeal without Remand: A Design Flaw in WTO Dispute Settlement and How to Fix It. ICTSD International Centre for Trade and Sustainable Development.
[49] Article 11 DSU.
[50] Pauwelyn (n. 48).
[51] Howse R. (2003). "The Most Dangerous Branch? WTO Appellate Body Jurisprudence on the Nature and Limits of the Judicial Power". The Role of the Judge in International Trade Regulation: Experience and Lessons for the WTO. p. 13.
[52] Office of the US Trade Representative, 22-28 (n. 5).

The most vital concern was that both the panels as well as the Appellate Body were "adding to or diminishing rights and obligations under the WTO Agreement" instead of simply interpreting the agreements as they were.[53] It has been argued that the reach of the findings in the adopted reports went a step too far. Additionally, the main discontent of the United States with the Appellate Body also referred to the failure to comply with the 60-day (and in complex cases 90-day) time period for deciding on appeals.[54] Pursuant to Article 17.5 of DSU, "[a]s a general rule, the proceedings shall not exceed 60 days from the date a party to the dispute formally notifies its decision to appeal to the date the Appellate Body circulates its report". Further, it is added: "In no case shall the proceedings exceed 90 days". As observed by the United States, the Appellate Body has been respecting the imposed time limits in the first years of its establishment. Out of 101 appeals, in 87 it issued its report within the 90-day deadline, in the remaining 14, the Appellate Body consulted with the parties and obtained their consent to go beyond that period.[55]

The change came after six years. Starting in 2011 with the appeal in US-Tyres[56] (China), the Appellate Body departed from complying with the 90-day period providing no explanation and without reaching to the parties in dispute to obtain their consent to go above that limit. Already in 2011, the USA voiced its concerns regarding this situation to the Dispute Settlement Body, however, without any result.[57] Since then, the Appellate Body has been increasing the needed time for hearing disputes, achieving on average 163 days in 2014. On the one hand, the Appellate Body was arguing that it is not able to meet the prescribed time limits. It was pointed out by the United States that the Appellate Body would be able to issue its reports within the provided deadline if it refrained from addressing issues not necessary to resolve the case and thus limited obiter dicta decisions. Moreover, the USA underlined that even if the Appellate Body was struggling with complying with the timeframes set forth in DSU, it was not up the Appellate Body's discretion to disregard or amend the provisions thereof as the prescribed time limits are not discretionary.[58]

Another point that was heavily criticized was the legitimacy of Rule 15 of the Working Procedures for Appellate Review on the participation in appeal proceedings by the Appellate Body members after the expiry of their tenure.[59] Authorizing a person who is no longer a member of the Appellate Body raised many concerns. Pursuant to the view of the United States, "under the WTO Agreement, it is the Dispute Settlement Body, not the Appellate Body, that has

[53] *Ibid*, p. 22.
[54] Statement by the United States at the Meeting of the WTO Dispute Settlement Body. Geneva, June 22, 2018 (2018). Retrieved from: https://geneva.usmission.gov/wp-content/uploads/sites/290/Jun22.DSB_.Stmt_.as-delivered.fin_. public.rev_.pdf.
[55] Ibid.
[56] *United States — Measures Affecting Imports of Certain Passenger Vehicle and Light Truck Tyres from China*, WT/DS399/AB/R, 5 September 2011.
[57] Minutes of the DSB Meeting on October 5, 2011 (WT/DSB/B/304), p. 4.
[58] Statement by the United States at the Meeting of the WTO Dispute Settlement Body. Geneva, June 22, 2018' (2018). Retrieved from: https://geneva.usmission.gov/wp-content/uploads/sites/290/Jun22.DSB_.Stmt_.as-delivered.fin_.public.rev_.pdf.
[59] Statement by the United States at the Meeting of the WTO Dispute Settlement Body. Geneva, February 28, 2018 (2018). Retrieved from: https://geneva.usmission.gov/2018/03/01/statements-by-the-united-states-at-the-february-28-2018-dsb-meeting/.

the authority and responsibility to decide whether a person whose term of appointment has expired should continue serving."[60]

The United States have been issuing statements in which it expressly pointed to the cases it considered to be the Appellate Body overstepping. As to the appellate report in the case of Argentina-Financial Services[61], the USA was alleging that more than two-thirds (amounting to 46 pages) of the Appellate Body's analysis was in the nature of obiter dicta, creating persuasive arguments for future disputes between the WTO member states. Even though the main issue in the dispute was the understanding of likeness requirements, the Appellate Body went further and in a great detail interpreted various provisions of GATS.[62] Similar concerns were raised concerning India — Measures Concerning the Importation of Certain Agricultural Products.[63] In accordance with the United States' position, the Appellate Body devoted a considerable amount of time on the issues that were not raised by either party in the appeal. The United States discontent with the operation of the Appellate Body escalated to such a point that its entire closing statement was devoted to urging the Appellate Body not to focus on the issues that were not even appealed by the parties.[64] In United States—Safeguard Measures on Imports of Fresh, Chilled or Frozen Lamb Meat from New Zealand and Australia,[65] in the United States' opinion, the Appellate Body exceeded its mandate and created new obligations on its part stating that it must prove that unforeseen developments necessitate the imposition of a safeguard. Moreover, the report was subject to criticism as the Appellate Body resorted to making new factual findings whereas at the appellate stage de novo review is not allowed.[66]

4. What Should Be (and Has Been) Done to Cure the Appellate Body?

On 10 December 2019, the mandates of Amb Ujal Bhatia and Thomas Graham expired, leaving the Appellate Body unable to function due to the lack of a required quorum.[67] The attempts to bury the Appellate Body did not stop there – the WTO Members pressured by the United States agreed to significant cuts of the budget for 2020.[68]

[60] Office of the US Trade Representative, 26 (n. 5).
[61] *Argentina — Measures Relating to Trade in Goods and Services*, WT/DS453/AB/R, 14 April 2016.
[62] Statement by the United States at the Meeting of the WTO Dispute Settlement Body of 23 May 2016. Retrieved from: https://www.wto.org/english/news_e/news16_e/us_statment_dsbmay16_e.pdf.
[63] *India — Measures Concerning the Importation of Certain Agricultural Products*, WT/DS430/AB/R, 4 June 2015.
[64] Closing Statement of the United States of America at the Oral Hearing. Retrieved from: https://ustr.gov/sites/default/files/files/Issue_Areas/Enforcement/DS/Pending/US.Oral.Stmt.Closing.pdf.
[65] *United States — Safeguard Measure on Imports of Fresh, Chilled or Frozen Lamb from New Zealand*, WT/DS177/AB/R, WT/DS178/AB/R, 1 May 2001.
[66] *U.S. Slams WTO Lamb Ruling over Appellate Body Mandate*. Retrieved from: https://www.iatp.org/news/us-slams-wto-lamb-ruling-over-appellate-body-mandate, [https://perma.cc/C4SZ-KCR7], *see also*: Sykes A.O. (2003). "The Safeguards Mess: A Critique of WTO Jurisprudence". *SSRN Electronic Journal*. p. 15.
[67] Farewell Speech of Appellate Body Member Thomas R. Graham. Retrieved from: https://www.wto.org/english/tratop_e/dispu_e/farwellspeechtgaham_e.htm.
[68] B. Baschuk. WTO Members Agree on a 2020 Budget, Averting Jan. 1 Shutdown. Retrieved from: https://www.bloomberg.com/news/articles/2019-12-05/wto-members-agree-on-a-2020-budget-averting-jan-1-shutdown.

In order to resolve this situation, on 27 March 2020,the EU and 15 other WTO member states reached a "Multiparty interim appeal arbitration agreement"[69] ("Multiparty agreement"). This mechanism goes back to 2019 when the EU and Canada agreed on an interim appeal arbitration based on Art. 25 of DSU. It provides for expeditious arbitration within the WTO in order to resolve the issues clearly defined by both parties. Under the agreement, the appeal arbitration procedure will be based on the substantive and procedural aspects of the Appellate Review under Art. 17 of DSU.[70] In other words, the appellate mechanism under Art. 25 of DSU aims at replicating the same procedure existing in the WTO framework.

The main advantage of resorting to *ad hoc* arbitration is that this mechanism already exists and does not need any amendments of DSU or even Working Procedures for Appellate Review. This solution is not devoid of shortcomings. Resorting to arbitration proceedings can serve as a temporary cure for the settlement process. Unfortunately, it seems that in the long run the *ad hoc* arbitration proceedings within the WTO will not be sufficiently effective as they do not constitute a cure to the structure and operation of the organization. Despite the fact that the arbitral awards would be subject to surveillance of the Dispute Settlement Body under Article 25 of DSU, not much can be said at this point about the possibility to enforce unadopted panel report further amended in the arbitral proceedings. The Multiparty agreement does create however, a parallel arbitration mechanism and a separate category of appellate reports since the arbitration awards are not required to be adopted by the DSB.[71]

Even if the Appellate Body continues to operate thanks to temporary solutions, or the other way round, even if the appellate process becomes temporarily suspended, the WTO demands structural and fundamental changes with regard to dispute settlement system. Simply securing the appellate proceedings as it is, is not sufficient to cure it. The malfunctioning of the Appellate Body has been a subject of discussion for at least a decade when the United States started making complaints. We are now experiencing a peak of the problem and it seems that the issues concerning the Appellate Body have been neglected for too long. Even though some of the countries started coming up with initiatives to make changes, some say bitterly that it is too little, too late,[72] and that there are no quick fixes.[73] Despite the deadlock in the Appellate Body, it is essential to take a look at a bigger picture and start with negotiating amendments to the dispute settlement system in the long run as: "[p]reserving the WTO by strengthening its two essential legs: negotiation as well as litigation – will be crucial for the future of the world economy."[74]
As of 1 March 2021, Ngozi Okonjo-Iweala took office of the seventh Director-General of the WTO as the first women to hold this position. She is facing a daunting task of reforming the

[69] EU and 15 World Trade Organization Members Establish Contingency Appeal Arrangement for Trade Disputes. Retrieved from: https://trade.ec.europa.eu/doclib/press/index.cfm?id=2127.
[70] Statement on a Mechanism for Developing, Documenting and Sharing Practices and Procedures in the Conduct of WTO Disputes. p. 2, para. 3. Retrieved from: https://trade.ec.europa.eu/doclib/docs/2020/april/tradoc_158731.pdf.
[71] Jaswant S.S. Arbitration in the WTO: Changing Regimes Under the New Multi-party Interim Appeal Arbitration Arrangement. Retrieved from: http://arbitrationblog.kluwerarbitration.com/2020/05/14/arbitration-in-the-wto-changing-regimes-under-the-new-multi-party-interim-appeal-arbitration-arrangement/.
[72] Wagner M. (2019). "The Impending Demise of the WTO Appellate Body: From Centrepiece to Historical Relic?". SSRN Electronic Journal. p. 17.
[73] Farewell speech of Appellate Body member Thomas R. Graham. Retrieved from: https://www.wto.org/english/tratop_e/dispu_e/farwellspeechtgaham_e.htm.
[74] Fabry/Erik Tate, 19 (n. 15).

WTO dispute settlement system, especially in the face of the global pandemic. Okonjo-Iweala shares her view that the resolution of trade disputes "needs to be taken care of and reformed to a point where all members, big and small, believe and trust in the system and can use it."[75] We are yet to witness what those steps will be.

4.1. Institutional Changes

The first proposal of amendments to the dispute settlement system at the WTO concerns the improvements of selection of panelists and Appellate Body members. Firstly, it has been argued that the WTO member states require a team of exceptional specialists in the field to resolve their disputes. In order to provide the much-desired stability and high quality of the reports, panelists should also serve on permanent basis.[76] Moreover, the process of their selection should be improved in order to detach it from the political influences. It is essential to at least include a more transparent and clear eligibility requirements to serve the role of adjudicator at the WTO. Possibly, providing for a neutralized appointment process would diminish the pressures of sensitive political issues and their resolution.[77]

Additionally, it is evident now that the number of members of the Appellate Body is not sufficient to effectively tackle the increased workload within the time limits imposed by the provisions of DSU.[78] It is advisable to increase that number unless the member states decide to agree on prolongation of the time limits on deciding the dispute.

4.2. Amendments to Rule 15 Working Procedures for Appellate Review

One of the most frequently raised concerns by the United States on the self-empowerment of the Appellate Body concerned the scope of Rule 15 Working Procedures for Appellate Review to complete an appellate process despite the expiry of their mandate. Several proposals were made to address this issue:

(i) allowing the members of the Appellate Body to hear disputes even after their mandate expired only if a key stage of appeal is triggered;
(ii) prohibiting members from hearing disputes 3 months before expiry of their terms of office;
(iii) extending the term of office of the members until there is a consensus of the appointment of a new member.[79]

These proposals still do not address the core of the problem. The most attractive solution from the United States perspective would be to prohibit the members whose mandates are

[75] Worland J.Okonjo-Iweala Believes the WTO Can Change the World. But First It Needs Reform. Retrieved from: < https://time.com/5938816/ngozi-okonjo-iweala-wto-climate-change/> [https://perma.cc/AT6U-Q9XK].
[76] Party like it's 1995: Resolving the WTO Appellate Body crisis | VOX, CEPR Policy Portal. Retrieved from: https://voxeu.org/article/party-it-s-1995-resolving-wto-appellate-body-crisis.
[77] McDougall R. (2018)."The Crisis in WTO Dispute Settlement: Fixing Birth Defects to Restore Balance" J. World Trade.52(6). p. 891.
[78] R. McDougall (2018). Crisis in the WTO: Restoring the WTO Dispute Settlement Function. CIGI Papers No. 194. p. 16.
[79] Fabry and Tate, 12 (n. 15).

expiring from sitting on the cases. Thus, it would be advisable to create a mechanism where such a practice would not be possible.

4.3. Addressing Procedural Irregularities

Certain procedural irregularities that have been pointed out by the United States in the last decade definitely contributed to the current state of affairs at the WTO. Several countries undertook the possibility to make proposals regarding changes to the Dispute Settlement Understanding, taking into consideration the concerns the United States has been raising in the last couple of years. On 26 November 2018, two documents were circulated to WTO members with regard to the proposed amendments to the dispute settlement system: the first one was prepared by the European Union together with other WTO member states - Australia, Canada, China, Iceland, India, Korea, Mexico, New Zealand, Norway, Singapore and Switzerland, the other one was prepared by the European Union together with China and India.[80] The member states expressed the willingness to work on new solutions as to the impasse in the Appellate Body with preserving its main functions. The group of countries called on remaining members to fill vacancies on the Appellate Body and simultaneously amend certain provisions of DSU, concerning, for instance, inclusion of a set of provisions dealing with the potential failure of the Appellate Body to comply with a 90-day timeframe, providing expressly the possibility of the Appellate Body to exercise the judicial economy.[81]

The proposals were not accepted enthusiastically by the United States nor the scholars monitoring the crisis at the Appellate Body. It is a difficult task to reconcile the needs and proposals of all the members of the WTO.[82] The United States raised doubts whether the proposal made by the EU together with China and India addressed any of the concerns it raised.[83] Actually, in accordance with the United States, the proposed changes would "make the Appellate Body even less accountable, and more susceptible to overreaching, by extending the terms of Appellate Body members, removing the opportunity of Members to decide on any possible reappointment, making Appellate Body membership a full-time position, and increasing resources for the Appellate Body Secretariat."[84] Given the position of the USA and lack of any concrete proposals on its part, it will be an extremely difficult task to identify what the issues are and reevaluate the position of the Appellate Body in the dispute settlement system.

4.4. Introducing a Remand Procedure

One of the shortcomings of the WTO dispute settlement system and the powers of the Appellate Body is the lack of remand procedure. Under the current legal framework, pursuant to Article 17.6 of DSU, the Appellate Body has no possibility to send back the case to the panel

[80] Communication from the EU, China, Canada, India, Norway, New Zealand, Switzerland, Australia, Republic of Korea, Iceland, Singapore, and Mexico to the General Council. Retrieved from: https://trade.ec.europa.eu/doclib/docs/2018/november/tradoc_157514.pdf.

[81] McDougall, 16 (n. 78).

[82] Wagner, 19 (n. 72).

[83] Statement by the United States at the Meeting of the WTO General Council of 12 December 2018. Retrieved from: https://geneva.usmission.gov/wpcontent/uploads/sites/290/Dec12.GC_.Stmt_.items_.7.and_.8.as_.delivered.clean_.pdf.

[84] Ibid.

stage which can certainly make adjudicating more difficult as the Appellate Body cannot make new factual findings and at the same time the panel may wish to exercise its right to resort to judicial economy and conduct legal analysis only of the issues it deems are necessary to resolve the dispute.[85] It has been argued that the drafters of the DSU: "imposed a division of labour between Panels and the Appellate Body, based on a distinction between fact and law."[86] It has not been explained exactly what motivated the drafters to include such a specific division as panels may conduct both factual and legal analysis whilst the Appellate Body's adjudication is limited to the issues of law covered in the panel report as well as legal interpretations developed thereof.[87] The reason may be that the drafters intended for the Appellate Body to be able to comply with the 90-day time limit to decide on the case.[88] In case the panel report is lacking a proper assessment of the facts of the case, the Appellate Body is left with a difficult task to tackle and there is a risk that the case will not be adjudicated in the exhaustive manner. The Appellate Body will attempt to assess the issues based on the factual findings gathered by the panel, however, there may be a time when it will not be sufficient and the Appellate Body will not be able to actually proceed with a case and successfully resolve a dispute.[89] Therefore, the amendments to DSU should be made either allowing for a remand procedure, which would remove the temptation of the Appellate Body to cross the procedural lines it has to operate within, or to allow for a *de novo review*.

5. Closing Remarks

"Let us try to fix the problems that can be fixed. Let us not consider the alternatives of AB at this stage. Considering its alternatives indicates that we are already giving up on this institution. It will be very unfair to let the AB die in this manner."[90]

The Appellate Body has been playing a major role of the adjudicating function of the WTO. Letting it "die from the inside" does seem indeed unfair. Instead of looking for solutions in advance, the conflict has escalated to such an extent that looking for possible cures became doomed to failure. It is not the policy that was adopted by the United States, especially in recent years that led to this point. Blocking the appointments of prospective members of the Appellate Body was a symptom of the disease but not its cause.

As of now, the Multiparty agreement aims at maintaining a mechanism in place that would preserve their rights in WTO dispute resolution system. The main advantage of this mechanism is that Article 25 of DSU is already in place and does not require any changes to the existing legal framework. What is also appealing about this solution is the fact that the structure of the proceedings will remain largely identical to what the member states are familiar with under the current regime. Therefore, there will be no need for the readjustment period and the member states will have the ability to focus on the long-term amendments to the dispute settlement system. At this stage of the conflict, it is necessary to preserve the rights under the

[85] Pauwelyn, (n. 48).
[86] T. Voon and A. Yanovich (2006). "The Facts Aside: The Limitation of WTO Appeals to Issues of Law." *Journal of World Trade*. 40 (2). p. 240.
[87] Article 17.6 DSU.
[88] Voon and Yanovich, 241 (n. 86).
[89] Waincymer, 372 (n. 2).
[90] Bahri, 315 (n. 5).

WTO Agreement and ensure that there is a mechanism allowing to maintain the multilateral trading system. At the same time, the member states have to further negotiate long-term changes to the dispute settlement system, reevaluate the position of the Appellate Body and the powers it should possess.

The strong turn to anti-globalization trend worldview is worrisome. There is a risk that we will be facing once again a situation where big trade players can simply dictate the rules of trade.[91] However, as we learnt in the past, that system did not work out. The present solution may not be ideal and definitely has many flaws; however, instead of giving up on it, the WTO member states should further cooperate and find a meaningful solution that would satisfy all members at the "negotiating table".

[91] Bahri, 295 (n. 5).

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PRIVACY BETWEEN REGULATION AND TECHNOLOGY: GDPR AND THE BLOCKCHAIN

Asim Jusić*

Abstract

Compliance with the GDPR while using blockchain technology for data processing results in compliance issues, due to the fact that the blockchain and the GDPR employ different methods to ensure privacy-by-design and privacy-by-default. The blockchain is built on disintermediation and relative decentralization, whereas the GDPR aims for re-intermediation and relative centralization of the data protection process. This paper provides an overview of and suggestions on how to secure compliance with the GDPR while processing data using the blockchain. A focus is placed on the data protection impact assessment on the blockchain network, issues in identifying and determining the role(s) of sole and joint data controllers and data processors, obstacles to exercising the right to rectification and right to be forgotten when the data is recorded on the blockchain, GDPR data transfer requirements as applied to the blockchain, and the protection of privacy in the process of creating blockchain-based smart contracts.

Keywords
GDPR · Blockchain · Compliance Privacy

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1. Introduction

The EU's General Data Protection Regulation (GDPR) (EU/2016/679)[1] is considered among the most important privacy protection regulations to have entered into force in recent history. At the same time, the blockchain is considered to be a technological innovation that may well fundamentally alter economies and everyday life by enabling disintermediation and rapid extraction of value from data.[2] However, relatively few sources discuss in detail whether, and how, the processing of data on the blockchain can be organized in such a way so as to comply with the GDPR.[3] This paper has two aims. Firstly, it discusses the main differences between the blockchain and the GDPR. Secondly, it provides practice-oriented suggestions on how to secure compliance with the GDPR while processing data and transferring value using the blockchain.

Part two of the paper provides an overview of the GDPR and blockchain technology. Part three analyses the most important compliance issues that emerge in the process of applying the GDPR to the blockchain: the data protection impact assessment on the blockchain network, issues in identifying and determining the role of sole and joint data controllers and data processors, obstacles to exercising of the right to rectification and right to be forgotten when data is recorded on the blockchain, GDPR data transfer requirements as applied to the blockchain, and the protection of privacy in the process of creating blockchain-based smart contracts. Part four concludes the paper.

2. The GDPR and Blockchain: An Overview

2.1. The General Data Protection Regulation

The GDPR is considered a breakthrough in privacy protection regulations. Three factors make the GDPR one of the most influential privacy protection regulations in existence: the concepts and principles behind it are considered a 'golden standard' of privacy protection; its extraterritorial impact is immense; and its relevance for and impact upon international data transfer flows are equally significant.

[1] Regulation EU/2016/679, European Union, 'General Data Protection Regulation (GDPR) – Official Legal Text' (*General Data Protection Regulation (GDPR),* https://gdpr-info.eu/, accessed 16 May 2021.

[2] McKinsey, 'How Blockchains Could Change the World' (2016), https://www.mckinsey.com/industries/technology-media-and-telecommunications/our-insights/how-blockchains-could-change-the-world#, accessed 19 May 2021.

[3] See Michèle Finck, 'Blockchain and the General Data Protection Regulation', https://www.europarl.europa.eu/RegData/etudes/STUD/2019/634445/EPRS_STU(2019)634445_EN.pdf. accessed 14 May 2021; Tom Lyons, Ludovic Courcelas and Ken Timsit, 'Blockchain and the GDPR', https://www.eublockchainforum.eu/sites/default/files/reports/20181016_report_gdpr.pdf, accessed 14 May 2021; and Asim Jusic, 'Dealing with Tensions Between the Blockchain and the GDPR' in Sophia Adams Bhatti, Akber Datoo and Drago Indjic (eds), *The LegalTech Book: The Legal Technology Handbook for Investors, Entrepreneurs and FinTech Visionaries* (John Wiley & Sons 2020), on which this paper builds and expands.

2.1.1. The Gold Standard of Privacy Protection

The GDPR elevated privacy to the level of a fundamental human right, and restricted the collection and processing of the personal data of holders of data rights, i.e. the data subjects.[4] The GDPR achieved this by embracing the concepts of the privacy-by-design and –default, and operationalizing these concepts through six privacy principles for the processing of personal data.

'Privacy-by-design' means that privacy and associated data protection issues should be taken into consideration throughout the process of designing any system, service or product. 'Privacy-by-default' requires those governing data processing – primarily data controllers and data processors–to process only such data that is necessary to achieve the specific purpose of data processing.[5] This means that any data processing should be undertaken in line with six core GDPR privacy principles: (a) lawfulness, fairness, and transparency in relation to the data subject (owner of the personal data); (b) purpose limitation; (c) data minimization; (d) accuracy; (e) storage limitation; and (f) integrity and confidentiality.[6]

The concepts of privacy-by-design and -default and the six principles of data processing enshrined in the GDPR became influential even before the GDPR came into force. Presently, the influence of the GDPR is so strong that comparability to the GDPR has become a measure of the quality of non-EU data protection regulations, turning the GDPR into a global 'golden standard' of privacy protection.[7]

2.1.2. The GDPR's Extraterritorial Impact

The GDPR is implemented in the present age of the free flow of data across national borders via the web. For that reason, the GDPR departs from the traditional understanding of the territorial scope of application of law, having instead an extraterritorial reach. Organizations established in the EU are expected to comply with the GDPR, even if they process data outside the EU. Non-EU entities offering goods or services inside the EU must also abide by the GDPR, even if such goods and services are offered free of charge. Further, the GDPR applies to organizations that 'monitor' individuals in the EU, irrespective of the place of registration of such organizations.[8]

To understand the breadth and width of the GDPR's extraterritorial impact, consider the following examples. If a non-EU entity uses one of the official EU languages or the euro as an accepted currency for payments, such a non-EU entity is subject to the GDPR because use of one

[4] PricewaterhouseCoopers, 'Top Policy Trends 2020: Data Privacy' (*PwC*, 2021), https://www.pwc.com/us/en/services/consulting/risk-regulatory/library/top-policy-trends/data-privacy.html, accessed 10 April 2021.
[5] GDPR Art. 25. (1) and (2) and Information Commisioner's Office, "Data Protection by Design and Default" (ICO, February 9, 2021), https://ico.org.uk/for-organisations/guide-to-data-protection/guide-to-the-general-data-protection-regulation-gdpr/accountability-and-governance/data-protection-by-design-and-default/.
[6] GDPR Art. 5. (1).
[7] cf. Asim Jusic, "Practical Guidance: Data Transfers - Gulf Region" (Bloomberg Law, 2018).
[8] GDPR Art. 3 and Freshfields Bruckhaus Deringer, "The Extra-Territorial Scope of the EU's GDPR," accessed April 15, 2021, https://www.freshfields.com/en-gb/our-thinking/campaigns/digital/data/general-data-protection-regulation/.

of the official EU languages or euro as a currency signals that the non-EU entity is 'envisaging' offering goods or services within the EU.[9] Moreover, using cookies to track web traffic and online behavior of individuals in the EU also makes the non-EU entity subject to the GDPR.[10]

2.1.3. International Data Transfers

For the purposes of the GDPR, international data transfers (IDTs)are transfers of data to non-EU countries and countries outside the European Economic Area (third countries) and international organizations, as well as onward data transfers from a third country to another third country or international organization.[11] The main requirement for an IDT is that the protection of rights of data subjects provided by the GDPR shall not be circumvented in the process of such transfer(s). This means that, i.e. data subjects should be informed that their data is to be transferred internationally, and that data processors should comply with their GDPR obligations and retain records of data processing, etc.[12]

Consequently, the GDPR allows IDTs in a limited number of cases. Firstly, an IDT is permitted if an EU Commission adequacy decision exists.[13] Secondly, an IDT can be performed if adequate safeguards for protecting data subjects' rights during the process of data transfer also exist. The GDPR cites standard contractual clauses,[14] binding corporate rules,[15] codes of conduct,[16] and certification mechanisms[17] as methods of IDT that adequately safeguard data subjects' rights. Third, IDTs can be performed in cases of derogations listed in GDPR Art. 49. Finally, IDTs are also permitted if they are sanctioned by international agreements.

A further limitation on IDTs is the prohibition of the recognition and enforcement of a third-country authority's decisions compelling a data controller or processor subject to the GDPR to transfer or disclose personal data. The data controller or processor subject to the GDPR can comply with such decisions only if an international agreement on the recognition and enforcement of such decisions exists, or if the data transfer and disclosure is undertaken using one of the data transfer mechanisms outlined above.[18]

2.2. Blockchain: What It Is, and Why It Matters

In general, the blockchain can be described as a chain of blocks wherein each block holds data that can be created by multiple originators using multiple internet addresses, while retaining anonymity of the creators in the process of the creation of data. Each new block is attached to a preceding one in a process that is often computationally demanding. The result is the creation of

[9] GDPR, Recital 23.
[10] GDPR, Recital 24 and Paul Voigt and Axel von dem Bussche, *The EU General Data Protection Regulation (GDPR): A Practical Guide*, 1st ed. (Springer International Publishing, 2017), 22–29.
[11] GDPR, Art. 44.
[12] Christopher Kuner (editor) et al., *The EU General Data Protection Regulation (GDPR): A Commentary* (Oxford University Press, 2020), 757.
[13] GDPR, Art. 45.
[14] GDPR, Art. 46.
[15] GDPR, Art. 47.
[16] GDPR, Art. 40.
[17] GDPR, Art. 42.
[18] Jusic, "Practical Guidance: Data Transfers - Gulf Region," 7.

the 'distributed ledger', i.e. copies of the records of transactions distributed among several participants. There are several types of blockchain. In the permissionless blockchain, for example, records of transactions are transparent, and adding new and removing old records requires the consensus of all participants. In the permissioned type of blockchain, adding and removing new blocks and data need not be based on the consensus of all participants. Regardless, the data recorded in blocks remains private, because it can be accessed only by those in possession of cryptographic keys necessary to decrypt and read the data inside the block.[19]

There are two reasons for blockchain being touted as a revolutionary innovation that will fundamentally alter many industries, and perhaps the entire economy.[20] Firstly, the blockchain is decentralized and disinter mediated, i.e. it allows individuals to directly exchange data without need for an intermediary. Decentralization and disintermediation have made blockchain the technology of choice for the creation of crypto currencies. These crypto currencies enable the direct transfer of value from person to person while bypassing traditional intermediaries such as banks, and, in doing so, 'disrupt' the mainstream financial system and financial industry.[21]

Secondly, the technology behind blockchain provides a significant – albeit not absolute– trustlessness, anonymity and immutability of data records. The participants in blockchain transactions need not know or trust one another in order to enter a transaction. Instead, participants rely on the encryption and immutability of blocks to protect their data from privacy and counterparty risks.[22] The data within blocks is accessible only to those in possession of cryptographic keys, and, in the case of the permissionless blockchain, the immutability of data is protected by the fact that the consensus of all participants is necessary not only for the adding of new blocks to the chain, but also for their removal.[23] From a perspective of privacy protection, the very structure of blockchain *enforces* privacy-by-design and, partially, privacy-by-default.[24]

3. Compliance Issues

As suggested in Part II of this paper, the GDPR and the blockchain share commitment to privacy-by-design and -default. In this part, it is shown that compliance issues have arisen because the blockchain and the GDPR use different methods to ensure privacy-by-design and privacy-by-default. Whereas the blockchain is built on the ideas of disintermediation and decentralization, the philosophy behind the GDPR is the opposite: the GDPR aims for re-intermediation and relative centralization of the data protection process. The focus here is the most significant issues that emerge in the process of ensuring that data transfer using the

[19] Joseph J. Bambara and Paul R. Allen, *Blockchain. A Practical Guide to Developing Business, Law and Technology Solutions* (McGrawHill, 2018), 1–13.
[20] Bernardo Nicolletti, *The Future of Fintech: Integrating Finance and Technology in Financial Services* (Palgrave Macmillan, 2017).
[21] Rainer Böhme et al., "Bitcoin: Economics, Technology, and Governance," *Journal of Economic Perspectives* 29, no. 2 (May 2015): 213–38, https://doi.org/10.1257/jep.29.2.213.
[22] William Mougayar and Vitalik Buterin, *The Business Blockchain: Promise, Practice, and Application of the Next Internet Technology* (1 edition, Wiley 2016).
[23] Kevin Werbach, "Trust, But Verify: Why the Blockchain Needs the Law," *Berkeley Technology Law Journal* 33 (August 1, 2017): 489, https://doi.org/10.2139/ssrn.2844409.
[24] Silvan Jongerius, 'A Primer to GDPR, Blockchain, and the Seven Foundational Principles of Privacy by Design - Dataconomy', https://dataconomy.com/2019/01/a-primer-to-gdpr-blockchain-and-the-seven-foundational-principles-of-privacy-by-design/, accessed 19 May 2021.

blockchain is compliant with the GDPR: data protection impact assessment, issues in identifying and determining the role of sole and joint data controllers and data processors, obstacles to exercising the right to rectification and right to be forgotten, data transfer requirements, and the protection of privacy in the process of creating blockchain-based smart contracts.

3.1. The Data Protection Impact Assessment and the Blockchain

The data protection impact assessment (DPIA) is an exercise in, as GDPR Art. 35 states, "an assessment of the impact of the envisaged processing operations on the protection of personal data." Data controllers are expected to perform a DPIA if data processing will be performed using new technologies and is likely to create high risks for natural subjects' privacy. The DPIA is obligatory if the personal aspects of data will be used for decision-making in an automated process. In general, a DPIA should include a systematic description of the purpose and processes of data processing, an evaluation of privacy risks, information on the necessity and proportionality of the processing operations in relation to the purpose of processing, and measures in place to ensure compliance with the GDPR and to decrease risks to data subjects' and third parties' privacy.[25]

The application of the text of the GDPR's DPIA requirements to the blockchain yields the following implications and presents several questions for the users of the blockchain network and the data controllers.

Firstly, because it has already existed for two decades, blockchain is not an entirely a new technology. Nevertheless, blockchain is a form of automation, and there are a variety of as-yet-untested ways of using the blockchain. Because automation of data processing in untested ways can create unforeseeable adverse consequences for privacy, from the perspective of the GDPR, the blockchain constitutes a new technology. Hence, entities employing blockchain for the handling of data of natural subjects should conduct a DPIA in advance of creating the blockchain network if the data being processed involves the personal data of natural subjects. If the processing system is deemed unlikely to create heightened privacy risks for natural subjects, the conducting of a DPIA may well be redundant.[26]

Secondly, both the data controllers and the natural subjects could question the usefulness of engaging in the DPIA, for following reasons. The tacit assumption behind the DPIA is that those conducting the DPIA can anticipate most privacy risks with some degree of certainty at the time when the DPIA is performed. The natural subjects whose privacy rights are at stake could argue that such assessment of privacy risks leaves determination of the severity of present and future privacy risks in the hands of those that perform the DPIA. In turn, those conducting the DPIA could protest that the periodical or continuous undertaking of DPIAs is a costly, formalistic and risky exercise in assessment of privacy risks in an "experiment-like" environment that does not reflect real-world situations and privacy risks.

[25] Information Commisioner's Office, "Data Protection Impact Assessments" (ICO, January 11, 2021), https://ico.org.uk/for-organisations/guide-to-data-protection/guide-to-the-general-data-protection-regulation-gdpr/accountability-and-governance/data-protection-impact-assessments/.
[26] Tamás Bereczki and Ádám Liber, "Blockchain and the GDPR: Addressing the Compliance Challenge," 2018, https://www.lexology.com/library/detail.aspx?g=571106ac-1aaf-4db9-b1a0-0152848fd040.

3.2. Sole and Joint Data Controllers and Data Processors on the Blockchain

If the philosophy of the blockchain is disintermediation, the philosophy behind the GDPR could be labelled 're-intermediation.' This is because protection of data subjects' rights in the GDPR could be said to rest on the activities of two kinds of data intermediaries: the sole and joint data controllers and data processors.

The GDPR defines a 'data controller' as a natural or legal person or public entity that, alone or jointly with other data controllers, determines the purposes and means of the processing of personal data. The main tasks of the sole or several (joint) data controllers include estimation of privacy risks and implementation of proportionate technical and organizational measures that safeguard data subjects' rights listed in the GDPR. If joint controllers collectively determine the purposes and means of data processing, they should define their roles and responsibilities towards data subjects clearly and in advance. Should joint controllers fail to create a system of distribution of roles and responsibilities, each joint controller becomes responsible for the entirety of the damage to a data subject's privacy rights.[27]

Next in the line of data intermediaries is the data processor, which the GDPR describes as a natural or legal entity that processes personal data on behalf of the data controller. The relationship between the data controller and processor is contractual and largely hierarchical. For example, among many other obligations, the processor is expected to adhere to the controller's documented instructions, preserve data subjects' privacy rights throughout the process of data processing, and control sub-processors, if they are to engage any.[28]

National data protection regulators have suggested that identifying data controllers and processors on the blockchain could be done by classifying those writing on the blockchain as data controllers, while simultaneously treating those validating blockchain entries as data processors.[29] Applying this solution could be relatively straightforward in some cases. Complications ensue, however, when dealing with types of blockchain in which the same entity is simultaneously the data controller and processor.[30] In such cases, according to the GDPR, the data processor could be treated as a data controller, because in this case it is the processor that determines the purpose and means of processing.[31]

If, however, the data subject, controller and processor are merged into a single person or entity, sustaining a distinction between these three roles could be useless. This reveals the extent – and far-reaching impact – of philosophical differences between the blockchain and the GDPR. As boundaries between persons that the GDPR treats as data subject, controller and processor blur, decentralization and disintermediation using the blockchain are more complete. The implication is that the more the data subject, controller and process or merge into one person, the more sovereignty the data subject has over their privacy. At the same time, the regulation of and liability for privacy breaches becomes extremely difficult – if not impossible – to implement.

[27] GDPR Art. 4., 24. and 26.
[28] GDPR Art. 4. and 28.
[29] Commission Nationale Informatique & Libertes, "Premiers éléments d'analyse de la CNIL: Blockchain," 2018, 2, https://www.cnil.fr/sites/default/files/atoms/files/la_blockchain.pdf.2018, 2).
[30] Jusic, "Dealing with Tensions Between the Blockchain and the GDPR," 84.
[31] GDPR, Art. 28. (10).

Without employing intermediaries and a setting up a relatively centralized system for the data protection process, regulators lack the capability to deal directly with a myriad of individual data subjects. The world of data subjects' full sovereignty over privacy might be a world without an effective liability for privacy breaches.

3.3. Rectification and the Right to be Forgotten on the Blockchain

A promise of the near-immutability of the data recorded on the blockchain is among the core reasons for the blockchain's attraction to many users. The right to rectification and the right to erasure of data (i.e. the right to be forgotten), however, are among the most important rights of data subjects enshrined in the GDPR. The right to rectification means that a duty is owed by the data controller to the data subject to correct inaccurate personal data, and that the data subject has a right to request that the controller complete any incomplete personal data.[32] The right to be forgotten implies that, in some situations, the data subject can request the complete erasure of their personal data by the data controller.[33] The immutability of data recorded on the blockchain and the GDPR's right to rectification and erasure were often cited as core incompatibilities between the blockchain and the GDPR. Yet, technical and legal reasons suggest that these incongruities are not as insurmountable as might appear. Firstly, not even the permissionless blockchain – the one in which erasing data recorded in the blocks must be approved by all participants in the blockchain – is perfectly immutable.[34] Furthermore, other types of blockchain, such as the private blockchain, are specifically structured so that they are not fully immutable.[35] Secondly, the GDPR does not contain a precise definition of when data can be deemed to have been fully erased.[36] This issue is an important one, as many techniques for deleting data leave a possibility for data recovery, and thus a potential for abuse. A solution that is both applicable to the blockchain and compliant with the GDPR is to consider data to be erased at the point when the probability of recovering and reusing the data is minimal, even if the total physical deletion of such data is impossible.[37]

3.4. Data Transfers

Arguably *the* reason for blockchain's popularity is that it provides a seamless direct data transfer via the web, i.e. it allows individuals to directly exchange data across borders without the involvement of an intermediary. A disinter mediated, geographically unbound, free-flowing transfer of data is not entirely condoned by the GDPR; the GDPR only permits the transfer of data to third countries or international organizations and onward if relatively stringent conditions have been met.[38] Because data transfer is vital to both the blockchain and the GDPR, reconciling blockchain and GDPR data transfer requirements is – and will likely remain – a thorny issue, for a number of reasons.

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[32] GDPR, Art. 16.
[33] GDPR, Art. 16.
[34] Gideon Greenspan, "The Blockchain Immutability Myth," CoinDesk, May 9, 2017, https://www.coindesk.com/blockchain-immutability-myth.
[35] Grant Thornton, "GDPR & Blockchain," 2018, https://blockchain.grantthornton.es/en/blockchain-gdpr-2/.
[36] cf. Matthias Berberich and Malgorzata Steiner, "Blockchain Technology and the GDPR - How to Reconcile Privacy and Distributed Ledgers," *European Data Protection Law Review (EDPL)* 2 (2016): 426.
[37] (Finck 2018).
[38] (Jusic 2018, 7).

Firstly, the structure of the permissionless blockchain consisting of individual nodes transferring data around the globe makes the application of the GDPR's data transfer requirements unworkable. Some GDPR data transfer mechanisms, such as codes of conduct and certifications, can be more readily applied to company- and government entity-operated private and consortium blockchains. But even then, it is questionable whether such GDPR-approved data transfer mechanisms provide real data protection, or merely an appearance of compliance with the GDPR.[39]

Secondly, there are policy issues and trade-offs. The EU rests on and promotes four freedoms (the free movement of capital, people, goods and services) and the rule of law. As the data is already commoditized, it can be questioned whether the benefits of the free flow of data on the internet can be balanced with privacy rights enshrined within the GDPR, and, if not, whether economic interests or privacy will prevail.[40]

The more fundamental question behind this dilemma is whether individuals who act as both consumers and bearers of privacy rights value privacy at all.[41] The future will answer this question. If the pace and reach of technology-driven consumerism are any guide, it can be argued that data subjects will eventually come to use blockchain (or a similar future privacy-enhancing technology) to demand monetary incentives for unavoidable disclosures and sharing of their personal data.

3.5. Smart contracts

The GDPR does not entirely prohibit decisions made using technology without human involvement (automated decision-making).[42] Automated decision-making is permitted when a data subject explicitly consents to it, if it is authorized by the EU or the Member State law applicable to the data controller responsible for safeguarding the data subject's right, or if it is necessary for contractual relations between the data subject and a controller.[43]
Presently, the emerging technology of smart contracts is among the most important forms of automated decision-making based on the blockchain. Smart contracts use executable codes to resolve a 'trust problem', i.e. to facilitate, execute, and enforce a contract between unknown counterparties without engaging an authoritative third party, such as a government.[44] In yet-to-be-developed versions, smart contracts could be used to seamlessly govern contractual

[39] Sonia Daoui, Thomas Fleinert-Jensen, and Marc Lempérière, "GDPR, Blockchain and the French Data Protection Authority: Many Answers but Some Remaining Questions," 2019, https://stanford-jblp.pubpub.org/pub/gdpr-blockchain-france.
[40] Stan Sater, "Blockchain and the European Union's General Data Protection Regulation: A Chance to Harmonize International Data Flows" (Rochester, NY, November 6, 2017), 38, https://doi.org/10.2139/ssrn.3080987.
[41] Joshua Fairfield and Christoph Engel, "Privacy as a Public Good," *Duke Law Journal* 65, no. 3 (December 1, 2015): 456.
[42] Jusic, "Dealing with Tensions Between the Blockchain and the GDPR," 85.
[43] See GDPR Art. 22 and Finck, "Blockchain and the General Data Protection Regulation," 83–84.
[44] Shafaq Naheed Khan et al., "Blockchain Smart Contracts: Applications, Challenges, and Future Trends," *Peer-to-Peer Networking and Applications*, April 18, 2021, https://doi.org/10.1007/s12083-021-01127-0.

transactions of, for example, transfer of property deeds, currencies, and intellectual property rights.[45]

As the GDPR is not opposed to automated decision making as such, presently the application of the GDPR to smart contracts is an issue of risk management and adjustments to technological advancement. If smart contracts become widely used, however, privacy issues will become more pronounced. In such a scenario, smart contracts will comprise a part of longer transaction chains. Within such transaction chains, it will become progressively more difficult for data subjects to exercise their right to be informed of the use of their data and to ensure that potential data errors can be rectified via exercise of their right to human intervention.[46]

4. Conclusion

The GDPR and the blockchain could be said to be on a same mission: to increase individuals' sense of privacy and autonomy. Methods used to fulfill that mission – re-intermediation and relative centralization in the case of the GDPR, disintermediation and decentralization in the case of the blockchain –differ significantly, however, and may also come into direct conflict with one another. In this paper, it was shown that ensuring compliance with the GDPR while using the blockchain for data processing is not necessarily impossible, despite the seeming irreconcilability. Future research and, more importantly, developments in industry and practice should lead to an investigation of other means of ensuring a heightened level of GDPR-compatible privacy protection when data is processed using the blockchain.

[45] Balázs Bodó, Daniel Gervais, and João Pedro Quintais, "Blockchain and Smart Contracts: The Missing Link in Copyright Licensing?," *International Journal of Law and Information Technology* 26, no. 4 (December 1, 2018): 311–36, https://doi.org/10.1093/ijlit/eay014.
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DISCRIMINATION BASED ON PLACE OF RESIDENCE IN RECENT JURISPRUDENCE OF THE EUROPEAN COURT OF HUMAN RIGHTS WITH EMPHASIS ON BOSNIA AND HERZEGOVINA

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Abstract

Widening case law of the European Court of Human Rights (ECtHR) interpreting the notion of discrimination, especially the ambit of discrimination based on "other status" offers important elements in the understanding of the legal definition of discrimination. More specifically, it offers elements in understanding of the scope of discrimination grounds listed under "other status", such as the place of residence. Discrimination cases before the ECtHR against Bosnia and Herzegovina relate primarily to the discriminatory nature of Bosnia and Herzegovina's election system, focusing on ethnicity as the main basis for discrimination. However, often overlooked is the place of residence as the discriminatory ground, identified in numerous cases alongside ethnicity (such as the cases of Pilav, Zornic and recently Pudaric), or as a stand-alone basis as in the case of Baralija. The ECtHR's positions expressed in judgements to these cases offer certain interpretations important for Bosnia and Herzegovina's election system, legal and constitutional order and showcase the potential power and influence which the ECtHR's judgements may have in the strengthening of rule of law and overcoming political stalemates. Outside Bosnia and Herzegovina, the cases may offer some new insights in defining and reinterpreting the legal notion of discrimination and the legal ambit of the prohibition of discrimination on the grounds of place of residence, such as discriminatory effects of legal void and the discriminatory treatment between persons having a place of residence within the same respondent country.

Keywords

Discrimination · Place of Residence · Right to Free Elections · Rule of Law

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1. Introduction

As a general principle, to which all the Member States of the Council of Europe subscribe, the prohibition of discrimination should be one of the basic pillars of rule of law in any democratic society. As such, it is enshrined in the basic texts of human rights law such as the Convention for the Protection of Human Rights and Fundamental Freedoms (Convention), as well as multiple other general human rights documents and specific anti-discrimination documents. Prohibition of discrimination is a principle recognized by the international documents and case law of international bodies. The unlawful distinction in the treatment of citizens based on an open-ended list of grounds, including place of residence is prohibited and States cannot bring into question should it be allowed that some rights and freedoms are available to certain groups based on where they live.

The case law of the European Court of Human Rights (ECtHR) concerning discrimination on the grounds of place of residence is relatively new, compared to similar grounds that are to be counted under the umbrella of "other status". One of the first cases defining the place of residence as the grounds of discrimination, falling within the open-ended list of "other status," is the case of Carson and Others v. United Kingdom[1] from 2010, followed by other cases, such as the one of Aleksandr Aleksandrov v. Russian Federation[2] from 2018 and, more recently, the case of Baralija[3] from 2019. The case of Pilav[4] and a recent case of Pudaric[5] from 2020 are also noteworthy. Although the primary basis of discrimination in the cases of Pilav and Pudaric was ethnicity, due to specific constitutional arrangements in Bosnia and Herzegovina, the discrimination of applicants based on place of residence is also evident.

Cases finding discrimination based on place of residence have certain distinctions between them, which makes the formulation of a pattern or a unified legal stance an uneasy task. For example, the case of Carson refers to persons having a permanent place of residence outside of the State in question (i.e. the UK). Such situation, for example, may bring into question the issues of personal and territorial application of the Convention and thus open further debate whether the place of residence is an actual basis of discrimination in the concrete case. Furthermore, in the case of Aleksandr Aleksandrov, although the place of residence within the State was evident, the core issue of the case was one of the criminal law proceedings and sentencing, where the particular place of residence (or lack thereof) is taken as an aggravating circumstance in sentencing. These circumstances may call into question discussion on the margin of appreciation in criminal law sentencing practices of the States. The cases related to Bosnia and Herzegovina, on the other hand, could be identified as cases where the place of residence as a discriminatory basis is prominently evident. The applicants in cases of Baralija and Pilav as well as Pudaric all have places of permanent residence within Bosnia and Herzegovina and the justifications set forth by the State were thoroughly examined and rejected by the ECtHR.

[1] *See* Carson and Others v. United Kingdom (GC), Case no. 42184/05, Judgment 16 March 2010.
[2] *See* Aleksandr Aleksandrov v. Russia, Case no. 14431/06, Judgment 27 March 2018.
[3] *See* Baralija v. Bosnia and Herzegovina, Case no. 30100/18, Judgment 29 October 2019.
[4] *See* Pilav v. Bosnia and Herzegovina, Case no. 41939/07, Judgment 9 June 2016.
[5] *See* Pudaric v. Bosnia and Herzegovina, Case no. 55799/18, Judgement 08 December 2020.

In the following text, the most notable cases establishing discrimination on the grounds of place of residence shall be examined and compared, with a particular look into the circumstances and background of cases emanating from Bosnia and Herzegovina. Further point of interest in the article is the influence of ECtHR jurisprudence and the impact of recent case law and its novelties in clarification and reinterpretation of the notion of discrimination and the ambit of discrimination based on "other status" such as place of residence. Another important point, specifically linked to Bosnia and Herzegovina as a primary focus of the article, is the question of whether the ECtHR and its judgements hold the potential to contribute to the efforts of strengthening the rule of law and the search for solutions in order to overcome the constitutional and political stalemates and discriminating situations.

2. The Notion of Discrimination under the Convention and Discrimination Based on Place of Residence

Article 14 of the Convention constitutes a right of an individual not to be discriminated against in the enjoyments of rights and freedoms enshrined within the Convention. Hence, Article 14 complements other substantive provisions, having an "ancillary nature".[6] However, the subsequent practice of the ECtHR gave a wide interpretation to the notion and the scope of the substantive rights in concern. On the other hand, Article 1 of Protocol No. 12 sets the scope of protection against discrimination to "any right set forth by law", introducing a general prohibition of discrimination and a "free-standing right" not to be discriminated against.

The discrimination may present itself in a form of direct or indirect discrimination. Direct discrimination describes a "difference in treatment of persons in analogous, or relevantly similar situations" which is "based on an identifiable characteristic or 'status'", as stated in the case of Biao v. Denmark.[7] Indirect discrimination, however, may appear in disproportionately detrimental effects of a general policy or a measure which, although it may be constructed in neutral terms, results in a discriminatory effect on a particular group, as found in the case of D.H. and Others v. the Czech Republic.[8] Further, discrimination by association may be found in situations where the protected ground in a particular case relates to another person who is connected to the applicant.[9]

In determining the existence of the discrimination, the ECtHR must apply the test to determine whether such difference in treatment can be explained by "an objective and reasonable justification,"[10] as reiterated in the case of Molla Sali v. Greece.[11] The test entails the following questions: 1) has there been a difference in treatment in the situations which are analogous or relevantly similar to the situation at hand; and 2) can such difference be objectively justified, by the means of a legitimate aim, or through the application of proportionate means?

The other person or group of persons compared to whom the applicant is claiming the difference in treatment is called a "comparator". The other group or person do not necessarily

[6] White, R. C. A., Ovey, C., & Jacobs, F. G. (2010), pp. 641.
[7] *See* Biao v. Denmark (GC), Case no. 38590/10, 24 May 2016.
[8] *See* D.H. and Others v. the Czech Republic (GC), Case no. 57325/00, Judgment 13 November 2007.
[9] W. A. Schabas, (2015), pp. 18.
[10] White, R. C. A., Ovey, C., & Jacobs, F. G. (2010), pp. 642.
[11] *See* Molla Sali v. Greece [GC], Case No. 20452/14, Judgment 19 December 2018.

need to be identical, but instead, similar in a manner relevant to the situation, taking into account the nature of the particular complaint.[12]

When it comes to the grounds which may be invoked by seeking protection against discrimination, the Convention and Protocol no. 12 are complementary. Both Article 14 of the Convention and Article 1 of Protocol no. 12 have an open-ended list, as indicated by the inclusion of the phrase "any other status".[13]

The ECtHR developed an extensive case law defining the scope of the "other status", giving an interpretation not limited only to a personal characteristic, which is innate or inherent and unchangeable, as found in the case of Clift v. the United Kingdom,[14] but also covering the circumstances which a person may change, such as the place of residence.[15]

The case law related to discrimination based on place of residence has thus far been mainly, but not exclusively, concerned with the situations which involve the difference in treatment directed at persons who are having permanent residence outside of the State in question. Such was a situation in the much-cited Carson Case.[16] The difference in treatment was directed against a British citizen living abroad and thus not having its pension indexed and adjusted on a periodical basis, but "frozen" at the level existing in the moment when the person left the UK.

Whether the nationals of one Member State who are living abroad are discriminated against by the legal measures of that State may trigger the discussion on the issue of the jurisdiction over these persons exercisable by that State. Such a debate would include the question on the application of jurisdiction *ratione personae*, or jurisdiction based on territoriality, or other links between them and the State in question.[17]

However, the situation in the cases emanating from Bosnia and Herzegovina are substantially different. The applicants in the case of Baralija, as in the case of Pilav and Pudaric, all have their place of residence within the State and are discriminated against other persons who also have their place of residence within the State but reside in a different administrative unit. Hence there is no doubt on the question of whether the territorial, as well as personal jurisdiction, is being triggered.

[12] Arnardóttir, O.M. (2012), pp. 35.
[13] White, R. C. A., Ovey, C., & Jacobs, F. G. (2010), pp. 107.
[14] *See* Clift v. the United Kingdom, Case No. 7205/07, Judgment 13 July 2010.
[15] Gerards, J. (2013), pp. 107.
[16] *See* Carson and Others v. United Kingdom (GC), Case no. 42184/05, Judgment 16 March 2010.
[17] Supra, note 14.

3. Overview of the Case Law of ECtHR Regarding the Place of Residence as a Discriminatory Basis

The case law of ECtHR is regarded as paramount in the development and application of the notion of discrimination as defined by the Convention. Following is an overview of some of the notable cases concerning discrimination based on place of residence.

As previously stated, the case of Carson relates to the situation where applicants, all having permanent residence outside the respondent state (United Kingdom), are denied the incremental annual increase of their pensions which was given to other persons having UK residence. The applicants claimed the violation of Article 1 of Protocol 1 (right to property). However, the main issue turned out to be the place of residence and the issue of whether the place of residence can be considered as a ground for discrimination based on "other status". In paragraph 71 of the Judgement, the ECtHR concluded that the place of residence constitutes an aspect of personal status for the purpose of Article 14 of the Convention. However, the ECtHR treated this issue as the question of whether "country of residence" falls within the meaning of the phrase "other status" found in Article 14", thus distinguishing the application of the laws onto the citizens of different regions within one country[18] to the different application of laws between the applicants having the residency status in another country.

The case of Pilav, on the other hand, was primarily the case of discrimination based on the grounds of ethnicity. However, the facts of the case make the place of residence an important factor. The applicant was precluded from running for the position of one of three members of the Presidency of Bosnia and Herzegovina due to the fact that the member of the Presidency that is voted from the entity of Republic of Srpska is to be an ethnic Serb. The applicant, due to his Bosniak ethnicity, could not run for the position, unless he changed his place of residence to another entity (i.e. the Federation of B&H), from which a Bosniak and a Croat member of the Presidency are voted in. The ECtHR rejected the argument set forth by the respondent State that the applicant could evade discriminatory treatment by changing his place of residence.[19] A more recent case following the logic of the Pilav case is the case of Pudaric. The facts of the case remain similar, but in this case they refer to an applicant who is an ethnic Serb, living in the entity of Federation of B&H, but who is being precluded to run as a Serb member of the Presidency who is elected exclusively from the entity of Republic of Srpska.[20]

The case of Aleksandr Aleksandrov v. Russian Federation, however, has its own specific characteristics. The applicant was found guilty of assaulting a police officer and was sentenced to one year of imprisonment. In determining the sentence, the criminal court took as an aggravating circumstance the fact that the applicant had a place of residence outside of the area where the incident happened (suggesting he wandered to another place to commit offences). Such circumstance was not prescribed by the law as an aggravating circumstance in terms of sentencing. The respondent State, however, claimed that it was not the only factor that the court considered in sentencing, but that it was taken in corroboration with other circumstances under

[18] *See* Carson and Others v. United Kingdom (GC), Case no. 42184/05, Judgment 16 March 2010.
[19] *See* Pilav v. Bosnia and Herzegovina, Case no. 41939/07, Judgment 9 June 2016.
[20] *See* Pudaric v. Bosnia and Herzegovina, Case no. 55799/18, Judgment 08 December 2020.

which the incident occurred (like, for example, the applicant being intoxicated). To sum up, the case basically concerned the sentencing policy of the criminal courts of the country.[21]

It may be said that all the presented cases have their specific characteristics pointing out to the place of residence being the grounds for discrimination; however, all of them having additional factors and circumstances. The case of Baralija, on the other hand, could be regarded as a clear case of discrimination based on the place of residence as a primary basis of discrimination, by (non)application of the same law (the Election Law of Bosnia and Herzegovina) within one State.

Further interesting point set out in the reasoning of the Judgement of the ECtHR is that in the case of Baralija, as opposed to the cases of, for example, Sejdic and Finci, Pilav and other cases, it is not a legal provision currently in force which has the effect of violation of human rights, but rather a legal void or the absence of an applicable legal provision that has produced a violating effect. The Constitutional Court of B&H, in its Decision adopted on 22 September 2004,[22] declared that certain provisions of Election Law of B&H and the Statute of Mostar which were deemed unconstitutional are without further legal effect, thus eliminating them from the legal system. The Decision further set out an obligation to replace the erased provisions with new provisions which are supposed to comply with the human rights standards.
Article 25 of the International Covenant on Social and Political Rights[23] applicable in Bosnia and Herzegovina, on the other hand, creates a positive obligation of the state to ensure free, democratic, and periodical elections[24] and to adopt laws and measures ensuring the enjoyment of the right. Thus, it may be concluded due to the nature of the obligation outlined in Article 25, that is, the presence of the positive obligation of the state to ensure the enjoyment of certain rights, the breach of human rights may exist in the situation of a legal void.

Upon the examination of the established backlog of cases, the ECtHR found a violation based on Article 1 of Protocol no. 12, a provision which extends the scope of the prohibition on discrimination in the fulfilment of the rights set forth by the Convention to include any right "set forth by the law". The prohibition of discrimination in this regard is therefore not limited only to the rights contained in the Convention but represents a general obligation to ensure that rights set out by the state's laws are enjoyed on a non-discriminatory basis.[25]

However, a substantive problem occurs if the wording "set forth by the law" is read narrowly, because not every discriminatory measure or action is "set forth by the law". It can be either the case of a discriminatory practice which is not overtly stated (as in the case of indirect discrimination) or when a discriminatory provision may not exist at all as a positive norm. Such absence of provision (legal void) may produce discriminatory effects, as was a situation in the Case of Baralija.

To overcome the narrow interpretation of the wording "set forth by the law", one must read it in conjunction with the Explanatory Report to Protocol No. 12, which states in Paragraph

[21] *See* Aleksandr Aleksandrov v. Russia, Case no. 14431/06, Judgment 27 March 2018.
[22] Decision by the Constitutional Court of Bosnia and Herzegovina, 22 September 2004, published in the Official Gazette of B&H no. 46/04.
[23] *See*: International Covenant on Civil and Political Rights 1966.
[24] Xenos, D. (2012), pp. 16.
[25] *See* Baralija v. Bosnia and Herzegovina, Case no. 30100/18, Judgment 29 October 2019.

22 that the scope of protection of Article 1 of the Protocol No. 12 concerns four categories of cases, in particular…

> *... where a person is discriminated against:*
>
> *1) In the enjoyment of any right specifically granted to an individual under national law;*
>
> *2) In the enjoyment of a right which may be inferred from a clear obligation of a public authority under national law, that is, where a public authority is under an obligation under national law to behave in a particular manner;*
> *3) By a public authority in the exercise of discretionary power (for example, granting certain subsidies);*
>
> *4) By any other act or omission by a public authority...*[26]

Therefore, when interpreting the facts of the case, in order to determine whether the alleged discrimination falls within one of these four categories, the apparent narrow constraints of the wording "set forth by the law" must be interpreted by the means of wording found in the Explanatory Report. Following the Explanatory Report, it becomes possible to interpret that the wording "...act or omission by a public authority ..."provides for the protection of discriminatory effect produced by omissions of the public authority (i.e. legislative body) in the case of existence of a legal void.

Further, differing from the Sejdic and Finci, Pilav, Zornic and Pudaric cases, in the Baralija case, the primary discriminatory basis is not some characteristic which is innate or inherent to the person claiming to be discriminated against, such as racial or ethnic background, or other feature that makes one group inherently distinguishable from other groups. This case follows the line of decisions giving the wide interpretation and the scope of the basis on which discriminatory treatment may arise. The discriminatory treatment, in this case, is based primarily on residence, which is not an inherent characteristic *per se*; however, as previously established by the ECtHR in the cases such as Carson, the ECtHR holds that the "…place of residence constitutes an aspect of personal status" and is considered to be within the ambition the prohibition of discrimination based on "other status."[27] The applicant, in this case, is discriminated against, compared to other citizens of Bosnia and Herzegovina who are enjoying the protected rights and have had the opportunity to partake in local elections in the previous two cycles.

Not a dissimilar situation was considered in the case of Pilav, where the appellant, a Bosniak with a place of residence in the entity of the Republic of Srpska, was barred from running for the position of Bosniak member of the state presidency. Although the main basis of discrimination, in that case, was on the grounds of the ethnic background of the applicant, the response from the State was that there was no discrimination, since the appellant could have changed his place of residence and run for that position as a candidate from the entity of Federation of Bosnia and Herzegovina.

[26] COE (2000), Explanatory Report to Protocol no. 12, retrieved from: https://rm.coe.int/09000016800cce48.
[27] *See* Carson and Others v. United Kingdom (GC), Case no. 42184/05, Judgment 16 March 2010.

Surely, one could argue that the appellant could move and partake in local elections in another city since the place of residence is not an inherent and unchangeable personal characteristic. However, such reasoning was dismissed in the case of Pilav, where the ECtHR concluded that the appellant has an established life in his place of residence and is under no obligation to forgo it to enjoy certain rights, such as the right to run for office.[28]

4. Specific Traits of the Cases Related to Bosnia and Herzegovina: The Issues of Rule of law, Non-Implementation of Judgements and Political Stalemate

The cases emanating from Bosnia and Herzegovina have certain specific characteristics holding significant legal, as well as political implications for the country. Looking into the cases against Bosnia and Herzegovina in front of the ECtHR related to the issues of discrimination, one cannot overlook some specific issues concerning the rule of law, non-implementation of judgements and consequences of political stalemates. These issues are very much noted and intertwined in the wording of the judgements, which makes them impossible to ignore.

The task of the full respect of human rights of every citizen should be a paramount objective of any democratic society based on the rule of law. However, it has proven itself to be difficult even in societies with long-standing democratic traditions, robust institutions, laws and procedures guaranteeing the rule of law. Further difficulties are faced in the societies undergoing transition, or healing from devastating conflicts which tore the very fabric of society. In the era of peace, at least on the European soil, which followed the conclusion of the Second World War, few conflicts were so devastating to cause such a rupture in the society and escalate mistrust between its ethnic groups as the 1992-1995 war in Bosnia and Herzegovina.

The General Framework Agreement for Peace in Bosnia and Herzegovina (Dayton Peace Agreement), which ended the armed conflict, defined Bosnia and Herzegovina as a state consisting of two entities: Republic of Srpska and Federation of Bosnia and Herzegovina, the latter one being further divided into ten cantons. Besides the two entities, there is a separate administrative unit under State sovereignty, the Brčko District. The Dayton system tries to find a way out of inter-ethnic mistrust and creates a delicate power-sharing mechanism.[29]

The constitutional order of Bosnia and Herzegovina, as well as the very nature of its society and its political structure, is a unique paradigm. Theoretically, it has been described as an asymmetrical consociation society.[30] However, it may be argued that the society of Bosnia and Herzegovina, as well as its constitutional order, may not be defined in terms related to the pure forms of consociational or other models, but instead needs its own model, one which is retaining the protection of the "constituent" peoples as well as protection of rights of all of its citizens (including the "Others"). The implementation of such a model may represent a precondition for the stabilization of Bosnia and Herzegovina's society.[31]

[28] *See* Pilav v. Bosnia and Herzegovina, Case no. 41939/07, Judgment 9 June 2016.
[29] C. Hartzell and M. Hoddie (2003), pp. 319.
[30] M. Kasapović (2005), pp. 77.
[31] Dž. Omerdić (2016), pp. 69.

The delicate compromise of the Dayton Peace Agreement is most visible in the country's election system. The election system of Bosnia and Herzegovina is rather complex and as such, was subject to a lot of scrutiny by the European Court of Human Rights. The constitutional stalemate resulted in discriminatory situations, and the ECtHR was called upon in numerous cases to determine the possible solutions.[32]

The discriminatory nature of Bosnia and Herzegovina's election system is well documented by the case law of ECtHR[33] in the cases like Sejdic and Finci[34]; Pilav; Zornic[35], Baralija and, more recently, Pudaric. It may be said that the issue of the discriminatory nature of Bosnia and Herzegovina's election rules is systemic in its nature. An interesting fact is that the judgements have found discrimination to exist on multiple grounds, most importantly, on the grounds of ethnicity and, more recently, on the grounds of place of residence.

One of the aspects of the constitutional setup of Bosnia and Herzegovina is the provision on direct application of certain human rights instruments, including the European Convention on Human Rights. Such provision has been seen as one of the instruments in rebuilding the country's legal system and the rule of law. Consequently, the jurisprudence of the ECtHR is bound to follow the special status of the Convention in interpretation and application of the Convention provisions and principles in Bosnia and Herzegovina.[36] Such position holds a potential that may be used in the strengthening of the rule of law.[37]

In the reasoning of the judgment in the Baralija case, the ECtHR concludes, in paragraph 62, that the core issue, in this case, is the failure of the State to implement a final and binding decision adopted by the Constitutional Court of B&H. Deliberating on that matter, the ECtHR notes that such practice *"...would be likely to lead to situations that were incompatible with the principle of the rule of law which the Contracting States undertook to respect when they ratified the Convention..."*. [38] The principle of rule of law is one of the core principles invoked in the Preamble of the Convention.

Generally, the notion of the rule of law, in general, may be described as a principle whereby all the members of the society are subject to publicly disclosed laws and procedures which are equally enforced.[39] Thus, as a matter of principle, a final and binding decision of the Constitutional Court is to be implemented, primarily by those specifically tasked to do so by the decision itself, namely the legislative bodies. Anything falling short of that leads to the erosion of the principle within a legal system. Further, it leads to the failure of fulfilment of the

[32] Dž. Omerdić and H. Halilović (2020), pp. 223.
[33] M. Mijić, (2011), pp. 13.
[34] *See* Sejdic and Finci v. Bosnia and Herzegovina (GC), Case no. 2799/06 and 34836/06, Judgement 22 December 2009.
[35] *See* Zornić v. Bosnia and Herzegovina, Case no. 3681/06, Judgement 15 July 2014.
[36] A. Caligiuri and N. Napoletano (2010), pp. 127.
[37] M. A. Shah (2006), pp. 438.
[38] See Baralija v. Bosnia and Herzegovina, Case no. 30100/18, Judgment 29 October 2019.
[39] L.G. Loucades, (2007) pp. 35.

obligation set out by the international law which the State undertook to obey by a manner of joining the Convention, as the ECtHR has concluded.[40]

The complexity of the issue and the difficulty in reaching a solution that would satisfy the once warring communities led to the non-implementation of the Decision adopted by the Constitutional Court of Bosnia and Herzegovina. Referring to it, the ECtHR recalled some of the positions that have been outlined in the response by Bosnia and Herzegovina, further reiterating the stance previously taken in the Sejdic and Finci case. ECtHR held that certain discriminatory aspects of the Constitution need to be amended, further accepting the fact that there is no obligation on the part of Bosnia and Herzegovina to remove all the power-sharing mechanisms and install a simple majority rule. The ECtHR even examined the justifications set out by the Constitutional Court of B&H in the original appeal to the Sejdic and Finci case stating that the overarching principle and the need to maintain peace and dialogue between the communities allows for certain inconsistencies with the Convention standards, pointing that a flawed solution is better than none. One would be compelled to agree with the strong wording of the dissenting opinion to the judgement in the Sejdic and Finci case held by Judge Bonello in which he states that the ECtHR is in danger of removing the "Dayton formula", which seems to give some results, and replacing it with Strasbourg "non-formula,"[41] thus compromising what has been achieved so far in the peace-building process.

The ECtHR, however, even when not fully acceptant, has approached these arguments with a certain degree of understanding and has provided in the very reasoning of the Judgement to the Sejdic and Finci Case certain formulas put forward by the Venice Commission[42] which would remove, or at least reduce, the discriminatory effects of the relevant provisions, while retaining the power-sharing checks and balances.

Again, in the Baralija case, the ECtHR examined justification set out by the State purporting to explain the lack of implementation of the Constitutional Court's decision, as the search for and a need for establishment of a "viable and sustainable power-sharing mechanism", ensuring that none of the ethnicities would receive dominant position within the City of Mostar, especially if that aim is set against the history of the past conflict in that area. The ECtHR nevertheless concluded in paragraph 58 of the Judgement that, even if the complexities of the issues and the difficulties in reaching the political agreement are amounting to the delay in the implementation, such circumstances cannot be taken as sufficient, objective and reasonable justification for the violation of human rights, especially taking into account the fact that such situation has already lasted for a long time.[43]

Although the argument is not expressly stated by the Bosnia and Herzegovina in response to the application in the application in Baralija case, the logic of ECtHR's reasoning is visible and resonating to the Sejdic and Finci reasoning. Even when the discriminatory provisions in question were adopted by the High Representative, the fact that the authorities of Bosnia and

[40] Dž. Omerdić and H. Halilović, (2020), pp. 234.
[41] *See* Sejdic and Finci v. Bosnia and Herzegovina (GC), Case no. 2799/06 and 34836/06, Judgment 22 December 2009, Separate opinion by Judge Bonello.
[42] Supra, note 42.
[43] *See* Baralija v. Bosnia and Herzegovina, Case no. 30100/18, Judgment 29 October 2019.

Herzegovina have at their disposal a legislative mechanism to amend these provisions does not absolve the State from the responsibility for the maintenance of such discriminatory provisions.[44] As stated, at the heart of the issue lays a problem of non-compliance with the final and binding decision adopted by the Constitutional Court of Bosnia and Herzegovina, which is described by the ECtHR as a situation detrimental to the principle of rule of law. Such non-compliance created a legal void, that has amounted to a situation where applicant's rights to free, democratic and periodical elections are violated resulting in discrimination against a category of people based on their place of residence (that is, residents of Mostar). Bosnia and Herzegovina's complex legal system and particular difficulty in reaching a compromise that would allow for the local elections in Mostar to be held is not accepted by ECtHR as a valid justification. The circumstance that the constitutional setup of Bosnia and Herzegovina has a complex origin and the fact that the Mostar City Statute and applicable election rules are imposed by the High Representative do not change the fact that there are mechanisms for the legal and democratic change of those rules. Hence the responsibility for the maintenance of that critical situation remains on the authorities of Bosnia and Herzegovina.

Due to non-compliance with the decision adopted by the Constitutional Court of Bosnia and Herzegovina, the applicant was absolved from the obligation of exhaustion of remedies in the national law, due to their ineffectiveness in this particular case.[45] The ECtHR found a breach of the applicant's rights under article 1 of Protocol 12, finding general discrimination in the enjoyment of provisions of national law. The ECtHR ordered a six-month period in which the Parliamentary Assembly of Bosnia and Herzegovina is to adopt measures that would allow the local elections in Mostar to be held.

Finally, the ECtHR interpreted that under the established laws and practices, the Constitutional Court of Bosnia and Herzegovina has the power to adopt temporary arrangements, thus elevating the position of the Constitutional Court of B&H and hinting at the possibility for it to act as an active legislator, capable of adopting solutions, albeit temporary, which would replace the invalidated provisions, instead of being only seen as a "negative legislator" that is depriving provisions which are inconsistent with the Constitution of their legal validity.[46] Implementation of the judgement has proven itself to be a significant challenge to the authorities in Bosnia and Herzegovina.[47]

Faced with such a situation, political leaders, under scrutiny and guidance of the representatives of the international community found a solution,[48] which was later adopted through the Parliamentary Assembly of Bosnia and Herzegovina,[49] filling the legal void by enacting, apparently, non-discriminatory amendments to the Election Law B&H, thus enabling

[44] *See* Sejdic and Finci v. Bosnia and Herzegovina (GC), Case no. 2799/06 and 34836/06, Judgment 22 December 2009.
[45] D. Shelton, (2006), pp. 89.
[46] K. Trnka, (2010), pp. 117.
[47] Dž. Omerdić and H. Halilović, (2020), pp. 219.
[48] EU Delegation to Bosnia and Herzegovina (2020), Press release, 17 June 2020, Retrieved from: http://europa.ba/?p=69147, Accessed February 2021.
[49] COE (2020), Press release, 9 July 2020, Retrieved from: https://www.coe.int/en/web/portal/-/mostar-congress-spokespersons-welcome-adoption-of-amendments-to-the-election-law-of-bosnia-and-herzegovina, Accessed February 2021.

the elections in Mostar to be held in the 2020 local elections cycle.[50] This could be viewed as a positive sign and one of the potential influences of the ECtHR judgments in the rebuilding of rule of law; however, it has to be noted that the solution to Sejdic and Finci, and connected to it, the Pilav, Pudaric and Zornic cases, is proven to be more difficult.

It is not uncommon in comparative legal and political practice that the highest courts within the country, as well as courts and other judicial or non-judicial bodies when deliberating on certain important issues, can leave a profound mark on the political system and the society as well. Moreover, supreme courts and constitutional courts in numerous countries do have a history of intervening in their respective legal systems. Supreme courts and international courts, especially those adjudicating on human rights, including the ECtHR, have previously found themselves under criticism for "judicial activism". In Bosnia and Herzegovina, however, the activity of the Constitutional Court of B&H as an active legislator is rather limited. The ECtHR hinted in the Baralija judgement that the Constitutional Court of B&H should step in and offer solutions. However, the country is facing a problem of a different nature. Instead of having a problem of "active judicial legislation", there is a problem of non-implementation of final and binding judgements.

The ECtHR is not keen on instructing countries how to solve political issues. However, in the judgement to the Sejdic-Finci case, the ECtHR, rather uncharacteristically, referred to the solutions offered by the Venice Commission as possible solutions for the political stalemate in finding the way out of the political deadlock related to election rules, discrimination and functioning of the three-person presidency of Bosnia and Herzegovina. The political conflicts and stalemates in finding the solutions which would implement the decisions of both the Constitutional Court of Bosnia and Herzegovina and the ECtHR are likely to continue and rise. Many of the proposed solutions, including the aforementioned one offered by the Venice Commission, have been rejected. The global political situation, as well as the relations within the region of Western Balkans and within Europe itself, are getting more complex. Already strained relations between the political representatives are worsened by the lack of any newly proposed solutions and by the regression into more incendiary rhetoric.

However, it is an opportunity for the Council of Europe and the ECtHR to have a significant influence. The Council of Europe mechanism of oversight of the compliance and implementation of the ECtHR judgements produces international political pressure and a constant reminder on the unfulfilled tasks. Backed with legal argumentation of the ECtHR judgement, the reminder alerts the public on the outstanding obligations and human rights issues.

Furthermore, the inclusion of the requirements on the respect of the rule of law and implementation of judgements and the conditionality embedded by the European Union within the legal instruments related to the accession process puts the topic of human rights in a more prominent spot. Although a separate legal and political structure from the Council of Europe, the European Union relies on the fundamental principles found in the ECtHR. Further, it embeds the

[50] COE (2020), Press release, 22 December 2020, Retrieved from: https://www.coe.int/en/web/congress/news-2020/-/asset_publisher/XLGtwSgAs7nz/content/-mostar-made-the-first-step-towards-a-return-to-democratic-normality-says-congress-president, Accessed February 2021.

principles of the rule of law in the instruments such as Stabilization and Association Agreements concluded with the countries of Western Balkans.

To conclude, it is likely that the stalemate in finding solutions in the outstanding cases related to the rules of the election system of Bosnia and Herzegovina will not be ended soon. The political positions are drifting furthermore. However, the case of Baralija may show a positive example of how a judgement by the ECtHR, with its legal strength and clarity, coupled with the international pressure by the Council of Europe mechanisms and the conditionality applied by the European Union, may lead to positive developments.

5. Conclusion

The jurisprudence of ECtHR leaves a mark and points a way for national legislative and judicial bodies to develop their own human rights jurisprudence.[51] The Convention and the European Court of Human Rights in application and interpretation of the Convention have proven themselves to be of great importance, contributing to the search for a solution of legal and political stalemates.[52]

Legal implications of the judgements of the ECtHR, dealing with discriminatory aspects of the election system of Bosnia and Herzegovina on the legal order of the Bosnia and Herzegovina, have proven to be significant. The constitutional order in post-conflict societies such as Bosnia and Herzegovina have certain specific elements that reflect on the nature of such society and obstacles it strives to overcome.

The election system of Bosnia and Herzegovina, in its preoccupation with the position of the "constituent peoples" and check and balances which sought to ameliorate the ethnic mistrust, is repeatedly found to produce discriminatory effects to the "others", namely persons not declaring to belong to one of the "constituent peoples".[53] However, as stated, the election system produced a discriminatory stalemate resulting in the situation where even the members of the "constituent peoples" are discriminated against based on "other status", namely, their place of residence. Following the Judgement in the Case of Baralija and the interpretation of the ECtHR which has given the Constitutional Court of Bosnia and Herzegovina the possibility to enact interim arrangements, local leaders, under pressure and guidance from the representatives of the international community, found the solution to the Mostar elections which were held in 2020.

Unfortunately, the solution to other cases related to the election system of Bosnia and Herzegovina is still in waiting. Bosnia and Herzegovina has a characteristically complex constitutional order and discriminatory situations which resulted from its complex election system might have no comparable cases with elements of equal legal nature and societal structure.

However, the experience of the process which started by defining the discriminatory practice in the judgement of the ECtHR and went on to overcoming of such a situation through

[51] H. Keller and A. Stone-Sweet (2008), pp. 14.
[52] S. Graziadei (2017), pp. 208.
[53] L. Sadiković (2015), pp. 6.

the democratic legislative process is a sign of the ECtHR's influence in strengthening the rule of law and overcoming political stalemates. It is a possible example in similar cases and a sign that international scrutiny applied by Council of Europe and the conditionality embedded in the accession agreements with the European Union can, in the end, give a way out of political deadlocks.

Stepping outside Bosnia and Herzegovina, the widening case law of the ECtHR concerning the notion of discrimination has brought some new important elements for its understanding and interpretation. The place of residence as grounds for discrimination based on "other status" has been reaffirmed in a way that reiterates the discrimination of residents within the State, not just of the nationals of the State having residence abroad, or to aspects related to criminal proceedings. The understanding of ECtHR gives way to broaden the notion of discrimination on the grounds of place of residence, making it firmly a part of the "other personal status", giving protection to the persons having different treatment by the same law within the borders of one respondent state.

The position held by the ECtHR that a legal void can produce discriminatory effects is helpful in the understanding of the notion of discrimination, especially in the cases which result from the non-implementation of final and binding decisions of the country's highest court, which may be defined as a situation contrary to the principle of the rule of law.

The EctHR's condemnation of the State's inactivity in adopting necessary measures needed to fill a discriminatory situation produced by legal void and the Court's reaffirmation of the paramount importance of the rule of law is particularly needed in the societies undergoing transition. In Bosnia and Herzegovina, the political stalemate in finding solutions to the outstanding cases of discrimination is likely to continue; however, a seemingly positive precedent is set in the case of Mostar which can be used as an example going forward.

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SETTLEMENT PROCEDURE IN TURKISH COMPETITION LAW

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Abstract

Settlement procedure, whose legal basis is to be found in the Law No. 4054 on the Protection of Competition, is conceptually discussed in this article by focusing on its legal nature and comparing it to other alternative dispute resolution methods. Our study in this article is limited to competition law, with settlement procedure being the most used procedure in the European Union (EU) and the United States of America (USA) in this area of law. The study, which was based on the Law No. 4054 on the Protection of Competition, was completed by making maximum use of the scholarly works on the subject.

In the study, comparisons have been made with EU competition law on how the settlement procedure can be conducted in Turkish Competition Law. The regulations in the Draft are also discussed while making a comparison. The settlement procedure, which did not have a legal basis before in Competition Law, has been evaluated in the light of the decisions in which leniency programs are implemented in current practice. In Turkish Competition Law, the problems that may be encountered in the implementation of the settlement procedure regulated by the Law No. 4054 on the Protection of Competition and suggestions on the solution of these problems are included.

Keywords

Competition Law · Settlement Procedure · Leniency Programs

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1. Introduction

The settlement procedure's basic aim is resolving the dispute resolution effectively and quickly, while optimal use of resources is ensured. This situation creates a view of the procedural savings. With the settlement procedure regulated in the article 43 in the Competition Law No.4054, it is possible to implement the procedure within the legal framework. Comparative explanations are given as to whether there is a need for settlement procedure in this context, with the leniency program and penalty regulation mechanisms that the regulation on settlement, which is a new procedure to Turkish competition legislation, is closely related.

In the study, the concept of settlement procedure is addressed within the framework of the procedure, the spread of the settlement procedure throughout the Turkish competition legislation, and the country's practices and the evaluations in the doctrine. In this context, in terms of which components will be included in the settlement setup, where the settlement envisaged in the draft is separated from the European Union (EU) and the United States (USA) practices, how the process will be operated and managed, whether it can find actual application areas in the presence of current and planned regulations. Explanations were made on the secondary regulations regarding the process. A comparative analysis of the EU draft law with the Law No. 4054 is included, and suggestions are given regarding the problems that may be encountered in practice and their solutions.

2. What is Settlement Procedure?

Settlement, in terms of word meaning, refers to the fact that more than one person may resolve the existing or future differences of thought and interest by making mutual compromises in order to resolve the dispute.[1] The definition and scope of settlement in the Competition Terms Dictionary is explained as follows: "Within the scope of the plea agreement/settlement, which is generally used in cartel investigations, discounts are determined within the framework of criteria such as application orders and maximum sanctions that can be applied. The settlement that the interested parties have agreed to avoid possibilities such as the emergence of their trade secrets, deterioration of their public image and exposure to more severe sanctions, especially the maximum punishment, at the end of a very costly investigation process has also benefits in terms of competition authorities.

With the benefits of cooperation, such as preventing unnecessary extension of files, enabling competition authorities to obtain precise evidence, provide effective use of public resources. However, despite these benefits, there are also criticisms of settlement. Some of these criticisms are the damage to the defense rights and the reduction of the deterrence."[2] The settlement procedure is designed to create an effective way to prevent cases of violation of the Competition Law as a result of cartelization. Cartel screening techniques are "structural, economic and statistical studies carried out in order to identify markets that might face

[1] Candan Turgut, *Taxation Methods and Settlement* (Istanbul: Finance and Law Publications, 2006), 260; "Candan Turgut, Settlement I," *Finance Post*, No:271(13) (1991): 61; E. Yılmaz,, "*Evaluation of the Settlement Procedure in Terms of Legal Nature and Basic Taxation Principles*," GÜHF Review, Vol.13(1-2) (2009): 322.
[2] *Competition Terms Dictionary*, Revised Sixth Ed. (Ankara: Competition Board, 2019), 151.

competition problems and undertakings that may have adopted practices restricting competition.[3] Basically in cartel scanning techniques; information such as price, cost, market share, tender offers are evaluated by statistical methods and it is investigated whether the data provide signs of the existence of an inter-competitive anti-competitive agreement. In this context, some features that affect the cartelization tendencies such as the number of producers, product homogeneity, and demand predictability are scanned. In addition to these data, the existence of factors such as parallels between enterprise behaviors, regional differences or significant breaks in the data are investigated. According to the results of screening techniques, it is decided whether the market examined is worth examining more closely."[4]

The competition authority stated that the settlement was not used as a platform to detect the existence of the violation or to negotiate it regarding the level of fines or sanctions.[5] The EU Commission's message on this issue is clear: "These meetings are not about negotiation or discussion. The Commission will not negotiate the evidence or objections."[6] Therefore, "*settlement*" in the settlement procedure does not imply bargaining in general. The measures committed to the Commission are subjected to market analysis to show that this procedure is not the result of hidden bargains behind closed doors. When talking about the "*meetings*" factor in the settlement procedure, only the interaction and negotiations between the competition authority and undertakings are meant.

The beginning of a successful settlement means that undertakings accept their responsibilities in joining the cartel and in violation. After the undertakings acknowledge that they have violated, they are expected to arrive at a common solution in which serious legal consequences are accepted. An undertaking applying for a settlement submission must waive some rights in the compromise, for example it cannot request an Oral Hearing. However, the right of appeals to the undertakings is kept separate due to the acceptance of the responsibilities of the undertakings in violation, and their appeal is not blocked. Within the context of the settlement procedure, the problem arises from the settlement procedure, as it is unthinkable that the compromising parties can waive their right to object to the main issue[7] and the resolution of cartel cases is also burdensome for the undertakings. Therefore, the appeal that is the final appeal rights are reserved. However, a problem will be raised here. An undertaking that has agreed to compromise is an undertaking that has also accepted the existence of a violation. The appeal of the decision to be made by the competition authorities at this point causes controversy.[8]

A major factor, without encouraging undertakings to participate in the settlement procedure, is for a 10% fine reduction in response to settlement and cartel violations. Meanwhile, up to 10% fine reduction is not as generous as in other legal remedies (click, the amount of

[3] Leniency Regulation, Article 3.
[4] Competition Terms Dictionary, 151.
[5] Greg Olsen and Mark Jephcott, "Sharing the Benefits of Procedural Economy: The European Commission's Settlement Procedure." *Antitrust* 25 (2010): 76.
[6] Neelie Kroes, Assessment of and Perspectives for Competition Policy in Europe - Celebration of 50th Anniversary of the Treaty of Rome (Speech, November 2007).
[7] A. Scordamaglia, "The New Commission Settlement Procedure for Cartels: A Critical Assessment," *Global Antitrust Review* No. 2 (2009): 78.
[8] R. Zheng, *Settlement Procedure in EU Commission's Competition Law Enforcement - A 'Negotiation Game' between the Commission and Cartelists* (Europa Kolleg Hamburg, 2017): 21.

compensation appreciated by concrete case) that can reduce the deterrence of the settlement procedure.[9] The settlement procedure works in three meeting rounds, with the undertakings communicating with the Commission on the definition and scope of the violation and an appropriate amount of punishment to achieve a common solution.[10] Theoretically, it is an indisputable fact that when the settlement procedure is initiated, the undertakings concerned are engaged in certain illegal activities. The appropriate amount of punishment is based on the extent and severity of the existing violations and, of course, on the calculation of fines executed by the competition authority. Unless a settlement application is filed, the undertaking has the freedom to give up, while the competition authority maintains its flexibility to end compromise throughout the entire process. For example, in the *Smart Cards Chips*[11] *case The Commission has announced that it has stopped meetings on the grounds that they have not been able to record a stage and returned to the standard procedure. Again, in the Animal Feed Phosphates case*[12] the undertaking that participated in the meeting decided to leave the settlement desk. However, upon the initiation of the settlement procedure in 2008, hesitations about its effectiveness arose. If the Commission will continue its stated position on the meeting, a 10% reduction in the penalty for them will not seem sufficient incentive for them to reach an agreement after the settlement decision has been made.

In summary, it can be thought that despite the uncertainty/gap in the meeting, the Competition Board may not be evaluated in terms of undertakings, despite the "authority" position of the compromise procedure, away from "bargaining". It is likely that there is an uncertain area for undertakings regarding the scope of violation and punishment. The settlement procedure is the “negotiation” game between the competition authority and the cartels. We think that this uncertainty can be prevented by mutual concessions in this game process.

2.1. What is The Legal Structure of Settlement Procedure in Turkey?

Settlement means that the disputes that exist as words end in peace. Settlement[13] expresses the agreement of the competition authority with the undertakings by reducing the penalties in return for the acceptance of the violation by the undertakings in the competition law and the cooperation with the Board. In cases where the agreement exists, the existence of a legal contract cannot be disputed. It is not clearly revealed on which basis the legal nature of this contract concluded. Achieving a compromise agreement between the competition authority and undertakings is in a sense similar to a settlement institution in Tax Law. In Turkish Tax Law; discussing and resolving the dispute between the taxpayer and the administration by offering peaceful solutions within the framework of administrative control principles between the parties, without going through a trial; Accordingly, the “*settlement institution*”, which can be defined as the settlement of tax original and penalty, is one of the best examples of settlement ways in

[9] S. P. Brankin, “The First Cases under the Commission’s Cartel Settlement Procedure: Problems Solved?” *E.C.L.R.* 32(4) (2011): 5.
[10] “Commission Statement on the Implementation of Decision Making Procedures for the Adoption of Decisions in cartel cases according to Articles 7 and 23 of Council Regulation (EC) No 1/2003,” 2008, para.5.
[11] *Smart Card Chips*, Case 39.574 965 (The decision is not publicly available); See the page that the commission published: IP/14/960.
[12] Commission Decision of 20 July 2010, Com. (2010) 5004.
[13] Ejder Yılmaz,, *Legal Dictionary* (Ankara, Yetkin Publishing: 2015), 327.

Turkish law.[14] In this sense, it is necessary to examine the settlement agreement as arranged in the settlement agreement applied in Tax Law.

The settlement procedure offers an administrative solution system that is important for the non-dispute settlement of the dispute in our Competition Law. However, the legal nature of the compromise and its current position in the competition system, its importance in practice, and its impact on Competition Law have not been discussed. The settlement procedure has definitive results for the administration / competition authority and undertakings and directly affects the provision of a healthy competition environment and punishment processes in competition law.[15] For the reasons listed, the settlement procedure needs to be discussed as a whole both in terms of its legal quality and its effects on the application. It is an imperative to present the legal nature of a legal institution correctly, to make accurate evaluations related to settlement and to conclude.

The relationship between competition law and administrative law consists of tight and strong ties. The reason for this is "*Competition Law is a special application area of Administrative Law and in this context, a 'special administrative law' discipline.*"[16]It is not possible to accept that the settlement institution is an administrative process. The reason for this is that the administrative process, which is a public law regulation, occurs with a unilateral declaration of will, without the consent of the other party. However, mutual consent is sought in compromise.[17] While the settlement meetings are going on, there is an undertaking on the one hand, although there is a competition authority on behalf of the administration, and on the other hand, there is an undertaking, and the written report reflects the will of both the administration and the enterprise. For these reasons, it is not possible to accept the settlement institution, which does not have the characteristics of the administrative procedure. Even if it is possible to claim that the settlement occurs with a mutual declaration of will, the competition authority and undertakings overlap with the mutually declared wills, aiming to have the same legal result, the settlement procedure differs from this. This is because in order for a contract to qualify as an administrative contract, it is necessary to grant powers to perform the public service of the contract and exceed the powers of the administration-specific law.[18] Settlement has nothing to do with the execution of public service and it is not possible for the competition authority to grant superior rights that exceed private law powers.[19]

The undertaking with the competition authority, by revealing their will to end the violation, meetings on a common ground and make these wills applicable with a settlement submission. In our opinion, if we compare the establishment of settlement to a type of agreement, it can be said that it can be compared to the "*peace contract*" in Civil Jurisdiction Law, but it still remains weak to fully reflect the legal nature of the settlement procedure.

[14] Metin Pektas, *An Alternative Way in Competition Law: Settlement* (Ankara: Competition Authority Specialization Theses Series: 2008), 7.
[15] Yılmaz, *Legal Dictionary*, 327 (n. 13).
[16] M.Ates, "Relation of Competition Law with Administrative Law," in *Introduction to Competition Law* (Ankara: Adalet Publishing, 2013), 181.
[17] D.Şenyüz, *Tax Criminal Law* (Bursa: Ekin Publishing, 2005) 191.
[18] Kemal Gözler, *Introduction to Law* (Ekin Publishing, 2018), 385.
[19] Şenyüz, *Tax Criminal Law*, 191 (n. 17).

The compromise, which is the alternative solution of the Criminal Law, the pre-payment and the alternative dispute resolution way of the Competition Law, contains various similarities. However, it is not possible to match the settlement procedure with the prepayment system in terms of its legal nature. In the pre-payment, the perpetrator accepts or refuses to pay the amount of the penalty, which is determined unilaterally and in advance. On the other hand settlement procedure accepts that the undertaking has committed a violation and discusses the amount of the penalty to be imposed by sitting at the same table as the competition authority. Unlike pre-payment, there is no acceptance or rejection of unilaterally determined punishment in settlement. In the event that the will of the parties coincides, both parties endure sacrifices by giving up certain rights. As a result, some advantages are obtained. In this case, it is not possible for one side to force the other's will or be superior to the other. The parties are in an equal position in the settlement institution.[20] It is not possible to compare it to the prepayment institution in Criminal Law due to its legal nature due to the listed reasons.

Competition Law, with its own rules and practice, is important in our legal system. Competition Law is closely related to private law as well as other branches of public law. The connection of Competition Law with public law or private law does not limit its independence. Competition Law, which has its own rules, institutions, terminology and objectives, is an independent discipline, and the contract concluded between the undertaking and the competition authority as a result of settlement meetings is not an administrative contract in administrative law nor is it a civil contract in civil law. The settlement agreement is a contract with sui generis, which has its own characteristics and quality, which is suitable for evaluation in the category of anonymous contracts.[21] In our opinion, it is the most appropriate approach to accept that the settlement procedure is a unique institution of Competition Law.

[20] A. Erol, *Turkish Tax System and Tax Law* (Ankara: Yaklaşım Publishing, 2008), 134.
[21] Yılmaz, *Legal Dictionary*, 335 (n. 13).

3. Examination of Turkish and EU Competition Law Settlement Procedure Within The Framework Of Comparative Analysis

	Judicial Review	**Discount in the amount of the penalty**	**Scope of the Settlement Procedure**	**Arrangement of the Settlement Procedure**
Settlement Procedure in EU Competition Law	It is possible to refer the decision made as a result of the settlement to the appeal.	10% penalty discount is provided.	The main purpose is to ensure faster and more efficient conclusion of cartel files.	It is regulated by the Statute and Regulations numbered 1/2003.
Settlement Procedure in Turkish Competition Law	It is stipulated in the text of the law that they waive their right to legal remedy.	25% penalty discount is provided.	It has been defined to include all types of violations (art. 4 and art. 6) defined in the Law No. 4054..	It is regulated in the Law No. 4054.

Table 1: Comparison of EU Material Law and the Settlement Procedure Regulated in Law No. 4054

In the justification of Article 4 of Law No. 4054 includes:

> *For the purpose of the article, the agreement has been used to mean any compromise or agreement on which the parties feel bound, even if it does not comply with the validity conditions of the Turkish Civil Law.*

In this sense, in the understanding of Turkish Competition Law, it has been defined as an alternative concept that is intended to be used to prevent agreements between competitors that restrict competition. Along with the 2020 amendment to the Act on the Protection of Competition, with the provision of Article 43, under the heading of "Starting an Investigation, Commitment and Settlement", the settlement procedure, which has not been applied before in Turkish competition law, has been ruled. According to this,

> *Article 43/5: After starting the investigation, the Board, upon the request of the concerned parties or ex officio, may initiate the settlement procedure, taking into account the procedural benefits that may arise from the rapid completion of the investigation process and the differences of opinion regarding the existence or scope of the violation. The Board may reconcile with the undertakings or associations of undertakings about whom an investigation has been initiated and*

> *which acknowledges the existence and scope of the violation until the notification of the investigation report.*
> *43/6: In this context, the Board gives a certain period of time to the parties investigated to submit a compromise text in which they acknowledge the existence and scope of the violation. Notifications made after the given time has elapsed will not be taken into account. The investigation is terminated with a final decision containing a violation determination and administrative fine.*
> *43/7:As a result of the settlement procedure, a reduction of up to twenty-five percent can be applied to administrative fines. The fact that a reduction in the amount of administrative fines is applied in accordance with this article does not prevent the reduction within the scope of the sixth paragraph of Article 17 of the Law No.5326.*
> *43/8: In the event that the process is concluded with settlement, the administrative fine and the matters included in the settlement paper cannot be subject to litigation by the parties of the settlement.*
> *43/9: Other procedures and principles regarding settlement procedure are determined by the regulation issued by the Board.*

3.1. Nature of the Violation-Just for Cartels?

In the Law No. 4054, it was regulated how the way of settlement would work with the amendment dated 24.06.2020. Article 43 of the Law is stipulated that,

> *The Board is conducting an investigation and the undertaking must accept the existence of the violation and make it a subject of discussion. Undertakings or associations of undertakings that acknowledge that they have committed a violation can mutually agree with the Competition Authority until the notification of the investigation report*.

Unlike the Draft, after the initiation of the investigation, it is regulated that the Board can initiate the settlement procedure, upon the request of the relevant persons or ex officio, by taking into account the procedural benefits arising from the rapid completion of the investigation process and the differences of opinion regarding the existence or scope of the violation.[22] Efficacy from the procedural benefits, which is the purpose of the settlement procedure, is stated under the provision in the Law No. 4054.

Settlement procedure is regulated in EU legislation with leniency programs and is only applied for cartel cases. The Regulation No. 622/2008 shows that the settlement procedure is a mechanism established to enable the Commission to terminate cartel cases in a shorter and more effective time period. It is noteworthy that while in the EU legislation, the settlement is regulated solely for cartel cases, in the Turkish Competition Law the settlement is designed to cover all types of violations regulated in the Law No. 4054. All investigations under article 4 and article 6 of the Law will be made possible to be concluded by settlement.[23] In the regulation of the Law, it is foreseen that the settlement will be appointed in the period from the decision to open an

[22] Regulation 622/2008, para.4.
[23] E., Ince and N. Unubol, "Settlement: Journey to Uncertainty," *Competition Journal* Vol. 16, No. 4 (2015): 53.

investigation to the notification of the investigation report, but there is no provision for the waiver of the Oral Hearing and written defense right or the right to enter the file, which the Law allows for undertakings during the investigation phase.[24] It can be stated that the files based on the effects of the settlement in the Turkish Competition Law in a stage before the notification of the investigation report may leave the boundaries of the actual implementation of the files. This thought has two pillars: First, the settlement decisions that adopt a different procedure than the standard investigation in stages consist of violation decisions. The fact that the competition authority expresses its opinions regarding the violation clearly removes hesitations in terms of the acceptance of the violation. In terms of the files based on their effects, the detection of the violation often becomes clear in the investigation report, which requires considerable time. It can be said that the cases of abuse of the dominant position will be more appropriate for the settlement procedure, as the situation in question is taken into consideration at a stage after the notification of the investigation report. Although there is no legal basis for the settlement, which is described as "*early decision agreement*" in England; the settlement scenario develops over the cases faced by the Commission in practice. In the UK, settlement is implemented in a way to include violations other than cartel formations, depending on the nature of the concrete event, and can be initiated at a stage before or after the reporting of the investigation report.[25] In this context, it is noteworthy that if the settlement procedure is foreseen to operate before the investigation report, the primary scope of application is cartel cases associated with the leniency program.[26] Considering the regulation of the law, it is predicted that the scope of application will be limited to a high rate of cartel cases, and will not be able to find a field of application, especially in cases requiring impact-based assessment, by foreseeing the settlement procedure in a period before the notification of the investigation report. Considering that the settlement procedure can be applied in cartel cases (also in cases with a high rate of leniency in this context), the period given for the preparation of the investigation report is limited to a period of 6 months as regulated in the Law No. 4054. It was believed that the Competition Board would become stronger. With the new regulation in Article 43, no changes were made within a period of 6 months.

3.2. Discount from the Fines

In Article 43/9 of the Law, it is regulated that the administrative fine and the issues existing in the settlement agreement will not be subject to litigation if the process is concluded with compromise. While the legislation regulates the provision of 10% reduction on the agreed fine for the undertaking that has come to a settlement table; Unlike the Draft, it was decided that a 25% discount would be applied. The Draft does not include any discount rates, only it is stated that an administrative fine will be agreed with the undertaking. Acknowledgment of the violation and the provision of a penalty reduction, which is a reward as a result of acceptance, are among the basic elements of the settlement procedure. Providing sufficient benefits and incentives for undertakings to choose the settlement procedure is a requirement for an effective settlement. In addition, undertakings that reached a compromise with the Board in accordance with the Draft did not know what kind of advantages they would gain, in other words, there were uncertainties

[24] Ibid., 55.
[25] Ibid., 63.
[26] Ibid.

as to whether the penalty amount to be provided for the undertakings would be reduced or not. The fact that the penalty reduction, which is one of the most fundamental principles of the settlement procedure, was not handled as a provision of law in the Law No. 4054 suggested that it could create problems for implementation. As a result of settlement with Law No. 4054, a reduction of up to 25% in administrative fines may be applied. In the Draft, there was the expression "agreed administrative fine". Contrary to the practice of EU competition law, it was concluded that the amount foreseen for the administrative fine could be negotiated. However, with the amendment, the rate determined as a result of the settlement has been clarified. In the regulation of the commission, it was clearly stated at the settlement table that no meetings were made with the undertakings in terms of the amount of the penalty. In accordance with the provisions of EU law regarding penalties on the nature of the violation, the minimum and maximum amount of the penalty was calculated and imposed on the attempt and the undertaking's statement stating that they accepted the maximum amount of penalty determined by the Commission in the settlement submission was required to be submitted at the time of settlement meetings.[27] As can be seen in the recent decisions made by the Commission[28] a reduction of more than the determined rate of 10%, which was limited in the EU settlement system, was achieved. In the confession bargain held in the USA, the reduction rate provided in the penalty amount over a fixed rate of 10%, which is the measure regulated in the EU competition law, was not foreseen, it was decided that a discount would be provided according to the severity of the violation, the impact of the violation attempts and the bargaining power. Therefore, the rates in the last three decisions will be possible to change within the implemented leniency programs, as well as the weight, effect of concrete violation, etc. as in the confession bargaining procedure in the USA. The discount rate is also regulated for reasons.[29]

Although it is thought that one of the parties that will sit at the settlement table with the undertaking is the Board, in practice, it is not thought that the interlocutors and the Board sit at a table and participate in the settlement. It is expected to reach a decision by taking into account the issues agreed with the Board in the process of making the final decision through the execution of the relevant units of the Board or the appointment of conciliators to the investigation, taking the practice of the EU Commission as an example. Therefore, it is considered that the agreement on the amount of administrative fines determined by the undertaking will restrict the discretionary power of the Board. It is important for a third person to achieve compromise at the point of ensuring impartiality and independence. The conciliator to be appointed bears the responsibility of always being neutral towards the parties to the dispute. The fact that these are third parties by the Competition Board will ensure that independent decisions are made at the point of resolution of the dispute, while leaving the Competition Board to third parties to reach a result quickly and effectively with the settlement procedure will be beneficial in terms of both the workload and the use of resources. As in mediation, these people should be resolved by experts who are well-versed and knowledgeable in Law No. 4054, as well as graduates of law faculties.[30]

[27] Ibid., 55.
[28] Press Release of the EU Commission, http://europa.eu/rapid/press-release_IP-18-6844_en.htm; Press release of the EU Commission, http://europa.eu/rapid/press-release_IP-19-1828_en.htm; AB Komisyonu basın bildirisi http://europa.eu/rapid/press-release_IP-18-4601_en.htm.
[29] Ince and Unubol, "Settlement: Journey to Uncertainty," 56 (n. 23).
[30] Regulation on Mediation Law in Legal Disputes, art. 42.

3.3. Waiver of Appeal is Possible?

In EU law, the Commission uses the settlement to eliminate some procedural steps included in the standard procedure. The aim is to resolve the violation quickly and effectively. With the help of the settlement procedure of cartel investigations, cases that are terminated faster and the resource savings achieved will be used to detect other cartel cases and deterrence will be increased.[31] Unlike the US competition law, the right to judicial remedy is a right that can be exercised after the final decision is made, rather than the investigation stage, in which the only right to waive the undertakings is a judicial remedy against the final decision. In terms of settlement scenarios, the regulated Oral Hearing, entry to the file etc. while procedural rights pertain to the processes currently underway in terms of authority; The waiver of the right to apply for a judicial remedy is related to the process in which the courts decide, and envisages a waiver of the right in this context.[32] The semi-judicial system, which exists in competition law systems carried out by administrative institutions, is the main argument often defended against the criticism of the undertaking that it harms the right to a fair trial; In the US practice, where cartel cases are criminalized and the criminal dimensions go up to prison sentences, the system called "plea-bargain", where the final decision is made by the competent courts at the end of the settlement and the waiver of the right to legal remedy takes place before the court, the system is less than the systems where the settlement is dealt with under administrative proceedings.[33] The renunciation of the right to appeal to a judicial remedy needs to be evaluated carefully, taking into account the constitutional rules under the current judicial regime in the country, within the framework of the protection of the appeal.[34] It is believed that the regulation of the condition of giving up the decision within the settlement to the appeal as one of the basic building blocks will create efficiency in terms of using and directing the resources with the disappearance of the litigation phase in terms of violation decisions.[35] It is considered that the process at the court stage is an important step in terms of both resource and time regarding the finalization of the aforementioned violation decision, and a significant amount of resource savings can be achieved by eliminating this step.[36] In a contrary scenario, even if the waiver of the right to litigation is not required, the rate of actually filing a lawsuit will decrease with the settlement, and therefore, whether a limitation is required to abolish judicial review will become clear with the implementation of the settlement.

In the last paragraph of the Law, it is stipulated that the procedures and principles regarding settlement will be determined by the regulation to be issued by the Competition Authority. As can be seen, in the Law, as in the Draft, the compromise clause is a short and framework arrangement, and it is foreseen that its content will be shaped in practice.

[31] Ince and Unubol, "Settlement: Journey to Uncertainty," 55 (n. 23).
[32] Ince and Unubol, "Settlement: Journey to Uncertainty," 57 (n. 23).
[33] D. Slather, S. Thomas, and D. Waelbroeck, "Competition Law Proceedings Before the European Commission and the Right to a Fair Trial: No Need for Reform?" *College of Europe European Legal Studies*, Research Papers in Law 5 (2008): http://aei.pitt.edu/44310/1/researchpaper5_2008.pdf.
[34] OECD, "Competition Law and Policy in Turkey," 2005, 44. https://www.oecd.org/daf/competition/prosecutionandlawenforcement/34645128.pdf.
[35] Ibid.
[36] Ince and Unubol, "Settlement: Journey to Uncertainty," 57 (n. 23).

4. Evaluation of the Settlement Procedure in Terms of the Relation of Leniency and Penalty Regulation

As many competition authorities in the world, Turkey Competition Authority (TRC) is fighting against cartels and cartel to be regarded as the most serious violation of competition law. The Competition Authority tries to adopt different mechanisms to make its implementation more efficient.

The settlement procedure has not been clearly implemented in Competition Law. However, there are cases where the Competition Authority reduced fines on the grounds that cartel participants accepted their responsibilities and cooperated with the TCA.For example, the Competition Authority, Siemens Sanayi ve Ticaret A.Ş. (Siemens) and its 14 dealers to determine whether the cartelization will be realized in the tenders after the dealership system and whether the system in question has anti-competitive effects and consequences in the traffic signaling market. In the *Siemens*[37] decision, one of the parties was fined a minimum fine for helping to reveal the violation, while other participants were fined up to 6% of their turnover. The defense of the cooperating undertakings supports the investigation's findings. *Yonga Levha I*[38] and *Yonga Levha II*[39] cases have taken into account the cooperation with the Competition Board and the fine has been calculated accordingly. Collaborating firms were fined 0.5%, while other cartel undertakings received fines corresponding to 1% of their turnover. One of the mitigating factors in the *Ytong* case[40] was the firm's denial of the alleged cartel's existence. Collaborating parties were fined up to 2% of their turnover, while other parties received fines corresponding to 3% of their turnover.

The decision implementation of the Competition Authority regarding the rewarding of accepting the violation and cooperation has been criticized in the past. It has been claimed that the practices of the Competition Board are not as successful as in the USA or the EU, because the general fines are not high enough to guarantee the cooperation of the undertakings. In addition, it is emphasized that there should be clear rules regarding the awards brought by cooperation. The need for transparent, objective and consistent policies on leniency and settlement institutions for an effective fight against cartels is also expressed.[41] Similar criticisms were expressed in one of the OECD reports. Turkey made some evaluation results "Review Report" has been proposed in the following considerations: “To improve the implementation capacity of the Competition Authority and the Competition Act, the law must be changed.” In this regard, the adoption of the settlement mechanism and leniency programs becomes more important. The settlement mechanism makes it possible to terminate the process in a short time if the undertaking changes its behavior according to the Competition Board's suggestion. Therefore, it will ensure that investigations are resolved effectively.[42]Undertakings that provide some basic information about the cartel may receive a reduction in fines when they accept their

[37] No. 05-13/156-54 and dated 10.03.2005, p. 84, 98-103. See also Annual Report On Competition Policy Developments In Turkey (2006), DAF/COMP(2006)7/20.
[38] No. 02-53/685-278 and dated 06.09.2002.
[39] No. 03-12/135-63 and dated 25.02.2002.
[40] No. 06-37/477-129 and dated 30.05.2006, p. 86, 88.
[41] H. Arı, G. Kekevi, and E. Aygun, “The Evaluation of Turkish Competition Authority’s Fining Policy for Cartel Cases.” *Annual Symposium on Recent Developments in Competition Law* 4 (2008): 158.
[42] OECD “Competition Law and Policy in Turkey” (n. 34).

responsibilities. The Guideline Draft Regarding the Disclosure of the Regulation on Active Cooperation for the Purpose of Revealing Cartel, without seeking the significant amount of value of the violation by the Competition Authority, only evaluates whether the undertakings meet the conditions specified in the 6th and 9th articles of the Leniency Programs. In this sense, fine reductions are assumed to be automatic when information about cartels is provided, and that the penalty reductions are linked to the acceptance of liability for the breach. In this sense, it can be accepted that these provisions mean that compromise has a place in Turkish competition law. However, it has different features than those of the Commission. The main difference from the EU settlement procedure is that there is no provision on procedural savings. Although there is a fixed reduction in EU law for all parties, the Leniency Program has different levels of reduction depending on the nature and timing of the cooperation. Apart from this, since the Competition Law makes it possible to punish individuals, there are provisions regarding the imposition of fines on the directors and employees of undertakings.

The reason for the lack of provisions on procedural savings is explained by the fact that in Turkish Competition Law, compromise is not seen as a resource saving mechanism. It aims to reward the admission of liability for the violation and thus facilitate the identification of cartels. Providing clear rules for leniency program and settlement is considered important for a strong sanction. These provisions also aim to address the criticism brought by international reports. In other words, the Commission aims to obtain procedural savings and direct them to the detection of other violations that would increase deterrence. In this sense, according to the views in the doctrine, the general purpose of the two systems is to provide deterrence, but they differ in terms of the way they are implemented. Another difference between the two systems is that the cooperating undertakings do not accept the possible amount of fines in the Turkish "settlement" option.

It has been understood that 17 leniency applications have been received so far within the scope of the Competition Board's leniency program. Nine of these applications were made to obtain a discount for an investigation that had already started. In three of these applications, it is observed that the Competition Board applied reductions in the amount of penalties to cooperating undertakings. We believe that it is beneficial to analyze these decisions, since a reduction in the amount of penalty will be foreseen in return for accepting the responsibility of the violation as “settlements”. In two cases, cartel participants initially cooperated but resorted to the leniency program after the investigation decision. During the application, the Competition Authority is of the opinion that sufficient evidence has been provided that the 4th article of the Competition Law has been violated. However, the Competition Authority did not look at whether there was a significant amount of evidence submitted by the parties and whether it provided reductions in the amount of fines. Therefore, these three applications have similar features to the settlement procedure, as a penalty reduction is provided for the liability of the violation. Here are some cases that the Competition Board has been reduced fines:

- *21 Driving Courses Operating in Kahramanmaraş*[43]

The investigation was initiated as a result of the preliminary investigation carried out upon the application, which alleged that the said driving courses agreed and raised the prices.

[43] 20 August 2014, dated and numbered 14-29/610-264.

During the investigation phase, it was determined that the driving courses examined came together to determine the price and payment conditions, and that they envisaged inspection and punishment mechanisms to ensure price unity.

The Private Gençbilir Motor Vehicle Driving Course, one of the undertakings under investigation during the investigation phase, applied to benefit from the Regulation on Active Cooperation for the Purpose of Revealing Cartels (Leniency Program) on 08.01.2014 and 15.01.2014 and accepted the existence of the agreement.

As a result of the discussion of the file by the Competition Board on 20.08.2014; Administrative fines were imposed on the driving courses that were determined to violate Article 4 of the Law No. 4054 by agreeing to determine the fees for the driving license training.

While the administrative fines were assessed within the framework of the Agreement Restricting Competition, Concerted Actions and Decisions and the Regulation on Fines for Abuse of the Dominant Position (Penal Regulation), it was taken into consideration that no determination was made regarding the implementation of the agreement. In addition, the discount regulated in the Leniency Program was applied in terms of Private Gençbilir Motor Vehicle Driving Course. It is decided to be given 0.75% administrative penalty of 2.138.42 TL.

- *Investigation Against 45 Bakeries Operating in Aksaray*[44]

The investigation in question was initiated on 16.09.2013 as a result of the information and documents obtained from the preliminary investigation process, which was initiated ex officio following the application of denunciation that the bakeries operating in Aksaray. They had agreed to determine the price of bread and many news on the local internet news sites.

In addition, 45 undertakings on which an investigation were under investigation accepted the existence of the cartel by making an application on 21.11.2013 in order to benefit from the Regulation on Active Cooperation for the purpose of Revealing Cartels (Leniency Program).

On April 16, 2014, as a result of the meetings, an administrative fine was imposed for violating Article 4 of the Law No. 4054 by determining together the sale price of bread in 2013. In the determination of the administrative fines, taking into account the applications of the undertakings under the Leniency Program, the Agreements Restricting Competition, Concerted Actions and Decisions and the Regulation on Fines to be Imposed in the Case of Abuse of the Dominant Position (Penal Regulation) and the Penalty Regulation were applied.

Considering the general principles for the settlement procedure, an arrangement similar to the leniency program and penalties may be adopted. In these arrangements, possible procedural elements of the settlement procedure can be designed. In the regulation, the initiation of settlement meetings, confidentiality problems, withdrawal from settlement meetings or violation of the process can be explained by taking EU law. Waiver of appeal can have clear benefits in terms of reduced legal costs and the Competition Authority should use these benefits in resolving

[44] 6 April 2014, dated and numbered 14-15/287-120.

other cases.[45]It should also be remembered that transparency should be ensured for the settlement process as much as possible.

5. Concluding Remarks

The settlement procedure in competition law allows for the detection and analysis of violations of competition as quickly as possible and to provide a healthy competitive environment in the market as soon as possible. In this context, the continuation of the violation is prevented and the damage to be caused is prevented. On the other hand, the limited public resources of the competition authority are saved and these resources are redirected to other violations and resolved. Ending legal uncertainty in the settlement procedure, protecting commercial reputation, reduction in penalty amount and optimal use of resources, etc. undertakings that gain advantages also take advantage of the settlement process.

In the competition legislation in other legal systems, there are settlement procedures regulated in different ways. In most of these methods, undertakings accept their obligations arising from the breach, waive some procedural rights granted to them, obtain a reduction in fines as a result of their cooperation with the competition authority and ensure that the violation is terminated at an early stage. While the settlement implemented by the EU Commission and the plea bargain implemented by the USA are similar in shape, they differ from each other in terms of the way of implementation and penal dimensions.

The success of the settlement depends on the fact that undertakings decide which party's benefits outweigh the benefits after choosing to compromise with the judgment in the normal procedure. Like an effective leniency program, an effective cartel settlement requires a sufficient amount of benefits and incentives for both the Commission and undertakings joining the cartel.
When the competition authority invites the parties to negotiate the settlement, a time limit is set, stating whether the parties want to participate in the settlement with a written notice, "this written statement does not mean that the parties agree to participate in a violation or be responsible for it" and the settlement procedure is started. In this way, undertakings can participate in the settlement procedure in their innocent status. Therefore, the competition authority is obliged to ensure that the responsibility of each party is examined on the basis of its own infringement. In this context, an undertaking will not be limited by pressure from other undertakings forming a cartel and will therefore be free to make the best decision for itself.

[45]ICN, “Cartel Settlement.”, 2008, p.26. https://centrocedec.files.wordpress.com/2015/07/cartel-settlements-2008.pdf.

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