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# BETWEEN THE JUDGE AND THE LAW: JUDICIAL INDEPENDENCE AND AUTHORITY WITH CHINESE CHARACTERISTICS

LARRY CATÁ BACKER\*

## *Abstract*

*What is the scope and nature of judicial reform? To what extent does borrowing from Western models also suggest an embrace of the underlying ideologies that frame those models? It is a common place in the West, whether in Common Law or Civil Law states, that the integrity of the judiciary depends on their authority to interpret law and to apply that interpretation to individual cases and the litigants that appear before the courts. That presumption, however, embeds premises about the organization of political and administrative authority that may be incompatible with those of states developing Socialist Rule of Law structures within Party-State systems. In Common law states those deep presumptions touch on the disciplinary role of judicial opinions as a constraint on judicial interpretation. In civil law states that discipline arises from the constraining principles of the legal codes themselves. In both the legislatures serve as the ultimate check in a complex dialogue with courts in three respects. First, judges serve a political role in their relation to law. Second, cases themselves serve an important political role as well. Third, courts begin to serve as the place where societal narratives are forged and popular expression is constructed and applied. In Socialist rule of law systems, the disciplinary systems are quite different and ought to produce a different relationship between courts, law, and the cases they are bound to apply fairly and consistently under law. This paper considers the way that the logic and grounding principles of Chinese Marxist Leninism may provide guidance in the construction of a judicial enterprise that is both true to its organizational logic and which enhances the authority of judges to serve litigants fairly. It suggests the points of compatibility and incompatibility in the ideologies of these distinct systems of judging and what it may mean for judicial reform in China. That consideration, in turn is based on a fundamental difference, in Socialist Rule of Law systems, between the authority to interpret law and the authority to apply law to an individual case. For Chinese judicial reform it is in the perfectibility of the judge that lies the perfectibility of law that in turn ensures the perfectibility of the judge. Part II considers in very broad strokes the relationship*

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\* W. Richard and Mary Eshelman Faculty Scholar & Professor of Law & International Affairs, Pennsylvania State University 239 Lewis Katz Building, University Park, PA 16802. The ideas in this essay were first presented at the 11<sup>th</sup> Annual Conference of the European China Law Studies Association, Roma Tre University, Rome, Italy, September 22, 2016. My thanks to Flora Sapio and Chris Mittelstaedt for their engagement with these themes. My thanks to Gao Shan for his usual excellent assistance. An earlier Chinese language only version will be published in 17 BEIJING POL. & L. REV. 2017.

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*between the judge and law in the West. Part III then considers Chinese reforms touching on the relationship between the judge and the law, and the evolution of normative structures within which one can speak to judicial independence. Part IV then considers the project from the perspective of the grounding ideology of the Chinese state. From that fundamental distinction, the paper will propose a Socialist approach to the judicial function compatible with its own logic and legitimacy enhancing under global consensus principles for a well-organized and functioning judiciary.*

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## I. SITUATING THE TENSIONS OF CHINESE JUDICIAL REFORM.

Must judges have the independent authority to interpret the statutes and regulations they apply to disputes before them as a necessary element of the legitimate exercise of their authority? This essay argues that in China they do not. Judicial reform in China has emerged as one of the most important political, administrative and governance reform efforts of the last decade.<sup>1</sup> Judicial reform itself is deeply embedded within a larger discussion about the rule of law within the Chinese political and judicial systems.<sup>2</sup> Much of that reform has been technical, to make the institution of the judiciary better at producing results compatible with the larger political issues in China, from corruption to the training of judges and the management of dispute resolution.<sup>3</sup> Reform has been grounded in the attainment of pragmatic objectives.<sup>4</sup> But form follows ideology; always lurking is the specter of technical changes as the methodology of fundamental transformation of the political order.<sup>5</sup> Those tensions in the development of Chinese judicial reform were nicely summarized by Ben Liebman almost a decade ago at the beginning of the current waves of judicial reform.

Such reforms appear aimed at making the courts institutions for the fair adjudication of individual disputes. At the same time, commentators in China and in the West have argued for greater changes, contending that courts should serve not only as adjudicators of private disputes but also as checks on state power and as fora for the resolution of public rights—in sum, that the courts should play a significant role in the development of Chinese governance and society.<sup>6</sup>

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<sup>1</sup> See generally, Taisu Zhang, *The Pragmatic Court: Reinterpreting the Supreme People's Court of China*, 25 COLUM. J. ASIAN L. 1 (2012); Benjamin L. Liebman, *China's Courts: Restricted Reform*, 21 COLUM. J. ASIAN L. 1 (2007).

<sup>2</sup> RANDALL PEERENBOOM, *CHINA'S LONG MARCH TOWARD RULE OF LAW* (Cambridge Univ. Press 2002); Teemu Ruskola, *Law Without Law, or Is "Chinese Law" an Oxymoron?*, 11 WM. & MARY BILL RTS. J. 655 (2003).

<sup>3</sup> Susan Finder provides a good brief summary of the thrust of reform, focusing on jurisdiction (to reduce local protectionism), hearing centered process, changes to internal allocation of roles in proceedings, openness, transparency and accessibility of judicial proceedings, professionalization of court personnel, and insuring judicial independence while preserving the leadership role of the CCP. Susan Finder, *China's Master Plan for Remaking Its Courts*, THE DIPLOMAT (March 26, 2015), <http://thediplomat.com/2015/03/chinas-master-plan-for-remaking-its-courts/>. Most of these address longstanding criticisms. See, Jerome A. Cohen, *China's Legal Reform at the Crossroads*, COUNCIL ON FOREIGN RELATIONS (March 2006), <http://www.cfr.org/china/chinas-legal-reform-crossroads/p10063>. See also, Polly Botsford, *China's Judicial Reforms are No Revolution*, INTERNATIONAL BAR ASSOCIATION (Aug. 10, 2016) <http://www.ibanet.org/Article/NewDetail.aspx?ArticleUid=846c87e8-a4aa-4a88-a7fc-e6fc136c2fca> (“The changes improve governance, but do not challenge the foundation of the existing system, which is that the courts, the judiciary, must ultimately answer to the CPC.”).

<sup>4</sup> Zhang, *supra* note 1 (describing the emulation of stare decisis through the mechanisms of the introduced concept of guiding cases).

<sup>5</sup> E.g., Note, *Chinese Common Law? Guiding Cases and Judicial Reform*, 129 HARV. L. REV. 2213 (2016).

<sup>6</sup> Liebman, *supra* note 1; see generally Chris X. Lin, *A Quiet Revolution: An Overview of China's Judicial Reform*, 4(2) ASIAN-PACIFIC L. & POLY. J. 255 (2003); Vernon Mei-Ying Hung, *China's WTO Commitment on Independent Judicial Review: Impact on Legal and Political Reform*, 52(1) AM. J. COMP. L. 77 (2004).

The judgment has been made much more explicitly by other influential Western commentators: “today’s PRC legal system is basically a perversion of the European civil law system easily recognized by continental legal specialists. . . . “Judicial independence,” as it is commonly understood outside China today, is the enemy and forbidden by Party rulers even to be discussed in law schools.”<sup>7</sup>

The problem, then, revolves around the ideological baggage of technical improvements modeled on or borrowed from political systems whose organization of state power are quite distinct from that of China. It is, as well the tensions inherent in the assessment of such changes, especially assessment from foreign peers—whose standards of assessment are themselves grounded in and meant to further, the ideological foundation from which they operate. In other words, it is impossible to separate the techniques of judging and judicial administration from the principles and politics that gave the system its form. To embrace one requires embrace of the other.

At the root of the problem are the premises on which judicial systems are founded and assessed. That is, the problem of judicial legitimacy and authority, the way such authority is perceived and maintained within a political system in which it is embedded haunts not merely the efforts at judicial reform in China, but the way in which foreigners approach the evaluation of those reforms as legitimate (and thus the exercise of judicial power as legitimate). These basic premises are so deeply embedded in Western political cultures that they appear natural. For example, it is a common place in the West, whether in Common Law or Civil Law states, that the integrity of the judiciary depends on their authority to interpret law and to apply that interpretation to individual cases and the litigants that appear before the courts. That authority to interpret and apply law to the disputes before them is to be exercised autonomously of other political actors and with a strict fidelity to the fundamental legal principles of the system.

That presumption, however, embeds premises about the organization of political and administrative authority. In Common law states those deep presumptions touch on the disciplinary role of judicial opinions as a constraint on judicial interpretation. In civil law states that discipline arises from the constraining principles of the legal codes themselves. In both systems, the legislatures serve as the ultimate check in a complex dialogue with courts. And all actors, that is all institutional political actors—administration, legislature and judiciary—and the people who serve them, are constrained by the principles set forth in the document that memorializes the constitution of state and government and the delegation of sovereign power thereto by the people. Both systems provide for judicial authority to interpret and apply this “higher law” to both ensure against abuse of judicial and legislative authority. The authority of the judge, and the cultural expectation on which legitimacy and authority are based, are themselves meant to underline and strengthen the underlying ideological basis of the system of which the form an important part. That, in turn, is possible only because of the underlying ideal of the judge within a government in which all political and administrative power is vested, and then divided.<sup>8</sup> As a

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<sup>7</sup> Maurits Elen, *Interview: Jerome Cohen*, THE DIPLOMAT (Sept. 1, 2016), <http://thediplomat.com/2016/09/interview-jerome-cohen/>.

<sup>8</sup> Discussed in Larry Catá Backer, *Reifying Law—Government, Law and the Rule of Law in Governance System*, 26 PENN ST. INT’L L. REV. 521 (2008).

consequence, it comes as no surprise that Western academic and political criticism reflects these views. The criticism tends to fall into two categories. The first is the technical and administrative: focusing on how to make the courts more efficient and independent and very much in line with the thrust of Chinese reform efforts. The second is institutional and political. These touch on the role of the CCP and the authority of courts to constrain the power of the state. And ultimately, they tend to function as a particular application of the not uncommon Western academic literature about the illegitimacy of the Chinese political order.<sup>9</sup>

But the issues have become more complicated in globalization, as the vertical organization of power within states is also fractured by horizontal alignments of judges across states. Judges talk to each other.<sup>10</sup> They begin to feel they have more in common with each other—theirs is a singular community—than perhaps with the other branches of the government in which their functions are embedded.<sup>11</sup> Convergence of practices may also produce convergence of sensibilities—of the nature, role and character of the courts whose practices are tending toward a common set of principles.<sup>12</sup> Judges may find it important to cultivate legitimacy among their own class, and to conform to global class expectations. This may affect the way they approach reform within their own political orders. As important, perhaps, the expectations of global classes of important consumers of judicial resources—repeat player litigants,<sup>13</sup> business and the state, will also likely help shape the underlying

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<sup>9</sup> See Lance L.P. Gore, *The Political Limits to Judicial Reform in China*, 2 CHINESE J. OF COMP. L. 213 (2014), discussed generally in Larry Catá Backer, *The Rule of Law, The Chinese Communist Party, and Ideological Campaigns: Sange Daibiao (the “Three Represents”), Socialist Rule of Law, and Modern Chinese Constitutionalism*, 16 TRANSNAT’L L. & CONTEMP. PROBS. 29 (2006).

<sup>10</sup> Press Release, *Chinese Judges Meet with ALI*, AM. L. INST., (Jan. 11, 2016), <https://www.ali.org/news/articles/chinese-judges-meet-ali/> (“A distinguished group from the Supreme Court of China, visiting the U.S., sought information about ALI and its law reform procedures.”); Press Release, *First-Ever “U.S.-China Judicial Dialogue” Supports an Exchange of Views on Judicial Reform*, U.S. DEPT. OF JUSTICE, (Aug. 19, 2016), <https://www.justice.gov/opa/blog/first-ever-us-china-judicial-dialogue-supports-exchange-views-judicial-reform> (“Our three talented and experienced U.S. judges discussed with senior Chinese judges and other experts topics relevant to commercial cases, ranging from case management to evidence, expert witnesses, amicus briefs, the use of precedents and China’s system of “guiding cases.”).

<sup>11</sup> ANNE-MARIE SLAUGHTER, *A NEW WORLD ORDER* (Princeton University Press 2004); Cf. Jinting Deng, *The Guiding Case System in Mainland China*, 10 FRONTIERS L. CHINA 1 (2015) (convergence of Chinese practices and common law system).

<sup>12</sup> Jocelyn E.H. Limmer, *China’s New “Common Law”: Using China’s Guiding Cases to Understand How to Do Business in the People’s Republic of China*, 21 WILLAMETTE J. INT’L L. & DISP. RESOL. 96 (2013).

<sup>13</sup> The reference here is especially to the large multinational corporations, international banks, large financial entities, global state-owned enterprises that tend to engage in a larger volume of litigation around the same general issues. The importance of repeat players in litigation has been the object of useful study. For the germinal study, see Marc Galanter, *Why the ‘Haves’ Come out Ahead: Speculations on the Limits of Legal Change*, 9 LAW & SOC. REV. 95 (1974); Marc Galanter, *Afterword: Explaining Litigation*, 9 LAW & SOC. REV. 347 (1975). For its application within and beyond the United States. See generally, Flemming, Roy B. & Glen S. Krutz, *Repeat Litigators and Agenda Setting on the Supreme Court of Canada*, 35 CANADIAN J. OF POL. SCI. 811 (2002); McGuire, Kevin, *Repeat Players in the Supreme Court: The Role of Experienced Lawyers in Litigation Success*, 57 J. OF POL. 187 (1995); Stacia L. Haynie Kaitlyn L. Sill, *Experienced Advocates and Litigation Outcomes: Repeat Players in the South African Supreme Court of Appeal*, 60 POL. RES. Q. 443 (2007).

normative base line within which judicial reform is understood and assessed.<sup>14</sup> As a consequence, it comes as no surprise that Chinese reformers begin to reflect global perspective, even when seeking to embed them within the political culture of China.<sup>15</sup> And these convergences make it difficult to contextualize even basic concepts like judicial independence.<sup>16</sup>

The direction judicial reform will take in China cannot be predicted; yet, its contours are increasingly transparent, even as it is buffeted between internal and external normative expectations. In March, 2016, the Chinese State Council released a White Paper on Judicial Reform prepared by the Supreme People's Court.<sup>17</sup> In the forward to its report, the Supreme Judicial Court announced the structures around which its analysis would emerge:

The rule of law is the basic way of governing a country and the judiciary is the significant cornerstone of the rule of law system. Judicial courts apply laws to adjudicate cases in accordance with their statutory powers and procedures and play such roles as settling disputes, protecting rights and constraining public powers, so as to ensure the effective implementation of laws and maintain social fairness and justice.<sup>18</sup>

The White Paper comes on the heels of a series of reforms accelerating since 2013 that have focused on judicial reform without directly challenging the political premises on which the underlying system is grounded.<sup>19</sup> But the reluctance to

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<sup>14</sup> Cf. Marc Galanter, *Why the "Haves" Come Out Ahead: Speculation on the Limits of Legal Change*, 9 L. & SOC'Y REV. 95 (1974); Kevin T. McGuire, "Repeat Players in the Supreme Court: The Role of Experienced Lawyers in Litigation Success," 57 J. POL. 187 (1995).

<sup>15</sup> See, e.g., Stanley Lubman, *China's Highest Court Eyes Judicial Reform, While a Lawyer Criticizes TV Confession*, WALL ST. J. (Mar. 11, 2016), <http://blogs.wsj.com/chinarealtime/2016/03/11/chinas-highest-court-eyes-judicial-reform-while-a-lawyer-criticizes-tv-confessions/>.

<sup>16</sup> Cf. Jerome Alan Cohen, *The Chinese Communist Party and "Judicial Independence": 1949-1959*, 82 HARV. L. REV. 967 (1969); XIN HE, JUDICIAL INDEPENDENCE IN CHINA 180 (Randall Peerenboom ed., 2010).

<sup>17</sup> *White Paper: Judicial Reform of Chinese Courts*, SUPREME PEOPLE'S COURT OF THE PEOPLE'S REPUBLIC OF CHINA (March 3, 2016), [http://english.court.gov.cn/2016-03/03/content\\_23724636.html](http://english.court.gov.cn/2016-03/03/content_23724636.html); for a summary, see *What China's judicial reform white paper says about its vision for its judiciary*, SUPREME PEOPLE'S COURT MONITOR (Apr. 12, 2016), available <https://supremepeoplescourtmonitor.com/2016/04/12/what-chinas-judicial-reform-white-paper-says-about-its-vision-for-its-judiciary/>.

<sup>18</sup> *Id.*

<sup>19</sup> See John A. Ferejohn & Barry R. Weingast, *A Positive Theory of Statutory Interpretation*, 12 INT'L REV. OF L. & ECON. 263 (1992) ("Fundamentally, this implies that judicial interpretations – especially those that stand unchallenged—must be seen as reflecting the strategic setting in which they are announced, no matter how they are motivated or justified."). I have noted as well that the judicial role in that political context makes inevitable that judicial interpretation will be severely disciplined where pronouncements tend to wander too far from the customs, traditions and expectations of the polity for which it is made. See Larry Catá Backer, *Chroniclers in the Field of Cultural Production: Interpretive Conversations Between Courts and Culture*, 20 B.C. THIRD WORLD L.J. 291, 340 (2000) ("Authority is measured by compliance.").

challenge the underlying political system as a formal matter does not mean that the *effect* of reforms is not potentially transformative by the nature of its character.

That structure reveals both the context and contradictions within which judicial reform proceeds in China.<sup>20</sup> Those presumptions may be incompatible with those of states developing Socialist Rule of Law structures within Party-State systems. In Socialist rule of law systems, the disciplinary systems are quite different and ought to produce a difference. Such systems are grounded in the political leadership of a vanguard party whose obligation to lead the state and people to a specified objective fundamentally orders the structures and operation of the state.<sup>21</sup> In China that has produced a system in which all political power is vested in the vanguard party and all administrative authority is exercised through the state and its organs. That division between political and administrative authority marks every level and every institutional structure of the state.<sup>22</sup>

Chinese judges are both looking to the West for innovation in the operation of their court system, and simultaneously seeking to induce change that is consistent with the fundamental Chinese political line.<sup>23</sup> Yet what is emerging is neither compatibility with Western notions of efficient operation nor a sense that technical reforms are compatible with the fundamental political ideology of the state and its working style<sup>24</sup>—and ultimately a challenge to the leadership role of the Chinese Communist Party itself. It reflects a dialectical model of inter-systemic engagement that tends to mark Chinese approaches to the foreign.<sup>25</sup>

One of the areas of critical importance in the enterprise of judicial reform is centered on the *relationship between the judge and law*. In more conventional terms, it focuses on the issue of the extent and practice of judicial interpretation of law, and with it the independence of the judge from the political and administrative organs of state in rendering a decision in an individual case. The two are interrelated—to resolve a case, a judge must first determine the meaning of law and then apply that meaning and the standards of liability that may be inferred from it, to the facts

<sup>20</sup> HE, *supra* note 16 (antagonisms between courts and CCP).

<sup>21</sup> See HU ANGANG, *CHINA'S COLLECTIVE PRESIDENCY* (Springer, 2014).

<sup>22</sup> Discussed in Larry Catá Backer, *Party, People, Government and State: On Constitutional Values and Legitimacy of the Chinese State-Party Rule of Law System*, 30 B.U. INT'L L.J. 331 (2012),

<sup>23</sup> See Rebecca Liao, *Judicial Reform in China: How Progress serves the Party*, FOREIGN AFFAIRS, SNAPSHOT (Feb. 2, 2017), available at <https://www.foreignaffairs.com/articles/china/2017-02-02/judicial-reform-china> (“On January 14 [2017], Zhou Qiang, the chief justice of China’s Supreme People’s Court, rejected judicial independence in a speech to jurists in Beijing. China ‘should not fall into the trap of the West’s erroneous thinking and the independence of the judiciary,’ Zhou said.”); see generally, e.g., Qianfan Zhang, *The People’s Court in Transition: The Prospects of the Chinese Judicial Reform*, 12 J. CONTEMP. CHINA 69 (2003). This is an old story. See, e.g., Yu Chuan Chang, *The Chinese Judiciary*, 2 CHINESE SOC. & POL. SCI. REV. 68 (1917); Chang Yao-tse, *The Present Conditions of the Chinese Judiciary and Its Future*, 10 CHINESE SOC. & POL. SCI. REV. 163 (1926).

<sup>24</sup> San ba zuo feng. 三八作風; see Gucheng Li, *A Glossary of Political Terms of the People’s Republic of China* (Compiled by Kwok-Sing Li, Mary Lok, trans., The Chinese University of Hong Kong, 1995) p. 349. See *infra* Section III.

<sup>25</sup> See, e.g., Ji Weidong, *The Judicial Reform in China: The Status Quo and Future Directions*, 20 IND. J. GLOBAL LEGAL STUD. 185 (2013). This is well described in the context of international law in Björn Ahl, *Chinese Law and International Treaties*, 39 HONG KONG L. J. 735, 737 (2009) (dialectical model of international law grounded in distinct systems infiltrating and supplementing each other).

developed in the trial of the dispute among the litigants appearing before her. Within Chinese judicial reform initiatives, the Guiding Cases system<sup>26</sup> and the proposed rules on judicial independence are among the most important. The former seeks to harvest from Chinese rulings and judgments. “People’s courts at all levels should refer to the Guiding Cases release by the Supreme People’s Court when adjudicating similar questions.”<sup>27</sup>

This essay considers the way that the logic and grounding principles of Chinese Marxist Leninism may provide guidance in the construction of a judicial enterprise that is both true to its organizational logic and which enhances the authority of judges to serve litigants fairly. Part II considers in very broad strokes the relationship between the judge and law in the West. Within that constructed relationship the nature of judicial independence and the relationship between the judge and the state can be sketched—along with the ideology from which it emerges. Part III then considers Chinese reforms touching on the relationship between the judge and the law, and the evolution of normative structures within which one can speak to judicial independence. Part IV then considers the project from the perspective of the grounding ideology of the Chinese state, including its refinement after the conclusion of the 19<sup>th</sup> Chinese Communist Party Congress of October 2017. That consideration, in turn is based on a fundamental distinction, in Socialist Rule of Law systems, between the authority to interpret law and the authority to apply law to an individual case. From that fundamental distinction, the essay will propose a Socialist approach to the judicial function compatible with its own logic and legitimacy enhancing under global consensus principles for a well-organized and functioning judiciary. It is in the understanding of those distinctions that it is possible both the read the utility of Western models of judging in China, and to develop a means of realistically assessing the effectiveness of Chinese judicial reform within the constraints of its own ideological bases.

## II. THE RELATIONSHIP BETWEEN THE JUDGE AND THE LAW IN THE WEST

To understand the relationship between the judge and the law in the West, one must be sensitive to framing structures that have permeated Western thought at least since Aristotle<sup>28</sup>—the first is the relationship between law and the state as a general

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<sup>26</sup> See *Zuigao Renmin Fayuan Guanyu Anli Zhidao Gongzuo de Guiding* (最高人民法院关于案例指导工作的规定) [Provisions of the Supreme People’s Court Concerning Work on Case Guidance] (discussed and passed by the Adjudication Committee of the Supreme People’s Court, Nov. 15, 2010, issued Nov. 26, 2010), <https://cgc.law.stanford.edu/wp-content/uploads/sites/2/2015/08/guiding-cases-rules-20101126-english.pdf>; 《最高人民法院关于案例指导工作的规定》实施细则》(Detailed Implementing Rules on the “Provisions of the Supreme People’s Court Concerning Work on Case Guidance”), passed by the Adjudication Committee of the Supreme People’s Court on Apr. 27, 2015, issued on and effective as of May 13, 2015, China Guiding Cases Project, English Guiding Cases Rules, June 12, 2015 Edition, <http://cgc.law.stanford.edu/guiding-cases-rules/20150513-english/>.

<sup>27</sup> Provisions of the Supreme People’s Court Concerning Work on Case Guidance, *supra* note 26; see generally *Chinese Common Law? Guiding Cases and Judicial Reform*, 129 HARV. L. REV. 2213 (2016).

<sup>28</sup> See WILLIAM ELLIS, *ARISTOTLE’S POLITICS: A TREATISE ON GOVERNMENT* (Trans., E. P. Dutton & Co., 1912).

matter (between *gubernaculum* and *jurisditio*); the second is the relationship between interpreting and applying the law in a specific matter (between *jurisditio* and *jus dicere*).<sup>29</sup> Together these framing concepts provide the foundation within which it is possible to think about law, rule of law, legitimacy and authority of law and the institutions that are established to apply, produce and safeguard them. There are two caveats worth mentioning. The first is that, as we will see below, this is not to suggest that these framing concepts are either straightforward or uncontested. Indeed the opposite is true, but the many variations, some incompatible, all revolve around the framing concepts: law and the state; law-state and the judge. Thus, what is important to remember is that the way one approaches thinking about the issues of law, rule of law, and the judge, tend to be framed by these basic orienting conceptions that then constrain the way in which one can understand a problem, evaluate its fidelity to “higher values” and the inferences one can draw from its functioning and “effects” (that is how it appears in the world). The second is that the West is by no means the only civilization that has gone to the trouble of constructing highly sophisticated world views around which it can then understand and manage the world around them. But its views on law, the state, and the judge tend to be highly influential at this stage in global development.

#### A. THE STATE AND LAW.

In medieval times in the West, the relationship between law, judge and the administrative apparatus of the state was fluid and quite fluid and dispersed.<sup>30</sup> Yet, medieval development grounded in these differences between *gubernaculum* and *jurisditio*, that is between government and law, played a substantial role in the way in which the ideals of law and of the state have developed.<sup>31</sup> *Gubernaculum*, of course has had a long and quite self-transforming history. For my purposes here, it signifies the principles of government as a self-constituted institution. Its purpose has been administrative from the first. Though the character of that administration has undergone substantial variation as the West’s taste for distinct forms of executive and administrative authority has changed—from republic to monarchy, to aristocracy, to Empire, and even a little, towards theocracy. All of these forms remain true to the principles of *gubernaculum*—the notion of a separate institution (or person) in whom legitimately rested or from whom could there could be legitimately exercised, the prerogatives of government. With respect to these, law had little to say; “Gubernaculum was effected by what we might call 'administrative', not 'legal', orders.”<sup>32</sup> Initially these were simple and direct; this meant of the affairs of those holding control of a territory, with respect to their affairs—which were both personal and eventually matters of state. They included the power to exercise authority, to keep the peace, and to order the territory over which those holding the authority of

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<sup>29</sup> See L.G. Baxter, “The State” and Other Basic Terms in Public Law, 212 THE S. AFR. L. J. 213 (1982).

<sup>30</sup> PAOLO GROSSI, MITOLOGIAS JURÍDICAS DA MODERNIDADE 23-54 (Boiteux 2004).

<sup>31</sup> CHARLES HOWARD MCLWAIN, CONSTITUTIONALISM ANCIENT AND MODERN 79-94 (Cornell Univ. Press 1940).

<sup>32</sup> Baxter, *supra* note 29, at 215.

gubernaculum held control. It said nothing about the legitimacy of their control of territory, or of the character of the exercise of their power. Nor did it speak to constraint. The powers of the prerogatives of gubernaculum were, within their scope, uncontrolled. But the scope of those powers could be delimited. They were to be exercised only within the space left to within their jurisdiction. It is here that one notes the first iteration of the notion of government, and of its unrestricted exercise in the service of the prerogatives of those who hold that authority. It continues in vestigial form in those aspects of power used to protect the state—principally the power to engage in actions with and against foreigners.

Gubernaculum, of course, has evolved substantially since its emergence in the pre-modern era in Europe. It has escaped its personal and private boundaries—that is its ties to the person of the monarch or “lord” or “official” and has assumed a defining character of the institution of state through which the business of the state is conducted. Much of that is administrative in character. Though that administrative character itself has undergone radical transformation since the 17<sup>th</sup> century. Today, our gubernaculum references not just the administrative and executive power of the state but also its intertwining with the legal structures on which it is built and through which it is operated. But for our purposes the original conceptual marker remains strong—the notion that there need not be an identity between law and the administrative apparatus of the state. Thus, it is important to underscore the original distinction between the state (as a territory of a self-consciously distinct community) and the governing of it. Gubernaculum referenced the government as an autonomous element of a cluster of such elements that together ordered the political community and contributed to its constitution.

Though the original power of gubernaculum was uncontrolled, it did never occupy the entire field of power in social space. Indeed, gubernaculum could not be understood in the absence of the concept of *jurisditio*, in its own way a more complex term referencing both law and the instrumentalities for its expression and application.<sup>33</sup> But *jurisditio* itself was complicated by the structures of religion and religious government that was firmly entrenched in Western thinking by the 14<sup>th</sup> century when many of these concepts began to gel. *Jurisditio* meant law itself—those norms and rules of behavior that existed quite independent and apart from the prerogatives of those who controlled the territory where they were applied. But law itself—as an autonomous object—was itself fractured. Thus, law could be understood as both imposed from above (though religion) and imposed from below (though customs and traditions—as they might evolve—representing popular practice).

On the one hand, law was in origin completely outside the control of people. It was the word of God or some like constituted paramount force whose directions were handed down in the form of religious practice and the moral-societal rules that came as a consequence. These were eternal and specific. They provided a source of law that no one—including those exercising gubernaculum, could disregard, without

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<sup>33</sup> See GIANLUIGI PALOMBELLA, THE MEASURE OF LAW: THE NON-INSTRUMENTAL LEGAL SIDE FROM THE STATE TO THE GLOBAL SETTING (AND FROM HANDEN TO AL JEDDA), IN THE LEGAL DOCTRINES OF THE RULE OF LAW AND THE LEGAL STATE 138-40 (James R. Silkenat, James E. Hickey Jr., Peter D. Barenboim, eds., Springer, 2014).

themselves becoming illegitimate (and thus subject to removal as out-law).<sup>34</sup> This “higher law” also acquired an administrative structure that existed quite apart from gubernaculum (and eventually from the state) in the form of the religious officials charged with its development and application. These notions remain strong within Islam. They retain only a vestigial (but important) vitality in the West, supplying the moral foundation of much of what is now the basic law and legal principles of Western governments. But more generally, and especially in the United States, they serve as a source of “natural” or “moral” law tied to the structures and legal systems of religion that produces a strong effect on the law of the American polity. In any case it is important to understand this as an autonomous source of law that stands apart and above the state and its gubernaculum.

On the other hand, *jurisditio* has long been understood as the customs and traditions of the people. That is, law has been understood as the societal rules through which people order their relations within a specific territory. They refer to those rules which form the common practices and understanding of “right” and of the measure necessary to, as the Institutes remind us as the core of justice, is meant to “give very man his due.” But custom and tradition cannot be understood in their primitive sense, as the Europeans were fond of doing as they became more “developed” and “scientific” in their approach to the structures and content of law<sup>35</sup>. In common law jurisdictions these formed the elements of practice that, in the hands of administrators eventually socialized into a functional-societal class—the judge—became the basis for and the touchstone against which the law for settling private disputes emerged.<sup>36</sup> For our purposes here, the important point—whatever its current form as common law, or customs, the fundamental premise was that law arose outside the structures and control of the state or of the administrator of territory. And, indeed, as Aristotle would long have it, the administrator, the magistrate, was advised to interfere with these laws at her peril.

Yet that the relationship between law and the government was autonomous, in its fundamental ordering, did not mean that they were forever separate. It has long been the case that *jurisditio* can arise through an assembly of people as it can from the autonomous evolution of custom or religion. From pre-modern times it has been clear that a representative collection of people can manage or adjust the law. And

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<sup>34</sup>The political consequences of excommunication in the West were not unknown and widely used as a political tool by Catholic Popes seeking to manage their authority through law. See, e.g., ELISABETH VODOLA, *EXCOMMUNICATION IN THE MIDDLE AGES*, (Univ. of Cal. Press, 1986). They are still used today. Consider this, “Pope Francis Excommunicates Donald Trump from Catholic Church Citing Un-Christian Behavior,” The National Report available at <http://nationalreport.net/pope-francis-excommunicates-donald-trump-catholic-church-citing-un-christian-behavior/>. The notion persists in modern times through the devices of “legitimacy” grounded in international normative principle and the consequences of illegitimacy remains as harsh—that is a lesson learned, for example by the regimes in Libya and other places in the first part of this century, so-called “soft coups.” See, e.g., Hector Perla Jr, *Here’s Why Some People Think Brazil is in The Middle of a ‘Soft Coup’*, THE WASHINGTON POST, (Apr. 16, 2016), <https://www.washingtonpost.com/news/monkey-cage/wp/2016/04/16/heres-why-some-people-think-brazil-is-in-the-middle-of-a-soft-coup/>.

<sup>35</sup> See JAN M. BROCKKMAN & LARRY CATÁ BACKER, *LAWYERS MAKING MEANING: THE SEMIOTICS OF LAW IN LEGAL EDUCATION II* (Dordrecht: Springer, 2013) at ch. 8-9 (on the “science of law”).

<sup>36</sup> See ARTHUR R. HOGUE, *ORIGINS OF THE COMMON LAW* (LibertyPress, 1966) (on the common law).

later that collection of people could eventually exercise the prerogatives of gubernaculum as well as government fused together the powers of administration, of law making, and of adjudication within its apparatus. By the 18<sup>th</sup> century, the notion had become well settled that the people could, though government, exercise an authority to make law—instrumentally—to the same extent and with the same authority as the prior constitution of tradition. That is, that law could cease to be autonomous of the state apparatus—at least to the extent that this apparatus was legitimately vested with the authority of the people themselves. Law, then, could serve as an instrument of popular will within government as it had been understood to represent that will autonomously of its government in earlier periods. These principles became universally embraced in the centuries after the American Revolution. Indeed, in civil law systems, the idea that law can exist autonomously from the state was both reduced and transformed by the embedding of the source of custom and tradition—the people—within the apparatus of the state itself and by the embrace of the notion of sovereign authority delegated to this representative assembly (a set of principles long in the making in the West). As a consequence, in most civil law jurisdictions the law and the state appear conjoined and inseparable. Law cannot exist independent of the acts of the people now embedded in the state. And law must be understood as a positive act designed to achieve some objective and in that effort invoking the administrative and police powers of the state.

But this did not mean that *jurisditio* notions were now subsumed within the state apparatus. On the contrary, the absorption of law making power neither negated the existence of a superior “natural law” in some jurisdictions, nor did it overcome entirely the role and importance of customary law as developed within a common law framework (in the state). More importantly, the rise of constitutional law began to serve the same limiting power against the prerogatives of the people represented in the apparatus of government as notions of *jurisditio* had done in earlier centuries. Constitutionalism, especially since the middle of the last century, now increasingly assumes a place beyond the control of the state.<sup>37</sup> And it is in this complex of relations between law, the state, and the people that modern Western rule of law notions emerge. They tend to serve as the transformed expression of the ancient notion of legal autonomy while recognizing the critical importance of the embedding of law within the architecture of government. It carves out a space for extra-governmental rules while acknowledging the centrality of government to the administration of law and justice. Rule of law is meant to provide those constraints on the exercise of power in the making of law that preserves its connection to the polity (process legitimacy) and that limits its reach (though the notions of substantive rule of law limits on the power of the state to legislate or to use its executive or administrative powers). But this entire complex of notions, on which mountains of analysis have been produced, are grounded in a set of simple principles that recognize the autonomy of the state and of law, even as the one can be made or unmade by the other. While the state may interfere with law as it likes (to the extent it is not constrained by “higher law”) it may not interfere with its autonomy once made (and made legitimately). That is the notion here is of the independence of law

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<sup>37</sup> See generally, Larry Catá Backer, *From Constitution to Constitutionalism: A Global Framework for Legitimate Public Power Systems*, 113 PA. ST. L. REV. 671 (2009).

from the state once it has been made. It is that notion of autonomy that then carries over to mark the relationship between law and its administration.

## B. THE JUDGE AND LAW

The autonomy of law and the state helps clarify the role of the judge in the West before the state and before the law. The judge stands before the law the way that the state stands before the law. Both are bound by the word of law, but are heavily embedded in its development, interpretation and application.<sup>38</sup> And the judicial space serves both as the site for the resolution of disputes and for the political contestations that have moved from society and the Church, into law. The interpretative function of the judge before the words that constitute law, then, serves to reinforce the embedded autonomy of the law.<sup>39</sup> The issue has been contentious as the 20<sup>th</sup> century saw legal intellectuals in the West divert their attention from the personality of law to the personality of the judge—to objectify the legal system within the body (and psychology) of the judge.<sup>40</sup> That obsession, too, travels with the transposition of Western law systems elsewhere, but does not displace the grounding reality of law as autonomous of the individuality that has sought to be imposed on it by the sometimes inward-looking and parochial predilections of a culture in transition (especially in the United States).<sup>41</sup> Let us briefly consider how this applies to common law and civil law jurisdictions.

In common law jurisdictions, the judge serves as the centering element of two complexes of law—judicially administered and statutory/regulatory rules. The first centers the judge in the determination of law—that is, it centers the judiciary within the nexus of cases produced by the judicial body the judge produces an interpretation of the law to be applied to the dispute to be resolved. The second centers the text of a legislative or administrative pronouncement in the determination of law—that is it reduces the function of the judiciary in common law to a methodology that is applied to the extraction of meaning from and around text from the nexus of cases that themselves have sought to produce not just clarity but meaning through application in factual context. The first necessarily places the judge at the center of law, the second does not. Let us further consider each in turn.<sup>42</sup>

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<sup>38</sup> The issues continue to attract attention for its paradoxes and challenges as old systems are transformed by modern realities. See Jonathan T. Molot, *Reexamining Marbury in the Administrative State: A Structural and Institutional Defense of Judicial Power Over Statutory Interpretation*, 96 NW. U.L. REV. 1239 (2002).

<sup>39</sup> The obsessive focus of the Western intellectual on what are usually reduced to issues of interpretation (a central element of the lawyer's "job") and hierarchy. See, e.g., Daniel A. Farber, *Statutory Interpretation and Legislative Supremacy*, 78 GEO. L. J. 281 (1989); Richard A. Posner, *Statutory Interpretation - In the Classroom and in the Courtroom*, 50 U. CHI. L. REV. 800 (1983).

<sup>40</sup> See generally, Ronald Dworkin, *Law as Interpretation*, 60 TEX. L. REV. 527 (1982); Stanley Fish, *Working on the Chain Gang: Interpretation as Law and Literature*, 60 TEX. L. REV. 551 (1982).

<sup>41</sup> See generally, Mark Tushnet, *New Forms of Judicial Review and the Persistence of Rights- and Democracy-Based Worries*, 38 WAKE FOREST L. REV. 813 (2003).

<sup>42</sup> See generally Larry Catá Backer, *Retaining Judicial Authority: A Preliminary Inquiry on the Dominion of Judges*, 12 WM. & MARY BILL OF RIGHTS J. 117 (2003); Backer, *supra* note 19.

The first are those law sub-systems that are entirely judge administered (tort, contract and the like). These are not memorialized—their scope and application are expressed in the sum of judicial applications of those rules over time. They represent the modern expression of custom and tradition that has been reshaped into a coherent and self-referencing system of rules and standards that are meant to guide behavior and allocate responsibility for loss. In that role, the judge does not create law so much as she develops and expresses it within the constraints of prior opinions of other judges and the sense of community expectations (which are themselves shaped by communal understanding of the aggregate of decisions). The law is extracted from its application over many cases. Here the judge plays a significant role in the recognition of law (usually and wrongly expressed as making law—though that argument is itself an expression of a political agenda aimed at destroying the role of the judge and of the autonomy of law as understood classically in the West).<sup>43</sup> The critical principle here is the link between the autonomy of law (from the state) and the necessary and equivalent autonomy of the judge as an instrument of the expression and application (and thus the development) of the law in the resolution of disputes between litigants. *Judicial independence in these cases then acquires a twofold character*. First, it is necessary as an expression of the political role of the judge in extracting the law by reference to the autonomous judgments of judges as a class over time—that is it speaks to the independence of judges as a class to develop jointly an understanding of the meaning of law and its standards. That is, in this sense one can understand judicial independence as a means of avoiding *systemic corruption* of the autonomy of law. Second, it is a necessary expression of the role of the judge as an impartial administrator of justice in those individual disputes brought before her. In this sense, judicial independence can be understood as a means of avoidance of *individual or personal corruption*—the traditional failures of the cage of regulation in the face of interference by individuals for personal aims.

The second are those sub-systems consisting of statutes and administrative regulations. Here, the relation between the judge, the state apparatus and the individual litigants becomes more entwined.<sup>44</sup> But because the law is given and not within the province of the judge to derive it, the role of the judge in relation to the law is quite distinct.<sup>45</sup> The judge is no longer free to discern and apply the law from out of its reduction from custom and tradition contemporaneously applied. The law is now written as the expressed command of the people—either in statute or through the actions of an administrative agency to which quasi legislative authority has been vested. It is in this situation that one commonly speaks to the differences between civil and common law. In common law countries, the statute becomes embedded in

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<sup>43</sup> See generally, Frank B. Cross & Emerson H. Tiller, *Judicial Partisanship and Obedience to Legal Doctrine: Whistleblowing on the Federal Courts of Appeal*, 107 YALE L.J. 2155 (1998).

<sup>44</sup> See generally, Jonathan R. Macey, *Promoting Public Regarding Legislation Through Judicial Interpretation: An Interest Group Model*, 86 COLUM. L. REV. 223 (1986).

<sup>45</sup> At its limit, of course, it is possible to suggest that such law, that does not require extraction from the body of cases, requires neither lawyer nor a judge trained in the common law. “As in many utopias, one of the objects of the Revolution was to make lawyers unnecessary ... Fear of a gouvernement des juges hovered over French post revolutionary reforms and colored the codification process.” JOHN H. MERRYMAN & ROGELIO PÉREZ-PERDOMO, *THE CIVIL LAW TRADITION: EUROPE, LATIN AMERICA AND EAST ASIA* 29 (3rd ed. 2007).

the ancient common law system over which it occupies a superior space. While the words of the statute command, they do so the way an authoritative and unchanging pronouncement of a highest court might bind. That is, the statute itself provides the rule which it is then left to the courts to apply. And application requires interpretation and application within the dispute in which interpretation arises. Every statute now has a common law of interpretation, and in some respects, the common law of interpretation may sometimes overwhelm the language interpreted itself. It is in this sense, certainly, that the judges can be understood as well embedded within the political processes of common law states.<sup>46</sup> And yet it remains principally embedded within its own politics.<sup>47</sup>

In civil law countries, the principle was once clear but its application has become quite muddled since the middle of the last century. Judges under the Napoleonic Code were prohibited from introducing general principles of law, viewed as legislative in character,<sup>48</sup> but they could fill in gaps in legislation by reference to the code itself.<sup>49</sup> Eventually they could develop a jurisprudence for the application of the Code, always remaining loyal to its principles and constraints, and its decisions, though not binding, could serve as a gloss, more or less mandatory, on judges exercising their authority. Note the principles at work here. First, a distinction is made between law making and interpretation within the law. Second, that interpretation is itself to be exercised within the law. Third, so exercised, those interpretations, and those principles of interpretation—of reading the law—could be used as a basis for the application of law. *Taken together, the law is viewed as autonomous of both legislature and judge once produced.* And thus, autonomous it must be treated as self-referencing. The principles of its interpretation and application must be found within the code itself. The object of the judge, then, is to apply the law referencing the judicially extracted principles of interpretation, but not to make law in the process. Three points—first the judge was prohibited from applying or suggesting the application of constraints in higher law. For that purpose, most civil law states instituted a political apparatus, the constitutional court. To vest judges with the power to invoke this higher law would have vested them with an authority that was to be exercised by the people (through the legislature), and checked by another political institution (the constitutional court) itself divorced from the specifics of a particular case. And indeed, it might be understood that vesting the power of constitutional determination in a court would produce corruption in the

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<sup>46</sup> See, John A. Ferejohn & Barry R. Weingast, *A Positive Theory of Statutory Interpretation*, 12 INT'L REV. OF L. & ECON. 263 (1992) ("Fundamentally, this implies that judicial interpretations – especially those that stand unchallenged—must be seen as reflecting the strategic setting in which they are announced, no matter how they are motivated or justified."). I have noted as well that the judicial role in that political context makes inevitable that judicial interpretation will be severely disciplined where pronouncements tend to wander too far from the customs, traditions and expectations of the polity for which it is made. See Larry Catá Backer, *supra* note 19, at 340 ("Authority is measured by compliance.").

<sup>47</sup> See generally, Felix Frankfurter, *Some Reflections on the Reading of Statutes*, 47 COLUM. L. REV. 527 (1947); ANTONIN SCALIA & BRYAN A. GARNER, *READING LAW: THE INTERPRETATION OF LEGAL TEXTS* (Thompson/West 2012).

<sup>48</sup> A BARRISTER OF THE INNER TEMPLE, *THE CODE NAPOLEON*, art. 5 (William Benning, 1827).

<sup>49</sup> *Id.* art. 4.

sense that the law would not be applied evenly but would be varied to suit the circumstances of the cases. Second, the judge could not go beyond the law in seeking justice from out of the compulsion of statute or administrative regulation. Third, political constraint was exercised outside the law, though with effects within it—through the internalization of the risk of non- or mis-compliance by states and administrative agencies.<sup>50</sup>

These notions, of course, are inverted in jurisdictions with origins in the common law. In that case, the idea of self-referencing law, or of law restricted to its enactment through the state, is rejected. The older double autonomy of law is preserved (that is the autonomy of ordinary law and of the higher law of the constitution). Judges in these courts exercise a substantial authority with respect to the preservation of that dual autonomy. Their only substantive check (and it has been an effective one through the current period) is the judiciary itself. Where in the civil law system the law is autonomous of the judge (and the legislature after enactment), in the common law system the judicial role is viewed as autonomous of the state in the service of the law which is itself viewed as autonomous. Judicial power, then, is both interpretative and normative. While this is inherent in common law, it also became a feature of the role of judges in the interpretation and application of statute. It is in the role of the common law judge as the interpreter of statute that the connection between judge and law becomes clearest in its administrative and political elements. That quite important relationship was accomplished by the transference of the methodologies of the common law to the project of the interpretation of statutes and administrative regulations. What does that mean? The judge in common law systems, and especially that of the United States, treats the statute like any expression of law. While the words of this form of expression of law cannot be changed, everything else around it is subject to interpretation. And that interpretation is subject to application in specific cases. And those applications are then subject to standards of assessment for conformity with larger frameworks—the statute, the law in general, the intention of the framers. And ultimately all of this complex of interpretation and application is subject to the judicial understanding and application of the higher law of the constitution to the extent these may apply—directly or indirectly. Cases become the vehicle for this development through interpretation-application. These cases become an increasingly dense gloss on the statute. And because at the center of the common law methodology is the autonomy of judges, disciplined through the notion of the binding effect of superior judgements and a socialized tradition of respecting prior opinion, at some point the aggregate of cases may in some instances supplant or so cover the statute that the actual words of the provision may be lost within its gloss.

What does all of this mean for the comparative project of judicial reform in China undertaken within the globalized networks of judges and their common cultures and embedded within ideological systems contextually quite distinct? It means for my purposes here, that when one seeks to embed the forms of the system of judging that have developed within the strong and ancient ideological contexts of the West, the effects or functions that these forms serve will migrate with them. It is

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<sup>50</sup>See generally, Clifford J. Carrubba, Matthew Gabel & Charles Hankla, *Judicial Behavior Under Political Constraints: Evidence From the European Court of Justice*, 102 AM. POL. SCI. REV. 435 (2008).

on the shoals of that migration—the cultural and historical framework within which systems arise and operate—that migration tends to flounder.<sup>51</sup> Form and function are to a great extent *impossible to separate since the conception of the form is the product of its effects*. These effects are now easy to summarize:

First, judges serve a political role in their relation to law.<sup>52</sup> Judges are an essential component in the production of law, not merely through their interpretive and glossing power, but through their application of these judicial glosses in the case. Judges themselves, as a group, serve as a political actor, and an independent source of law making. The judiciary, as a class, is a political class. Certainly, they exercise, as an institutional class, their authority quite constrained by both the logic of their role (as limited to cases and to the law brought to them in disputes) and by the cultures of their practice. But within those constraints they exercise a certain gubernaculum in relation to law. In the West that is an important and necessary element—a strong constraint on the power of government as a whole to strip the people of their customs, traditions, and habits. And in political systems in which the preservation of popular values is a significant value, this makes sense.<sup>53</sup>

Second, cases themselves serve an important political role as well. Especially in the United States, the move toward legalization of the societal sphere has produced, in equal measure, the growing political role of the courts. Not the judges. The *courts themselves* now serve as a space where mass mobilization, political rhetoric and mass actions are now situated.<sup>54</sup> There are a number of well known examples. The most successful was the attack on the structures of racial segregation in schools culminating in *Brown v. Board of Education*. But there were others—the rights of sexual minorities to the decriminalization of their sexual activity, and ultimately the right of same sex couples to marry, and now the rights of transsexual people have all been sited in the courts, especially when agitation in the political space has been unavailing. Where courts operate as the interpreters of law, where they can, as a supplemental matter produce the grounding principles through which statutes may be interpreted and applied, and where they may also evaluate these by reference to the “higher law” of the state, it is inevitable that political culture will also begin to center on the courts.

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<sup>51</sup> This is particularly apparent within the context of understanding the nature of judicial independence in China. The difficulty is especially apparent when one seeks to import Western notions of judicial independence, dependent on a broad scope of interpretative authority vested in the judge and grounded in the ethos of common law, onto a political system in which such interpretative functions are as inherently political and bound up in the authority of a vanguard party. Qianfan Zhang, *The People's Court in Transition: The Prospects of the Chinese Judicial Reform*, 12 J. OF CONTEMP. CHINA 69, 99-101 (2003).

<sup>52</sup> Cf. Larry Catá Backer, *Inscribing Judicial Preferences into Our Basic Law: The Political Jurisprudence of European Margins of Appreciation As Constitutional Jurisprudence in the U.S.*, 7 TULSA COMP. & INT'L L.J. 327 (2000).

<sup>53</sup> See generally, ARISTOTLE, *supra* note 28.

<sup>54</sup> See Backer, *supra* note 19.

Third, courts begin to serve as the place where societal narratives are forged and popular expression is constructed and applied.<sup>55</sup> That is, the judicial function is not limited or focused on law and law making, or even the politics of those efforts. Rather, and perhaps more importantly, this form of judicial culture also transforms the courts into a site of the production of strong societal narratives.<sup>56</sup> By choosing among facts to emphasize, facts to marginalize, by choosing the methodologies of inference, by applying societal conceptions to the evaluations of facts, courts become a critical place where society's self-conception is formed and reinforced. The courts, more even than the political classes, are instrumental in the construction of the perceptions and practices of popular culture. Its only competition in the United States, for example, is the tale-spinning of our modern troubadours—television and movie production. For states in which the direction of societal mobilization matters, this ought to be an important consideration of the choice of form, especially in its American iteration.

Fourth, the independence of the judge, the judiciary as a class, and the proceedings in court is a function of the autonomy of law from the state. The state as an administrative apparatus—its gubernaculum, stands at arm's length from statutes once produced. It is to the judge that the political task of interpretation and the personal task of application in specific instances is assigned. Judicial independence is then understood as a means of avoiding both systemic corruption and individual corruption. Even when the state is the sole source of law, this remains true. The connection between the state and its law is severed at the time of its enactment. From that point, it becomes the province of the judge. As long as judges have an interpretive function, and as long as they must apply the law, they must remain as autonomous of the state as the law they apply and interpret.

Within this conceptual context, it is easy to suggest that transposition, especially to Marxist Leninist systems, becomes nearly implausible. Yet that would not necessarily be true. Rather, a fundamental understanding of cultural fracture beneath methodological practice is helpful for a perhaps more successful engagement with foreign systems. Western models of judging, and notions of independence, remain important to the Chinese project of judicial reform—not necessarily as models mindlessly imported, but rather as irritants that might help develop an indigenous system within its own context.<sup>57</sup> To that end, understanding how judges think<sup>58</sup> in a specific political and cultural context becomes a central element of analysis that connects concept to reality.

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<sup>55</sup> See generally, Larry Catá Backer, *Tweaking Facts, Speaking Judgment: Judicial Transmogrification of Case Narrative as Jurisprudence in the United States and Britain*, 6 S. CAL. INTERDISC. L.J. 611 (1998).

<sup>56</sup> See generally, Larry Catá Backer, *Culturally Significant Speech: Law, Courts, Society and Racial Equity*, 21 U. ARK. LITTLE ROCK L.J. 845 (1999).

<sup>57</sup> Gunther Teubner's notion of legal irritants as the key focus of transplantation is useful here. See Gunther Teubner, *Legal Irritants: Good Faith in British Law or How Unifying Law Ends Up in New Divergences*, 61 MOD. L. REV. 11 (1998).

<sup>58</sup> Cf. RICHARD A. POSNER, *HOW JUDGES THINK* (Harvard Univ. Press 2008).

### III. THE CONCEPTION AND OPERATIONALIZATION OF CHINESE JUDICIAL REFORMS

Chinese judicial reforms fit uncomfortably within this ideological framework of Western judging. That is not to say that there aren't great points of convergence of both form and effects. It is to suggest, though, that the overlay of the quite specific framing principles of the Chinese political system point to areas of necessary divergence between not merely the effects of the forms of Western judging, but of the forms themselves. There is a sense of the need for the Chinese judiciary to achieve the same level of institutional autonomy as a class—and among individual judges—as is common in other advanced states, but that such independence not challenge the leadership role of the CCP.<sup>59</sup>

And, indeed, the overarching framework for reform in its current iteration suggests points of divergence with the judicial models from which judicial reforms, including the vision in the White Paper, have emerged. That overarching framework embeds judicial reform as part of a much larger political and economic project—the project of Socialist modernization. Reform and the continued development of Socialist modernization in its economic, political, social, legal and cultural forms<sup>60</sup> are now organized through the Central Leading Group for Overall Reform,<sup>61</sup> which was created in 2013 to oversee that the Decision of the CPC Central Committee on Comprehensively Deepening Reform (“Decision Deepening Reform”).<sup>62</sup> Indeed, one ought to read the White Paper through the overall structure and substantive objectives of the Decision Deepening Reform. Chapter IX focuses on Rule of Law and the judiciary, which are tied together.<sup>63</sup> The lynchpin is the establishment of the

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<sup>59</sup> “The vision that the SPC has for the Chinese judiciary and judges can be seen from the description of the reforms above. The SPC intends to create a more professional judiciary (with a lower headcount), that is better paid, more competent, has performance indicators that look more like other jurisdictions, with an identity and operating mechanisms separate from other Party/government organs, that will be more autonomous, no longer under the thumb of local authorities, but operates within the big tent of Party policy.” *What China’s Judicial Reform White Paper Says About its Vision for its Judiciary*, SUPREME PEOPLE’S CT. MONITOR (Apr. 12, 2016), <https://supremepeoplescourtmonitor.com/2016/04/12/what-chinas-judicial-reform-white-paper-says-about-its-vision-for-its-judiciary/>.

<sup>60</sup> The General Program of the Constitution of the Chinese Communist Party describes a coordinated leadership role for the CCP in all these areas and ties them all within the greater Project of Socialist Modernization. See Constitution of the Chinese Communist Party, General Program, discussed by Larry Catá Backer, *Introduction: On a Constitutional Theory for China – From the General Program of the Chinese Communist Party to Political Theory*, LAW AT THE END OF THE DAY (Feb. 14, 2015), <http://lcbackerblog.blogspot.com/2015/02/on-constitutional-theory-for-china-from.html>.

<sup>61</sup> Zhongyang Quanmian Shenhua Gaige Lingdao Xiaozu was established in the wake of the 3rd Plenum of the 18th CCP Congress in December 2013. It is tasked with determining guidelines for further reform within the CCP Basic Line, which was also reaffirmed. It is meant to sidestep the usual bureaucracy to establish reforms more efficiently. It is chaired by Xi Jinping and its deputy leaders include the Premier of the State Council, the Politburo Standing Committee First Secretary and its Vice Premier.

<sup>62</sup> *Decision of the Central Committee of the Communist Party of China on Some Major Issues Concerning Comprehensively Deepening the Reform*, CHINA.ORG.CN (Jan. 16, 2014), [http://www.china.org.cn/china/third\\_plenary\\_session/2014-01/16/content\\_31212602.htm](http://www.china.org.cn/china/third_plenary_session/2014-01/16/content_31212602.htm).

<sup>63</sup> *Id.* ch. IX (“We will deepen reform of the judicial system, accelerate the building of a just, efficient and authoritative socialist judicial system to safeguard the people’s rights and interests, and ensure that the people are satisfied with the equality and justice in every court verdict.”).

supremacy of the State Constitution as the operative source of administrative and institutional (though not political) norms.<sup>64</sup> But the constitutional supremacy principle is read institutionally as well as normative. The Decision Deepening Reform makes this clear: “We will establish a system of legal counsel universally, improve the review mechanisms concerning normative documents and major decisions, set up a scientific indicator system and assessment standard for legal system building, and improve review mechanisms concerning laws, regulations and normative documents. We will improve the law education mechanism and raise the public's awareness of the rule of law.”<sup>65</sup>

This institutional approach to constitutional supremacy then guides the necessary reforms to the administrative apparatus that is meant to operationalize the principles and structures in the State Constitution. Law enforcement mechanisms and institutions are to be made more efficient.<sup>66</sup> Law and its enforcement are critically tied together in the objective to strengthen, together, the independent exercise of the judicial and procuratorial powers, in accordance with law.<sup>67</sup> This is further refined by the objectives of improving the mechanisms for the use of judicial powers, through systemic reform of the judiciary.<sup>68</sup> This includes extending principles of transparency and popular participation.<sup>69</sup> But it is also embedded within the larger project of reforming the working style of officials.<sup>70</sup> Working style improvement brings with it more muscular systems of assessment and monitoring.<sup>71</sup> Lastly, the human rights enterprise in China is to be furthered<sup>72</sup> by centering the conception of

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<sup>64</sup> *Id.* ¶ 30 (“We will further improve the supervision mechanism and procedure for the implementation of the Constitution and raise to a new level the comprehensive implementation of the Constitution. We will establish and improve the system within which the whole society is loyal to, abides by, upholds and applies the Constitution and laws.”).

<sup>65</sup> *Id.*

<sup>66</sup> *Id.* ¶ 31 (“We will integrate major law-enforcement bodies, relatively centralize the law-enforcement power, press ahead with comprehensive law enforcement, and do our best to resolve problems such as overlapping functions and duplicate law enforcement to establish an authoritative and efficient administrative law-enforcement system with the integration of power and responsibility.”).

<sup>67</sup> *Id.* ¶ 32 (“We will establish a judicial personnel management system fitting their professional characteristics, improve the system for unified recruitment, orderly exchange and level-by-level promotion of judges, procurators and the police, improve the classified management system of legal personnel, and guarantee the job security of judges, procurators and the police.”).

<sup>68</sup> *Id.* ¶ 33 (“We will optimize the distribution of judicial functions and powers, improve the system of judicial power division, coordination, checks and balances, and strengthen and standardize the legal and social supervision over judicial activities.”).

<sup>69</sup> *Id.* (“We will increase the persuasiveness of legal instruments and press ahead with publicizing court ruling documents that have come into effect. We must strictly regulate the procedures of sentence commuting, release on parole and medical parole, thereby enhancing the supervision system. We will extensively implement the people's assessor system and people's supervisor system to expand channels for the people to participate in legal affairs.”).

<sup>70</sup> *Id.* ¶ 37 (“We will speed up institutional reform to fight formalism, bureaucracy, hedonism and extravagance. We will improve the system under which leading officials take the lead to improve work style”).

<sup>71</sup> *Id.* (“We will improve the examination and accountability system of selecting and appointing officials, and make efforts to correct such erroneous practices as craving for official positions. We will reform the evaluation process for the performance of official duties and focus on solving the problems of completing projects for the sole purpose of showing off or boasting about their performance, as well as nonfeasance and misconduct.”).

<sup>72</sup> *Id.* ¶ 34 (“The state respects and protects human rights.”)

human rights through the legal and judicial mechanism.<sup>73</sup> The conceptualization of human rights within the judiciary and law is framed within a quite specific set of objectives.

What emerges are the outlines of a quite distinctive conceptualization of law and the judiciary as embedded in each other. Law is the object of which the judiciary, as well as the police and the procuratorate are the instruments. Each has their role—and their relation to law—but each is autonomous of and embedded within law. Autonomous to the extent that they are the instruments of the application of law within the spheres of their jurisdiction and function. Embedded to the extent that their instrumentality is itself defined by and constrained within law, the same law that each administers and applied. Independence, then, is a necessary predicate of their operation. But not independence from but through law. And independence from each other, and from individuals whose positions might otherwise invite either systemic or individual corruption (through the influencing of interpretation or application in a particular case). But the independence to apply law is quite distinct from the independence to interpret and create it. And with respect to that the judiciary would exceed its authority. That is a function of the Socialist Democratic System itself.<sup>74</sup>

This conceptual framework, then is useful for understanding both the thrust and scope of the latest round of judicial reform. The reform is not meant to alter the basic premises under which the judiciary has been developed since the time of Reform and Opening Up.<sup>75</sup> Rather, the reforms tend toward technical improvements in the delivery of dispute resolution services—they touch on judicial competency and those methodologies that enhance the sense of legal certainty and predictability. These can be usefully divided into judicial system reform, trial system reform, and supervision reform.

Judicial system reform targeted systemic corruption and efficiency. It furthered judicial autonomy from other administrative units. It has included rules for the separation of the duty of executing verdict from judges, the restructuring of the financial system for judicial organs, and the establishment of circuit tribunals for Supreme Court with jurisdiction on civil dispute and disputes with government. In addition, there have been efforts to explore innovation in the hierarchy system that are the connection with local government hierarchy system, to clarify the jurisdiction of different judicial organs on different levels, and to improve the internal supervision mechanism. Most important, perhaps, are efforts to align CCP discipline

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<sup>73</sup> See *id.* (setting out a list of specific objectives).

<sup>74</sup> *Id.* ¶ 27 (“We will improve the socialist legal system with Chinese characteristics, and perfect the system of legislative drafting, argument, coordination and review to improve the quality of legislation and prevent regional protectionism and legalization of departmental interests. We will improve the system within which people's government, people's court and people's procuratorate are elected by, responsible to and supervised by the people's congress.”).

<sup>75</sup> See Mei Ying Gechlik, *Judicial Reform in China: Lessons From Shanghai*, 19 COLUM. J. ASIAN L. 97 (2005); Wang Yaxin, *Judicial Cost and Judicial Efficiency: The Financial Guarantee for Courts and Incentives to the Judges in China*, 2010(4) JURISTS REVIEW. See generally Qu Jingdong, Zhou Feizhou & Ying Xing, *From Macromanagement to Micromanagement—Reflections on Thirty Years of Reform From the Sociological Perspective*, 2009(6) SOCIAL SCIENCES IN CHINA.

and judicial discipline mechanisms with criminal investigations—an important element of the current focus on anti-corruption efforts.

Trial system reform, including its manifestation as the expression of the state's view of human rights has also produced some reform since 2013. These include reform of the trial evidence system, the establishment of case record tracing system and accountability systems, reform of litigation procedure to improve people's litigation rights and to build in basic human rights in criminal justice system. The latter is to be improved by certain measures, including prevention of extorting confession by torture and better control and mitigation of judicial error. The latter is especially to be understood as tied, again, to efforts to mitigate the effects of corruption. Human rights, and the democratization of the judicial process, are also meant to be furthered through the greater popular participation in the judicial system. This includes improvement<sup>76</sup> of the People's Assessor system,<sup>77</sup> which had been criticized for its empty form.<sup>78</sup>

Supervision reform targeted individual corruptibility. It thus focuses more on the judge than the system in which she is embedded. Reform has included improving regulations on illegal meetings between judicial employees and lawyers or other interested parties, separating the duty of executing verdict from judges, restructuring the financial system for judicial organs, and establishing circuit tribunals for the Supreme Court with jurisdiction on civil disputes and disputes with government. Supervision reforms have explored new hierarchy system that sever the connection with the local government hierarchy system. These efforts seek to clarify the jurisdiction of different judicial organs on different levels and improve the internal supervision mechanism. There have also been corresponding efforts to establish and institutionalize coordination of procedures between the Party disciplinary and inspection mechanism with criminal investigation.

But legal certainty and predictability has also pushed the courts to seek to develop their own internal cohesion as the course of legal doctrine and the standards for its application. The Guiding Cases system presents the best example of this effort to develop institutional self-referencing cohesion. The Guiding Cases system was announced officially in 2010.<sup>79</sup> It adds a new component to the Chinese legal system by effectively introducing a new legislative form—cases that must be considered by judges in deciding their own cases.<sup>80</sup> The Guiding Cases System was given approval in the 4<sup>th</sup> Plenum Decision's statement of objective that courts “strengthen and

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<sup>76</sup> The reform includes greater authority to participate, a clarification of their roles. See Terry Ng & Laura Zhou, *China to Expand Court Assessors System as Part of Judicial Reform*, S. CHINA MORNING POST (Oct. 30, 2014), <http://www.scmp.com/news/china/article/1628174/china-expand-court-assessors-system-part-judicial-reform>.

<sup>77</sup> On the initiation of the People's Assessor System, see, e.g., Di Jiang, *Judicial Reform in China: New Regulations for a Lay Assessor System*, 9 PAC. RIM L. & POL'Y J. 569 (2000).

<sup>78</sup> See Ng & Zhou, *supra* note 76, (“Tong Zhwei, a professor at East China University of Political Science and Law, said many assessors just followed the instructions of judges without careful examination because of a lack of legal knowledge.”).

<sup>79</sup> See *supra* note 26.

<sup>80</sup> See generally, Wang Chenguang, *System Construction and Technique Innovation: Challenges Our Guiding Cases System is Facing*, CHINA GUIDING CASES PROJECT, Feb. 1, 2012.

standardize judicial interpretation and case guidance.”<sup>81</sup> The 2013 Supreme Judicial Court Reform Plan emphasized the objective of expanding the important role of guiding cases.<sup>82</sup> There was a sense of their possible utility in augmenting the autonomy of the judiciary from law, and the law from the state apparatus through the development of a strong interpretive authority in the Courts.<sup>83</sup> But the construction of the Guiding Cases remained very much a top-down project, relying on the review and determination of the administrative apparatus of the Supreme People’s Courts for the determination of those cases to select and those to ignore.

But the relationship between these Guiding Cases and other law is unclear. First the Guiding Cases are not mandatory in the sense of statutory law—they are meant to be taken into account, the actual effects of which are ambiguous. It is unclear how one can measure the effectiveness of this obligation or police its uniformity. But then, that has been an issue of the common law and its methods of statutory interpretation. “The ambiguous status and function of the Guiding Cases in the Chinese codified legal system means that the Guiding Cases play only a supplemental role, by illustrating and improving codified rules through cases.”<sup>84</sup> And indeed, the object is not necessarily to introduce common law judging in China, but rather to amplify and coordinate the supervisory authority of the higher-level courts. Professor Susan Finder notes that these Model Cases serve substantive and well as political purposes (noting the direction of higher level thinking), they might serve as supplements to legislation, or to publicize the accomplishments of noted lower courts.<sup>85</sup> But they may also serve as a means through which the state communicates with stakeholders about political matters, for example with respect to domestic violence.<sup>86</sup>

The Guiding Cases are also subject to some suggestions for improvement. These suggestions are grounded in quite distinct principles that tend to define their purpose and effect. For those who seek to increase the binding authority of these cases as well as the autonomy of the Judiciary suggestions tend to focus on citation rates, internal monitoring and evaluation systems, and supervisory efforts to reward lower court

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<sup>81</sup> See *CCP Central Committee Decision Concerning Some Major Questions in Comprehensively Moving Governing the Country According to the Law Forward*, CHINA COPYRIGHT AND MEDIA (Oct. 28, 2014), <https://chinacopyrightandmedia.wordpress.com/2014/10/28/ccp-central-committee-decision-concerning-some-major-questions-in-comprehensively-moving-governing-the-country-according-to-the-law-forward/>.

<sup>82</sup> See Susan Finder, *Using Model Cases to Guide the Chinese Courts*, CHINA POLICY INSTITUTE ANALYSIS (Apr. 7, 2014), <https://cpianalysis.org/2014/04/07/using-model-cases-to-guide-the-chinese-courts/>. Finder notes that this innovation is not new, but its emphasis is. Model cases have been circulating in some form since the 1980s and are understood as inherent in the power of the Supreme Court to supervise lower courts.

<sup>83</sup> See *supra* note 5.

<sup>84</sup> Wang, *supra* note 80. Dean Wang notes as well further ambiguity – the lack of guidance with respect to the weight to be accorded to holding versus dicta, or the standards for distinguishing cases based on differences in facts. “While the SPC may have intended to introduce some elements of the common law tradition into the Chinese legal system through the Guiding Cases, the current Guiding Cases System overlooks some of the common law’s most important embedded skills and techniques and this may impair meaningful interpretation of Guiding Cases in lower courts.” *Id.* (I’m not sure what this *id.* is referring to).

<sup>85</sup> Finder, *Using Model Cases*, *supra* note 82, at 3; Deng, *Accord*, *supra* note 11, at 10.

<sup>86</sup> Deng, *supra* note 11, at 10.

judges actually referencing Guiding Cases in their decisions.<sup>87</sup> Those seeking greater autonomy of law through judges suggest a closer analogy to the common law practices of opinions with “natural authority” to reduce reliance on administrative power.<sup>88</sup> Yet others reject the project as little more than window dressing—they are selected precisely because they are not controversial thus making them meaningless additions to the jurisprudence.<sup>89</sup> And it remains rarely invoked, though it is hoped that the use of Guiding Cases in more specialized courts will produce better usage.<sup>90</sup> Interpretive power, to the extent it is exercised remains administrative—inherent in the authority in the Supreme People’s Court to issue judicial interpretations, binding on lower courts.

The March 2016 Report of the Supreme People’s Court, *Judicial Reform of Chinese Courts*,<sup>91</sup> gives us a sense of the future direction of reform. We consider those here. The conceptual foundation is the connection between the judiciary and the rule of law; the notion is that the judiciary in its application of law manifests the most intimate connection between people and law (in the old sense they are the instrument of justice or injustice).<sup>92</sup> But the connection of the judiciary is not merely to rule of law, but also to rule of law within the context of socialist modernization; improving the judicial system and its administration “are conducive to . . . accelerating the modernization process of China’s governance system.”<sup>93</sup> It follows that the structure of reform are not merely top down. They are also intimately connected to the general reform of the state and its apparatus in a coordinated way.<sup>94</sup> And indeed, the White Paper explicitly embeds itself into the comprehensive reform under the leadership of the CCP undertaken through the Central Leading Group for Deepening Overall Reform.<sup>95</sup>

The White Paper focuses on eight areas of reform: (1) Ensuring Independent and Impartial Exercise of Judicial Power Pursuant to Law; (2) Strengthening the Judicial Protection Mechanism of Human Rights; (3) Improving the Functional Mechanism of Adjudicative Powers; (4) Promoting Judicial Transparency; (5) Expanding Judicial Democracy; (6) Strengthening People-friendly Justice; (7) Improving Professionalism of Court Personnel; and (8) Enhancing the Information Technology Capacity of Courts. Much of this highlights reforms already well under way, and suggests their systematization. The White Paper concludes with its emphasis on its structural objectives—problem oriented approaches, incrementalism, and coordination with national policy and objectives. Judicial independence is understood as the development of centralized institutional mechanisms and control.

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<sup>87</sup> *Id.* at 10.

<sup>88</sup> *Id.* at 13.

<sup>89</sup> *Id.* at 15.

<sup>90</sup> Jeremy Daum & Jacob Clark, *Unprecedented: Beijing’s IP Court’s Use of ‘Guiding Cases*, CHINA LAW TRANSLATE (Aug. 31, 2016), <http://www.chinalawtranslate.com/beijing-ip-court-making-new-precedent-on-guiding-cases/?lang=en> (Guiding cases are so few they are easy to distinguish, they have no mandatory effect and they not be cited).

<sup>91</sup> SUPREME PEOPLE’S COURT OF THE REPUBLIC OF CHINA, *supra* note 18, at Conclusion.

<sup>92</sup> *Id.* at Foreword.

<sup>93</sup> *Id.*

<sup>94</sup> *Id.* at Ch. 1.

<sup>95</sup> *Id.* (six specialized sub groups consider judicial reform issues; these are supplemented by leading groups for judicial reform established under the auspices of the Chief Justice of the Supreme People’s Court, with mirror groups set up in lower levels of the judicial administration).

Human rights through the judiciary are understood in a very specific sense—avoid unjust, false and wrong cases (the law is always presumed to be right), protect attorney rights to exercise their duties in accordance with law, preserving prisoner dignity in proceedings, regulate state compensation and standardize judicial procedures. Improving the functional mechanisms of adjudicative power is understood as focusing on systemic corruption through judge shopping and interference with decision-making. It also touches on accountability and the reduction of individual corruption. And it also focuses on improving the Guiding Cases system, noting its particular utility for specialized courts. Transparency is limited to case reporting and “big data” issues. Judicial democracy touches on reform already underway for the People’s Assessor system and its challenge to the Western jury model. But it is also meant to tie the judiciary to the legislative apparatus, especially the NCP and the CPPCC. Lastly, it focuses on another aspect of institutional integrity—the system of supervision by case parties. People-friendly justice is meant to reduce the transaction costs of accessing courts. They speak to the construction of litigation service centers, national judicial aid systems, and people’s tribunals and alternative dispute resolution institutions. Improving professionalism touches on judicial selection and appointment and the conduct of judges and judicial personnel outside of their duties. Technological reform includes improving case management systems and case information.

Taken together, the trajectory of Chinese judicial reform emerges clearly. First, much of the focus appears to be on the office and functioning of the individual judge. An ideal of that office emerges, one in which the judge is a highly sophisticated administrator of law expert in applying the law to the cases before her. To the protection of that ideal that reform points. Protection against coercion, interference, and the indicia of judicial independence are cultivated in the service of the ideal. Second, just as the ideal judge must be protected from outside forces, so must internal discipline be cultivated. The judge herself must be socialized in a cluster of traits that make it possible for her to fulfill her office and administer the law appropriately. To that end monitoring and assessment, training and self-criticism are important. Important as well are vehicles like the Guiding Cases that serve as a hornbook of preferred administration of law. Third, the public must have confidence in the ability of the judge to appropriately administer law. To that end transparency and access to the courts must be developed. The people must be guided to the judge as the judge is guided to the administration of law. Fourth, the judiciary as a whole represents the institution of the judge which serves to protect its members and advance its development collectively. It serves to advance the narrative of the ideal judge and ensure that the systemic qualities of judging work appropriately—from the courtroom to the management of personnel and the budgeting of resources necessary for the administration of justice. Fifth, while the judge and the judiciary stand apart and independent in the administration of the law they do not have the power to create or change the law. Even the practice of gap filling is one with political implications. With respect to that, the judge must be cautious—it exceeds her authority to administer the law, and the judiciary must be mindful of the limits of its jurisdiction. Sixth, the judiciary is at its most powerful when it interprets the law in ways that serve the administration of justice. It is at its weakest when it seeks to interpret and

advance law through cases or other pronouncements beyond the regulatory framework it is charged with administering.

The curious thing that is missing in analysis, therefore, is the tie between judicial reform and the General Program and CCP Basic Line. Yet, the center of gravity remains the CCP and not the judiciary.<sup>96</sup> That absence of connection substantially weakens the vision of judicial reform precisely because it detaches that vision from the fundamental ruling ideology on which the operation of the state and its political culture rests. Is it possible to discern that connection between the judicial vision for reform, the importation of foreign forms and ideologies, and the basic first principles of the People's Republic? It is to that question that the last section turns.

#### IV. TOWARD A LENINIST APPROACH TO THE ROLE OF THE JUDGE IN A MARXIST-LENINIST STATE.

This essay suggests that the criticisms suggest only the surface of the problem—the recognition of the dissonance between the embrace of the forms of the Western judge and difficulty of then successfully grafting that form onto a system that rejects the effects of the graft. The effort either produces empty vessels or they suggest the need for further reform that tends toward the direction of embracing the normative structures that make the forms of the judge imported effective. This is only natural—the form of the Western judge is only effective as the cumulative product of its effects—and indeed it effects define the form. To have one without the other produces . . . contradiction. Or the need for new forms.

If that is the case, then what do these efforts at judicial reform, what does the accumulation of reform, reveal about the direction of reform thinking? Let us approach the question from the framework of the ideological relationship between the state, law and the judge that was developed in Part II. The relationship between the state and the law on which judicial reform efforts are grounded are quite precise and yet incompatible to those that have now become established in the West. Gubernaculum continues to exist in both in ancient and modern forms. The CCP exercises the prerogatives of governance, of the political authority that is the mark of a vanguard party. But the distinction between gubernaculum and jurisdiction does not exist. For the prerogatives of the gubernaculum include that of jurisdiction precisely because of the nature of the vanguard itself. The state and law stand in a relation of autonomy to each other, but the CCP and the law do not. Neither does the state stand in an autonomous relation to the CCP. Where are the delimiting constraints on the prerogatives of the gubernaculum of the CCP—they are those of the fundamental character of the mission of the vanguard itself. Jurisditio, then as an autonomous and constraining (though not controlling) force is quite strong. But it has no connection to law—understood in its traditional sense. Instead, the *jurisditio* of Marxist Leninist states is founded on the overall *jurisditio* of its objectives and the founding ideology on which the legitimacy of the vanguard status rests. In China

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<sup>96</sup> See Shan Yuxiao & Li Rongde, *Party Orders Judges to Follow Due Process in Commercial Cases*, CAIXIN ONLINE (Sept. 5, 2016), <http://english.caixin.com/2016-09-05/100985637.html> (“The party's Central Leading Group for Overall Reform, headed by Party Secretary Xi Jinping, released a document on Sept. 2 that aims to protect the interests of private firms and investors who face trial for fraud, flouting work safety or environmental rules, or are charged with other forms of illegal business dealings.”).

*jurisditio* is easy to identify—it is embedded in the General Program of the Communist Party and it is memorialized by the constraining notions of the CCP Basic Line. These are not mere propaganda or idle slogans. Rather they represent the strongly controlling law, understood as framing principles, within which the gubernaculum of the CCP can be exercised and through which its *jurisditio* with respect to law can be ordered.

Thus, within China, the principle of an autonomy between the state and law has been rejected as incompatible with its societal and political order. Likewise, there can be no autonomy between the state and the prerogatives of those who wield the entirety of political power in the state. The principles that constrain power in the West, grounded in memorialized constitutions, is exercised instead through the binding authority of the principles and objectives which constrain the exercise of legitimate authority by the vanguard party. As such, law is understood to be deeply embedded in governance authority of the wielders of political authority and exercised in accordance with the administrative structures that they, exercising their prerogatives, establish. That identity between the state and law, then, presumes a subordinate relationship between the law-state axis and the prerogatives of the vanguard party. But the vanguard party does not exercise gubernaculum unconstrained. Indeed, their constraints are to some extent far stronger and more precise than those of *jurisditio* as understood in the modern West. Where in the West *jurisditio* can be understood as law as an autonomous enterprise, in Marxist-Leninist China *jurisdictio* can be understood as the principles of its vanguard authority—and more specifically in the General Program of the Chinese Communist Party. That General Program assumes the character and role of the higher law of the West.<sup>97</sup> And in this context, it assumes the role of the higher law of the political order that both constrains and orders it, that provides the basis of legitimacy in conformity to it and that serves as the basis of the assertion of the authority of gubernaculum by the CCP. The state, then, assumes a quite distinct character—as an expression of government but not as the home or vessel of the authority of state.

This relationship between the law and the state clarifies the relationship between the judge and the law—and evidences the difficulties of appropriating the methodologies and practices of a system grounded in a different relationship between law, the state and the judge. The judge stands before the law the way the state stands before the law. Both stand as the instruments of a higher power, and their operating space is constrained by the autonomy the gubernaculum of the CCP. It is in that context that one can understand the nature of the constitution and operation of the judge and of the judiciary. There is an autonomy to both, but only a subordinate autonomy that must respect the limits of its independent operation constrained by the higher authority of the CCP. The path toward judicial reform in China suggests that the judge does not serve as the centering element of law. Rather, the judge is the mechanism through which law flows through from the vanguard party to the people and back again. The judge is the administrative agent of law but neither its source

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<sup>97</sup> See Larry Catá Backer, *Pt. 31 (The Constitutional Character of the General Program) – On a Constitutional Theory for China – From the General Program of the Chinese Communist Party to Political Theory*, LAW AT THE END OF THE DAY (Sept. 12, 2016), <http://lcbackerblog.blogspot.com/2016/09/part-31-constitutional-character-of.html>.

nor its guardian. The judge guards the institutional and administrative apparatus of law but not the law itself. For to guard the law one must be in a relation of autonomy with it—and that role is reserved within the prerogatives of the institution with the prerogatives of gubernaculum—the CCP. And thus, the role of the judge is to see to it that the law is properly administered, that it is properly applied to the people. In this way, the state apparatus can complete its self-referencing complex—law giver, administrator of societal, political and economic structures, and institutional protectors of the obligations of the state toward its masses. Indeed, that notion of obligation, of administrative burden grounded in law but not in an autonomous relation with it, is the essence of the relationship between the judge and the edifice of human rights as conceptualized and applied within the judiciary.

It is in this sense that one understands as well, the essence of the independence of the judge, and its centrality to the system of law. The judge stands between the law as an abstract obligation, and its activation in the relations among the masses and between them and the administrative officials of the state. The judge must stand in a subordinate or administrative relation to the law, but in that relation, must be absolutely independent of all of the rest of the apparatus of *state*. As the conduit of law, she stands alone and untouchable. That is the great limit of the gubernaculum of the CCP and the state in relation to the judge before whom stands litigants in need of the settlement of a dispute, or the state procuratorate seeking to *administer justice through law*. But that also delimits the boundaries of judicial independence. Just as the judge stands independent as the conduit of law, so she must remain the recipient of the of law which she must apply. Thus, the judge must be viewed as completely dependent on the political authority, and through the political authority on those vested with the power to make law for the interpretation thereof. The judge, therefore is as incapable of administering the law as she must be fully vested with the authority to administer justice through law. That is a distinction that is unknown in the West and incompatible with its basic construction of the law and the judge. The essence of judicial independence in the context of judicial reform in China is tied to the *protection against individual or litigation corruption*—the corruption of the case and the corruption of the individual understood as having its greatest effects in the ability of the judge to administer the law in the cases before her.

If the judge is a conduit, then the judiciary stands as the institutional edifice within which that authority may be developed and exercised. That authority, however, is not concerned as much with the development of law as with its application—with the science of the administration of justice and not its construction. The judiciary itself is meant to serve as the aggregated authority of the judges to administer law in accordance with its terms. That is, just as Western judges are disciplined in their relation to law and to the application of law in the cases before them through the institution of the judiciary—its customs, traditions, working style and the accumulated precedents that serve to guide and constrain the exercise of the judicial function—so the Chinese judge is disciplined in their relation to the administration of law through the cases they must determine through the institution of the judiciary, which serves to develop and promote a distinctive working style. But the Chinese judiciary focuses not on precedents but on the behaviors of the judge and the better

application of law.<sup>98</sup> That is the object of reform and the great problem at the center of judicial reform efforts: how does the judiciary develop the institutional capacity—the cultures, mores, and authority—to cultivate a distinctive working style among judges. It is to the perfectibility of the judge rather than to the development of law that the judiciary derives its greatest authority. Indeed, even the great Guiding Cases System<sup>99</sup> can be understood in this light, a project that is meant to provide those narratives that help a judge to better administer law through the internalization of the behaviors of the perfect judge—*qingguan* (清官). And the perfect judge stands in a perfect relationship to the law which she receives and administers—“Pure, orthodox and incorruptible in his own behavior, he unfailingly establishes the true nature of the crime and its culprit.”<sup>100</sup>

Even as the judiciary stands to ensure that judges strive toward perfectibility in their roles—rewarding the good and disciplining the bad, so the judiciary thus stands as the protector of the *systemic integrity of the office of the judge*. The aggregate of judges stands as the institutional protector of the individual judge against the failures of other officials who themselves seek to corrupt the system for their own ends. The judiciary stands against the official—whether administrative or CCP official—who fails in their own obligation to law and the administrative burdens of the state. Judicial reform must focus not merely on the corrupt judge, but on the corrupt official—including the corrupt Party cadre. It must develop the institutional infrastructures so that it may develop an institutional autonomy from the administrative apparatus with respect to the administration of law, even as it must develop the capacity to receive and apply the law that is produced by the administrative apparatus itself.

Who then, stands in a direct relationship with *jurisditio*? It is not the administrative apparatus. Their obligation is to memorialize law and to serve as the vehicle through which law is produced and delivered to the masses. The direct relationship, must, in the first instance develop between the CCP itself and the law. That relationship is primary and complete in itself. The *law, in this sense, does stand autonomous of the state, but only because it shares an identity with the vanguard Party*. But that identity is itself constrained by a higher law that constrains but does not control—the “higher law” of the CCP itself. It is that dual relationship between state and law and between law and Party that shapes the administration of law in China. And that is also the operational heart of judicial reform. It is an operational heart that is practically incomprehensible to those raised on the complex ideologies of the Western judge. But it is just as complete and just as authentic, in its own sphere. *For Chinese judicial reform, it is in the perfectibility of the judge that lies the perfectibility of law that in turn ensures the perfectibility of the judge.*

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<sup>98</sup> Fu Hualing, *Building Judicial Integrity in China*, 39 HASTINGS INT'L & COMP. L. REV. 167, 168-69, 175, 180 (2016) (describing the Chinese context).

<sup>99</sup> Jiang Xiaoyi & Shao Ling, *The Guiding Case System in China*, 1 CHINA LEGAL SCI. 106 (2013); see also Chen Xingliang, *China's Guiding Case System: A Study on the Mechanisms of Rule Formation*, 1 PEKING U. L. J. 215-58 (2015) (providing a historical view)

<sup>100</sup> See, WILT L. IDEMA, *JUDGE BAO AND THE RULE OF LAW: EIGHT BALLAD STORIES FROM THE PERIOD 1250-1450*, ix (World Scientific 2010).

And thus, there is something to the criticisms of the path toward reform, from left and right, and both within and outside China. These reflect both the contradictions of a grafting process that seeks to import the forms but avoid the effects of forms of judging developed in the West and now, to some extent internationalized *and* the difficulty of extracting the forms of the judge from its ideological context. For example, Jerome Cohen, an influential commentator, has rejected the idea of judicial independence, precisely because of its inability to move the judiciary towards independence from the CCP.<sup>101</sup> Chinese commentators, on the other hand, view the reforms, especially for example the new judicial selection committees as a means to reducing judicial corruption in individual cases.<sup>102</sup> The difference, of course, is perspective. The external view focuses on systemic corruption through a standard of systemic autonomy from the state. The domestic view tends to focus on individual corruption through a standard of individual independence from local officials and litigants. The thrust of criticism is the inability of the judiciary to establish itself as autonomous and to protect and expand the autonomy of its relationship with law as against the administrative and political institutions of state. For that is, of course, the fundamental ideological basis on which the conceptualization of the judge and judging rests in the West. Taking the forms of judging from the West opens the door to the insertion of its ideological foundations as well. And the resistance to that “door opening” produces tension and controversy over the efficacy and direction of reform. The answer, of course, is that such autonomy of the judge and the judiciary from the political and administrative institutions of state, and the protection of the autonomy of the relationship between the judiciary and law cannot be in China.<sup>103</sup> *And indeed it should not be.*

That does not mean—as is sometimes adopted by the simple minded, that autonomy of the judge, the judiciary and law ought not to be developed. The answer appears to be more complex. And the direction of that answer lies in an initial distinction between the relationship between the judiciary and law (the interpretive function) which retains its political and therefor its deeply embedded character, and between the judge and state apparatus in the application of the law to disputes to be resolved (the application function) which retains its autonomous function an on which judicial independence from both state and party must be based as the foundation. Thus, clarity of ideological foundation and further reform that is better

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<sup>101</sup> Cohen, *supra* note 7. Professor Cohen argues: “The Party totally dominates the legal system, including the education, training, and day-to-day operation of its personnel and institutions. “Judicial independence,” as it is commonly understood outside China today, is the enemy and forbidden by Party rulers even to be discussed in law schools. The term is only used in a positive way in Beijing to describe efforts to insulate local prosecutors and judges from local influences including corruption, social connections, local protectionism, and other forces that divert local legal officials from following the central Party authorities’ instructions.”

<sup>102</sup> Shan Yuxiao & Li Rongde, *China Pushes Ahead with Independent Committees to Select Top Court Officials*, CAIXIN ONLINE (Sept. 8, 2016), <http://english.caixin.com/2016-09-08/100986809.html> (“The committees also aim to tighten oversight on the conduct of judges and prosecutors inside and outside the courtroom. Four Shanghai prosecutors, including a deputy head of a unit handling civil cases at the Shanghai People’s High Court, were expelled or demoted in August 2013 after they were shown on video soliciting sex workers that a businessman paid for at a private club, the court said ... Analysts said an independent committee may also help rein in corruption among judges.”).

<sup>103</sup> Larry Catá Backer & Keren Wang, *The Emerging Structures of Socialist Constitutionalism with Chinese Characteristics: Extra-Judicial Detention and the Chinese Constitutional Order*, 23 PAC. RIM L. & POL’Y J. 251, 289, 340 (2014).

and more consciously tied to that foundation is necessary to align the judge, the judiciary and law in a more coherent manner, consonant with the governing ideology of the state.

But what it does suggest is that the process of interpretation—both the process of interpretation and application at the heart of common law judging, and the art of glossing statutes, developing standards for their application and a common law of their meaning, must be exercised—*but need not be exercised by the courts to retain their legitimate character*. What Chinese judicial reform makes quite clear is that it represents only half the effort at the reform of the judicial role in the development of truly Socialist rule of law in China. Current efforts focus on the administration of law. To focus on the interpretation and development of law as a living part of the administration of the state, it will be necessary to develop a robust institution that exercises the power to make the political determinations that are at the heart of both statutory glosses and judicial interpretation around classes of issues. What that requires, then, is the exercise of an interpretive capacity within the only institution with the political prerogative to make those determinations—*it must be made within the institutions of the CCP itself*.<sup>104</sup> This is not a call for the development of parallel courts. Far from it—such an institutional development would be subject to the same ideological constraints that those that now attach themselves to the Chinese judge. Instead, an interpretative facility must be created as part of the political work of the CCP. It may be staffed by experts—perhaps academics or other well-qualified officials who serve as the instruments of CCP authority and who provide guidance. And the institutionalization of this facility will be significant, most likely housed within the NCP complex of institutions and under the oversight of the Politburo Standing Committee or its designees. Its role would be to develop a web of interpretation that mimics the jurisprudence of the West. Perhaps all judges must seek a statement of the law (and standards) applicable to the particular case before them. Once that opinion—a political judgment—is rendered, then the judge is free to act independently in the administration of that law to the dispute before her. The institutions of that interpretive facility would then develop interpretive coherence that the Guiding Cases were meant to deliver but in a direct and coordinated way.

And that leads one again to *first principles*. Underlying all of these debates—some normative and some technical/methodological, is a fundamental issue that tends to go unexamined. That issue touches on the connection between the judge-judiciary and the exercise of the judicial function. When people speak to judicial reform, they use that as a shorthand to speak to the judge embedded within the institution of the judiciary. That, I suggest, overly narrows and centers the issue of judging and its connection of political system legitimacy on the institution of the judiciary rather than on the systems created for judging—and the legitimacy enhancing normative constraints of judging detached from the institution of the

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<sup>104</sup> This represents an extension of the arguments made with respect to the higher law of the Chinese Constitutional state for which a similar proposal has been advanced. See Larry Catá Backer, *A Constitutional Court for China Within the Chinese Communist Party?: Scientific Development and a Reconsideration of the Institutional Role of the CCP*, 43 SUFFOLK U. L. REV. 593, 596-97 (2010).

judiciary, though also applied to the institution of the judiciary itself. This requires a sensitivity to the normative context in which such an exercise must be undertaken.

In the West, there has always been a detachment between the institution of the judiciary and the role of judging.<sup>105</sup> The common law judiciary, from which the modern institution of the judge was derived in large part, was in its origins just one of many institutions for the settlement of disputes, one that ultimately proved more successful than other systems for meeting the needs of litigants, and of the state under the conditions of English feudalism. Those institutions have been consolidated to some extent, adjusting its structures and methodologies to suit changing historical conditions. But with every consolidation arose new manifestation of judging power outside the institutions of the traditional judge.<sup>106</sup> The consolidation of law and equity in the United States, for example, was implemented even as the administrative state arose, and with it the creation of a large “quasi-judicial” power (notice the way in which Americans are taught to reference these judges—by the very language of the judges themselves in their cases)<sup>107</sup> exercised by hearing officers and the like. But consolidation prevailed through the institution of hierarchy in which the most legitimate and superior institutional manifestation of the judicial power is vested in the institution of the judiciary—that society of judges whose cultures and habits are meant to be autonomous though connected with, the rest of the state apparatus. It is that hierarchy that has permitted the detachment of the judicial function from the judge—precisely because at some point the institution of the judge will pass on the soundness (one way or another) of the actions of inferior administrative hearing officers, arbitrators, or secondary officers with judicial roles (for example bankruptcy court judges). The structure of Article III of the U.S. federal constitution provides the hint—vesting the entirety of the judicial power of the federal apparatus *in courts* and thus consigning all judging undertaken elsewhere as inferior in form and effect.<sup>108</sup>

This is the model mimicked throughout the United States, less so elsewhere in the West, but enough so that a set of ordering premises can be discerned—and taken for granted in speaking with or engaging other systems. First, judging is best done by courts overseen by properly trained judges. Second, these judges must cultivate institutional solidarity with other judges, and thus unified, represent the institution for resolving disputes and “protecting” the law against other public or private institutions that may deploy or apply or interpret “the law” in the course of their own exercise of authority. Third, the connection between the judges, the institution of the judiciary may not be interfered with by other institutions of state. Fourth, within the

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<sup>105</sup> Consider John Ferejohn, *Independent Judges, Dependent Judiciary: Explaining Judicial Independence*, 72 S. CAL. L. REV. 353, 354, 362-63, 381 (1998-1999); CASS SUNSTEIN, *LEGAL REASONING AND POLITICAL CONFLICT* (Oxford, 1996); William M. Landes & Richard A. Posner, *The Independent Judiciary in an Interest-Group Perspective*, 18 J. L. & ECON. 875, 879, 885-86 (1975); Larry Catá Backer, *Retaining Judicial Authority: A Preliminary Inquiry on the Dominion of Judges*, 12 WM. & MARY BILL RTS. J. 117, 118, 124, 178 (2003).

<sup>106</sup> Harold A. Bruff, *Specialized Courts in Administrative Law*, 43 ADMIN. L. REV. 329 (1991).

<sup>107</sup> Ronnie A. Yoder, *The Role of the Administrative Law Judge*, 22 J. NAT'L ASS'N ADMIN. L. JUDGES 321, 327-29 (2002); Richard J. Pierce, Jr., *The Role of the Judiciary in Implementing an Agency Theory of Government*, 64 N.Y.U. L. REV. 1239, 1256 (1989).

<sup>108</sup> U.S. CONST. art. III, § 1.

institutions of the judiciary, all inferior judges owe a duty of obedience and loyalty to judges of superior courts, or better put, to those portions of opinions that are rendered in courts hierarchically superior, to the extent required within the specific judicial culture in which the judicial institution operates. Fifth, judging cannot be detached from the institution of the judiciary and must be exercised by the individual judge, alone or in groups as provided by law or judicial custom. Sixth, others who purport to exercise the power of judging may do so legitimately only to the extent their actions, to some minimum extent (as specified by the judicial institution itself through its own interpretation of its own constitutive powers, its *kompetenz-kompetenz*),<sup>109</sup> are subject to review or conformation by the judiciary. Seventh, only the judiciary, either generally or within specialized tribunals created for that purpose, may interpret the extent, limit and lawful application of governmental power. Eighth, only the judiciary (either generally or through specialized tribunals designated therefore), may interpret and apply authoritatively as against other institutions of states and non-state actors.

But are these premises, all or any of them, absolutely necessary to protect the integrity, such as one wants it, of the judicial process (and not necessarily of a particular judicial institution)? *It is possible to suggest that the answer is no.* For that purpose, one might consider the theoretical arrangement of the judicial authority in China. It is divided in two quite distinct respects. First, the authority to decide a particular dispute is divided from the authority to interpret the law to be applied to that dispute. Second, the authority to hear and decide a particular dispute is itself divided in accordance to the status of the disputants and the character of the dispute. For example, at the 11th Annual General Conference of the European China Law Studies Association (欧洲中国法研究协会).<sup>110</sup> There were three quite interesting discussions that brought home the challenge and possibilities of an assertion of the judicial power detached from the judiciary itself. The issue of the assertion of judicial authority by agencies in the context of the Chinese competition law.<sup>111</sup> Keren Wang spoke to the ambiguous context in which the role and power of a judge is

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<sup>109</sup> The power by an institution to determine the scope and allocation of its own competences, usually a sovereign power of states, but also exercised in some form by any institution with the authority to interpret the extent of its own power. Klaus Dieter Wolf, *Contextualizing Normative Standards for Legitimate Governance Beyond the State*, PARTICIPATORY GOVERNANCE: POLITICAL AND SOCIETAL IMPLICATIONS 35-50 (Jürgen R. Grote, & Bernard Gbikpi, eds., SPRINGER 2002). The issue was particularly well developed in Europe as the Member States of the European Union sight to determine the nature of their relationship to the European Union. See, e.g., Tobias Lock, *Why the European Union is not a State: Some Critical Remarks*, 5 EUR. CONST. L. R. 407, 408-09 (2009). But a powerful variation has been part of the political theory of the United States almost since the founding of the current Republic. *Marbury v. Madison*, 5 U.S. 137, 146-51, 174-78 (1803); *McCulloch v. Maryland*, 17 U.S. 316 (1819). In China one would expect that the ultimate exercise of *kompetenz-kompetenz* would be undertaken under the leadership of the CCP and through the appropriate state institution.

<sup>110</sup> Conference Program: 11th Annual General Conference of the European China Law Studies Association (欧洲中国法研究协会), <http://lcbackerblog.blogspot.com/2016/09/conference-program-11th-annual-general.html>.

<sup>111</sup> This has been nicely discussed in Wendy Ng, *The Independence of Chinese Competition Agencies and the Impact on Competition Enforcement in China*, 4(1) J. ANTITRUST ENFORCEMENT 188 (2016).

understood.<sup>112</sup> And Shaoming Zhu spoke to the exercise of judicial powers of interpretation within the legislative apparatus itself, even in the face of the reform of a vigorous judicial apparatus.<sup>113</sup> These investigations frame a quite different way of approaching the construction of a judicial power, and of the administration of law. It suggests that the review of disputes need not be aggregated within a single institutional authority. A state need not necessarily constitute a single institutional structure (the judiciary) for the purpose of authenticating the actions of judges and other hearing officers with respect to their actions resolving disputes or interpreting law or regulation in the course of resolving disputes. It suggests as well that the function of interpreting law can be separated from the function of applying law to a dispute, and that each can be administered through distinct institutional means. The former authority can be reconstituted as a political activity reserved to the political authorities of the institutionalized state; it represents the application of the generalized power of the political community to refine its reading of law. The latter reconstituted as an administrative mechanism in which the highest forms of integrity and the greatest protection against interference by the political bodies ought to be cultivated. In his 19<sup>th</sup> CPC Congress Report,<sup>114</sup> Xi Jinping was careful to separate the judiciary from the law. For the judiciary, the focus was on judicial reform,<sup>115</sup> and judicial accountability, “so that the people can see in every judicial case that justice is served.”<sup>116</sup> For law, the CPC itself was to lead the nation in the development of a “socialist culture of rule of law.”<sup>117</sup> The project of legal construction and the project

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<sup>112</sup> Keren Wang, Pennsylvania State University, *Fractured Legal Theology: Tension between the Socialist Doxa and Confusion Pistis in Chinese Judicial Reform Discourse, Judicial Reform and the Structures of Socialist Rule of Law. Persistently Emancipating the Mind* (Sept. 23, 2016) (notes on file with author). Wang notes a key underlying difficulty in Chinese legal reform centered on the potentially significant schism between Chinese Socialist legal doxa, which operates within the formal domains of the judge and the state, and the internalized system of Chinese societal beliefs still rooted in cultural Confucian principles.

<sup>113</sup> Shaoming Zhu, *Judicial Reform and Legislative Reform: Conflicts and Mutual Promotion, Judicial Reform and the Structures of Socialist Rule of Law. Persistently Emancipating the Mind* (Sept. 23, 2016) (notes on file with author). She noted the tension inherent in the current system in which judicial construction is both sometimes legalized through statutory reform and sometimes operates in tension with statute. See also Jeremy Daum, *The Curious Case of China's Guiding Cases System*, CHINA LAW TRANSLATE (Feb. 21, 2017), available at <http://www.chinalawtranslate.com/the-curious-case-of-chinas-guiding-cases-system/?lang=en>.

<sup>114</sup> Xi Jinping, *Secure a Decisive Victory in Building a Moderately Prosperous Society in All Respects and Strive for the Great Success of Socialism with Chinese Characteristics for a New Era, Report Delivered at the 19th National Congress of the Communist Party of China 19*, (Oct. 18, 2017), available at [http://www.xinhuanet.com/english/download/Xi\\_Jinping%27s\\_report\\_at\\_19th\\_CPC\\_National\\_Congress.pdf](http://www.xinhuanet.com/english/download/Xi_Jinping%27s_report_at_19th_CPC_National_Congress.pdf) (He explains, “We must further the reform of the judicial system, and strengthen rule of law awareness among all our people while also enhancing their moral integrity.”).

<sup>115</sup> *Id.* at 3.

<sup>116</sup> *Id.* at 34 (“We will carry out comprehensive and integrated reform of the judicial system and enforce judicial accountability in all respects”). The Communist Party “will establish an authoritative, efficient oversight system with complete coverage under the Party’s unified command” that includes judicial oversight. *Id.* at 62.

<sup>117</sup> *Id.* at 34 (“Every Party organization and every Party member must take the lead in respecting, learning about, observing, and applying the law. No organization or individual has the power to overstep the Constitution or the law; and no one is allowed in any way to override the law with his or her own

of judicial reform are not understood as identical, and their intersection must be guided by the political character of the state rather than by any fundamental characteristic of the judiciary as an institution autonomous of either state or Party. Perhaps in this sense it is possible to understand the implications of Xi's allocation to the CPC of the task to "strengthen public participation and rule of law in social governance, and make such governance smarter and more specialized."<sup>118</sup>

On the one hand, one could ask—what does any of this have to do with judicial reform? But *that question could only be asked by one oblivious to the power of the assumptions of judging* described above. In the Chinese context, the *better question* might be to consider the need either for a unitary judiciary or for a unitary legal sphere. Within China, then, the grounding question should be the one that is never asked in the West—the extent to which the judge and the judicial authority *must* be exercised exclusively or completely by or through the institution of the judiciary and by judges. In other words, does the political system suggest the possibility a different approach to the fracture of judicial authority consist with its own political logic. That poses the further question—must judicial modernization necessary require Westernization?<sup>119</sup> The answer within the Chinese context must be no—the fracture between the political-legislative exercise of legal interpretation (especially in a Chinese civil law context)

That fracture would see in the judges a mechanism for the resolution of disputes among private parties. But it might strip away from that institutional apparatus all authority of interpretation of law (to be given to a legislative authority, a separate political body charged exclusively with issues of interpretation in the context of disputes or some other body perhaps in the CCP itself). It might also strip away from the judge—and the institution of the judiciary all authority over disputes involving the state itself. The issue of relief from administrative excess, wrong decision making, corruption and abuse of power might itself be treated as executive in character and assigned to another and distinct competent authority. Within the Chinese context, and with the close connection that some of these issues might have with breaches by CCP cadres of their paramount duty to the CCP and its Basic Line, the institution might combine both CCP disciplinary and state disciplinary structures. And lastly, it might create, within the administrative strictures of the state structures of administrative hearing that can exist as judicial decision-making independent of a judiciary. In each of these cases, though, the one thing that must be respected—the lynchpin of judging, is the independence of the judge to decide the dispute before her on the basis of whatever received law and interpretation is demanded by the system. That judicial independence in the face of actual decision making in a live dispute, might be the only point of connection among those who might exercise the judicial authority in distinct and partial ways. Coordination and compatibility with western institutional forms of deploying the judicial power, and matters of legitimacy will then follow.

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orders, place his or her authority above the law, violate the law for personal gain, or abuse the law.”). See also *Id.* at 3, 17, 25, and 44.

<sup>118</sup> *Id.* at 44.

<sup>119</sup> YUWEN LI, *THE JUDICIAL SYSTEM AND REFORM IN POST-MAO CHINA: STUMBLING TOWARDS JUSTICE* 245-47 (Routledge 2014).

The result is medieval in the sense of the proliferation of multiple venues and institutions for judging—for exercising the judicial craft.<sup>120</sup> What is suggested as both possible and likely within a Marxist-Leninist state apparatus true to its theoretical foundations<sup>121</sup> is institutional multi-hierarchies in judging. The result is anarchic from an institutional level. But it has several advantages for a Marxist-Leninist system committed to the construction of socialist rule of law. First, it detaches law from the judiciary. There is no special relationship between law and the judiciary in a Marxist-Leninist system—other than the requirement that the judge apply the law, and that the law reflect the leadership and guidance of the vanguard and be appropriately drafted by the state organs with legislative authority. Indeed, the only special relationship or necessary connection ought to be between the vanguard party which guards the integrity of lawmaking as a whole, and the law as an expression of the protection of society and its forward movement along the objectives for which the vanguard has been constituted and empowered. This is inimical to Western thinking, but this is not a Western democratic polity. Second, that detachment permits a management of the administrative aspects of judging without the contradiction of also dealing with a latent political authority in the actions of judges. In other words, to reduce the judge—in all her variations—to aspects of administrative roles, to strip the judge of her relationship as curator of law (and thus with a political authority that might rival the Communist Party itself in implementation and interpretation), permits the advance of judicial reform in a manageable and attainable way. It does this by making it easier to manage corruption (without the complexities of defenses based on arguments that prosecutions are based on retaliation for exercise of political authority in judging or interpreting law), and to manage the craft of judging through assessment that should itself be free of politics. Third, it frees the development of law—statutory, administrative and Party law, within the context of its own politics. And it ensures that those with political authority are made responsible for their failures of leadership in law making, law enforcement and the interpretation of law. It is to the CCP itself that the responsibility belongs, and it is necessary to ensure that the CCP itself embraces that responsibility directly—by becoming directly accountable for its operation. That accountability should take two forms, indirect with respect to the disciplining of judges as administrative officials, and direct in the construction and interpretation of uniform law applied uniformly and fairly to the masses.

But it also suggests that this separation might be itself fragmented among different institutional mechanism, functionally distinguished by the subject matter of the dispute or the identity of the parties. Here one can at least touch on the great "elephant in the room" (an obvious element of judicial reform that goes unaddressed)—the problem of the reform of the judicial authority and judicial institutions that deal with actions involving the state. The thrust of judicial reform has tended to focus on two distinct but related forms of disputes—those between private parties both of

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<sup>120</sup> ARTHUR R. HOGUE, *ORIGINS OF THE COMMON LAW* (Liberty Fund 1985) (on proliferation in pre-modern England).

<sup>121</sup> See Larry Catá Backer, *Introduction: On a Constitutional Theory for China – From the General Program of the Chinese Communist Party to Political Theory*, *LAW AT THE END OF THE DAY* (Feb. 14, 2015), <http://lbackerblog.blogspot.com/2015/02/on-constitutional-theory-for-china-from.html> (considering the Constitution of the Communist Party of China, General Program)

whom are Chinese, and those between parties at least one of whom is not Chinese. More importantly, it remains problematic when an instrumentality of the state—a state-owned enterprise, for example, is involved, or where SOEs and local officials collude to avoid their respective obligations to the local people they ought to serve. It is in this context that China might most usefully draw on elements of judging from the West, though it bears repeating that such "inspiration" might touch on techniques rather than ideology. But it is in the matter of disputes involving officials—because their decisions violated law, or because of corruption or other failures, that the thrust of judicial reform remains substantially silent. And yet it is in this context that reform is most needed. The focus of that reform might not lead one either to the judiciary as an institution or to law. The CCP Basic Line, for example, might suggest that where the conduct of officials is involved specialized procedures ought to be created within specialized bodies. There is a precedent for this sort of status specific fracture—the hearing structures of the Central Commission for Disciplinary Inspection.<sup>122</sup> That model lacks a necessary connection between the function of accountability and the remedial obligations of the state toward its masses. That omission could be addressed through the creation of specialized bureaus that would serve both to discipline officials and to also provide remedies for those injured by official misconduct. That, in turn, would require the state, under the leadership of the CCP to develop a mechanism for assessing damage and a procuratorate of trusted officials to enforce the state's paramount duty to ensure that officials, in their conduct toward the people, exercise the care that their responsibilities demand.

The object of this essay is not to map out its operationalization. It is, however, to suggest that all roads of judicial reform that retain a fidelity to the highest expression of the ideology of the state must lead, inevitably to the understanding that the courts may not assert the political role of interpretation or glossing law, and that this function must inevitably derive from and be overseen by the only institution with gubernaculum in jurisdictio in China—the CCP. It may be time, though, to start from first principles in the approach to the analysis of the construction of a judicial power in China and its alignment to the state apparatus. Clearly the fundamental objectives of justice according to law, predictably and concisely applied ought to guide the analysis. But the normative foundation does not necessarily dictate a particulate institutional result and certainly not a singular institutional design. It is to those matters that Chinese efforts at judicial reform ought to be directed. Coordination and compatibility with western institutional forms of deploying the judicial power, and matters of legitimacy will then follow.

#### CONCLUSION

What is the scope and nature of judicial reform? To what extent does borrowing from Western models also suggest an embrace of the underlying ideologies that

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<sup>122</sup> Guo Yong, *The Evolvement of the Chinese Communist Party Discipline Inspection Commission in the Reform Era*, 12 CHINA REV. 1, 2-8, 16-21 (2012); see also David Gitter, *Chinese Communist Party Education: Now New and Improved: The CCP is using a two-pronged approach to ensure discipline among its cadres*, THE DIPLOMAT (May 13, 2016), <http://thediplomat.com/2016/05/chinese-communist-party-education-now-new-and-improved/>.

frame those models? The issue of judicial reform, and of the working style of the judge, has been at the forefront recently in China. Both national and foreign scholars, politicians, civil society elements and the like have weighed in on the issue. Each of them have their own axes to grind. Foreigners are looking for convergence with their own standards, ideologies, and practices—however contested these may be in their own home states. The national debate on judicial reform reflects playing out of more complex politics involving not merely the technical issues of judicial efficiency and operations, but also touching on the character of the judge, the judicial role, the relationship between judge and law, and the role of law within a Marxist-Leninist political framework. These issues remain at the center of the debate in China. “People's Courts at all levels must disregard erroneous western notions, including constitutional democracy and separation of powers, Chief Justice Zhou Qiang was reported by the news agency as saying at a Supreme People's Court meeting on Saturday.”<sup>123</sup>

This essay has suggested an approach to an answer. That approach is grounded in the importance of the underlying ideology of models of judging which are quite distinct among Western states and in the Socialist Law system being developed in China. If one is to understand the suitability of legal or administrative transplants, or their effects (intended or unintended) then it is necessary to understand the effects of ideology on the construction of judging systems and the need for reforms to retain a fidelity to the principles of the systems in which they are embedded.<sup>124</sup> The usual caveats apply here and generally when discussing Chinese institutions with foreigners: the reality of judicial action “on the ground” and its theory (or idealized forms) may be quite distinct, the level of corruption may make theoretical constructs fantasy, the disciplinary element where the CCP might be the worst offender when it comes to CCP cadres failing to follow their own Basic CCP Line in relation to the deployment and operation of a judicial authority (the problem if interfering with judicial administration). But these caveats need not necessarily concede the fundamental points of a theory of a detachment of the judge from the judicial function.

It is a commonplace in the West, whether in Common Law or Civil Law states, that the integrity of the judiciary depends on their authority to interpret law and to apply that interpretation to individual cases and the litigants that appear before the courts.<sup>125</sup> That presumption, however, embeds premises about the organization of political and administrative authority that may be incompatible with those of states developing Socialist Rule of Law structures within Party-State systems. In Common law states those deep presumptions touch on the disciplinary role of judicial opinions

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<sup>123</sup> *China's Top Judge Warns Courts on Judicial Independence*, REUTERS (Jan. 15, 2017, 1:56 AM), <http://www.reuters.com/article/us-china-policy-law-idUSKBN14Z07B>.

<sup>124</sup> See ALAN WATSON, *LEGAL TRANSPLANTS: AN APPROACH TO COMPARATIVE LAW* 10-30 (U. Ga. Press 1974) (for the perils and promise of legal transplantation and the importance of fidelity to contextually embedded normative orders); Pierre Legrand, *The Impossibility of Legal Transplants*, 4 *MAASTRICHT J. EUR. & COMP. L.* 111, 120 (1997); see also Donald C. Clarke, *Lost in Translation? Corporate Legal Transplants in China*, *GW LAW FACULTY PUBLICATIONS & OTHER WORKS*. [http://scholarship.law.gwu.edu/faculty\\_publications/1068](http://scholarship.law.gwu.edu/faculty_publications/1068) (for the Chinese context).

<sup>125</sup> *Cf.*, JOHN MERRYMAN, DAVID S. CLARK & JOHN O. HALEY, *THE CIVIL LAW TRADITION: EUROPE, LATIN AMERICA AND EAST ASIA* 705-98 (Mich., 1994).

as a constraint on judicial interpretation. In civil law states that discipline arises from the constraining principles of the legal codes themselves. In both the legislatures serve as the ultimate check in a complex dialogue with courts in three respects. First, judges serve a political role in their relation to law. Second, cases themselves serve an important political role as well. Third, courts begin to serve as the place where societal narratives are forged and popular expression is constructed and applied.

In Socialist rule of law systems, the disciplinary systems are quite different and ought to produce a different relationship between courts, law, and the cases they are bound to apply fairly and consistently under law.<sup>126</sup> This essay considered the way that the logic and grounding principles of Chinese Marxist Leninism may provide guidance in the construction of a judicial enterprise that is both true to its organizational logic and which enhances the authority of judges to serve litigants fairly. It suggests the points of compatibility and incompatibility in the ideologies of these distinct systems of judging and what it may mean for judicial reform in China. That consideration, in turn is based on a fundamental difference, in Socialist Rule of Law systems, between the authority to interpret law and the authority to apply law to an individual case. For Chinese judicial reform, it is in the perfectibility of the judge that lies the perfectibility of law that in turn ensures the perfectibility of the judge. Part II considered in very broad strokes the relationship between the judge and law in the West. Part III then turned to Chinese reforms, reforms touching on the relationship between the judge and the law, and the evolution of normative structures within which one can speak to judicial independence. Part IV then considered the project of judicial reform from the perspective of the grounding ideology of the Chinese state. From that fundamental distinction, this study pointed to a Socialist approach to the judicial function compatible with its own logic and legitimacy enhancing under global consensus principles for a well-organized and functioning judiciary. This is an approach that increasingly can be understood as fundamental to the emerging socialist culture of rule of law and its constitutionalism, the construction of which is an important element of China's "New Era" political line after the 19<sup>th</sup> CPC Congress of 2017.

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<sup>126</sup> See generally, Larry Catá Backer, *Jiang Shigong 强世功 on "Written and Unwritten Constitutions" and Their Relevance to Chinese Constitutionalism*, 40 MODERN CHINA 119 (2014).





THE TRANSATLANTIC TRADE AND  
INVESTMENT PARTNERSHIP:  
A THREAT TO THE INTERNATIONAL TRADING  
SYSTEM OR THE  
PANACEA FOR THE ECONOMIC PREDICAMENTS  
FACED BY THE EU AND THE USA?

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*Abstract*

*In recent years the Transatlantic Trade and Investment Partnership (TTIP) has received a considerable amount of attention, in part due to the secretive nature of the EU-USA trade deal talks. Conflicting views have been expressed. Some argue that TTIP is a threat to the international trading system while others believe that it is an economic panacea that is long overdue.*

*This article explores the various ways in which TTIP will impact the European Union (EU) and the United States of America (USA). It provides an overview of TTIP and the background to the trade talks, particularly in light of the 2008 financial crises. It then assesses the impact of TTIP on the EU and the USA in terms of the claimed benefits and drawbacks gleaned from available research. The impact of the TTIP on key sectors of the economy such as public health, agriculture, labour and enterprise, and issues relating to specific chapters dealing with regulatory cooperation, the dispute settlement mechanism and public procurement are also analysed. The impact of the trade deal on the international trading system and developing countries is also discussed. Reforms aimed at improving both the negotiation process and the agreement itself are discussed throughout the article.*

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## INTRODUCTION

The Obama administration proposed a series of trade-related initiatives to boost the American economy in the aftermath of the 2008 financial crisis.<sup>1</sup> The Transatlantic Trade and Investment Partnership (TTIP) along with the Trans Pacific Partnership (TPP), which is a trade deal between the USA and eleven Pacific Rim countries,<sup>2</sup> are the two major initiatives that aim to boost the economy and employment rate across the Atlantic and Pacific. The EU similarly suffered from the crisis and some EU member states such as Greece and Portugal are still struggling.<sup>3</sup> The EU has consequently intensified its relationship with the USA, especially on trade-related initiatives that have the potential to be mutually beneficial.<sup>4</sup> The combined effect of the two aforementioned trade deals has the potential to substantially improve trade facilitation and market access for the EU and the USA.<sup>5</sup>

There are two main drivers behind the transatlantic trade talks. The first and most important one is that the leaders of the USA and the EU fully acknowledge that it is time to make urgent moves in terms of trade initiatives in opening transatlantic markets in order to ensure a position of power in the increasingly competitive global trading system. The rise of new powers such as China and India in the sphere of international trade coupled with recent financial tumult has convinced EU and USA leaders that it is high time to address the situation before they lose the ability to maintain high standards in the fields of labour, public health and consumer protection in the near future. The second driver is the perpetual changing nature of international trade negotiations. The leaders in the EU and the USA believe that the liberalisation of multilateral trade, i.e., the definitive elimination of tariffs and regulatory barriers is the answer for sustained economic growth.<sup>6</sup>

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<sup>1</sup> John Marshall, *The Financial Crisis in the US: Key Events, Causes and Responses* 3 (House of Commons Library, Working Paper No. 09/34, 2009), [http://www.voltairenet.org/IMG/pdf/US\\_Financial\\_Crisis.pdf](http://www.voltairenet.org/IMG/pdf/US_Financial_Crisis.pdf).

<sup>2</sup> *Overview of the Trans Pacific Partnership*, OFFICE OF THE U.S. TRADE REPRESENTATIVE, <https://ustr.gov/tpp/overview-of-the-TPP> [<https://web.archive.org/web/20161022052319/https://ustr.gov/tpp/overview-of-the-TPP>] (last visited Oct. 21, 2017).

<sup>3</sup> Antonio Garcia Pascual & Piero Ghezzi, *The Greek Crisis: Causes and Consequences* 1-3 (Ctr. for Econ. Studies and IFO Inst., Working Paper No. 3663, 2011), [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1968873](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1968873).

<sup>4</sup> Madalina Laura Cuciurianu, *The Impact of Transatlantic Trade and Investment Partnership on European Union: A Solution for the European Economic Crisis*, 9 RES. & SCI. TODAY 89, 94 (2015).

<sup>5</sup> Michelle Egan, *Is TTIP Really that Different?*, in *THE TTIP: THE TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP BETWEEN THE EUROPEAN UNION AND THE UNITED STATES* 19, 19-21 (Joaquín Roy & Roberto Domínguez eds., 2014).

<sup>6</sup> Daniel S. Hamilton & Jacques Pelkmans, *Rule-Makers or Rule-Takers? An Introduction to TTIP*, in *RULE-MAKERS OR RULE-TAKERS? EXPLORING THE TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP* 1, 2-4 (Daniel S. Hamilton & Jacques Pelkmans eds., 2015).

The genesis of the TTIP dates back to November 2011 during an EU-USA Summit meeting in Washington.<sup>7</sup> President Obama, former European Commission President Jose Barroso, and former European Council President Herman Von Rompuy instructed the Transatlantic Economic Council (TEC) to set-up a High Level Working Group on Jobs and Growth (HLWG). The former European Trade Commissioner Karel De Gucht and the former US Trade Representative Ron Kirk were selected to chair the Working Group. The main task of the HLWG was to identify measures and policies that would boost investment and trade between the EU and the USA in order to create more jobs and enable the economic growth of both areas.<sup>8</sup> In its final report, the HLWG emphasised the necessity of an ambitious EU-USA trade deal that would encompass a broad range of issues, from investment and bilateral trade to regulatory cooperation.<sup>9</sup>

As a result of the recommendations stated in the HLWG final report, negotiations on TTIP officially began in June 2013, when President Obama, Van Rompuy and Barroso announced that the EU and the USA, two of the world's largest economic units, had the firm intention to successfully negotiate and conclude a transatlantic trade partnership.<sup>10</sup> The EU and the USA represent nearly half of the world's gross domestic product (GDP) and an impressive market of 800 million consumers.<sup>11</sup> Added to that, they hold 30% of the world's trade and also trade goods and services bilaterally on a daily basis worth \$2.7 billion which in turn promotes economic growth and sustains millions of jobs in both economies.<sup>12</sup>

TTIP has been presented as a solution to most of the contemporary economic predicaments faced by the negotiating partners.<sup>13</sup> According to the Office of the United States Trade Representative, the rationale behind the EU-USA trade deal is to expand and facilitate trade and investment between the EU and the USA. The agreement is supposed to boost the economy and increase employment rates for both negotiating partners.<sup>14</sup> TTIP also aims to reduce tariff barriers in order to make the EU and the USA more competitive at an international level and facilitate both economies to deal with global issues. However, critics argue that the

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<sup>7</sup> *EU-US Summit, Washington 28 November 2011*, EUROPEAN UNION EXTERNAL ACTION [http://eeas.europa.eu/us/sum11\\_11/index\\_en](http://eeas.europa.eu/us/sum11_11/index_en) [[https://web.archive.org/web/20160322100202/http://eeas.europa.eu/us/sum11\\_11/index\\_en.htm](https://web.archive.org/web/20160322100202/http://eeas.europa.eu/us/sum11_11/index_en.htm)] (last visited Oct. 21, 2017).

<sup>8</sup> U.S.-EU High Level Working Group on Jobs and Growth, 77 Fed. Reg. 1778 (Jan. 11, 2012).

<sup>9</sup> *United States-European Union High Level Working Group on Jobs and Growth, Final Report* (Feb. 11, 2013), [http://trade.ec.europa.eu/doclib/docs/2013/february/tradoc\\_150519.pdf](http://trade.ec.europa.eu/doclib/docs/2013/february/tradoc_150519.pdf).

<sup>10</sup> *T-TIP Issue-by-Issue Information Center*, OFFICE OF THE U.S. TRADE REPRESENTATIVE, <https://ustr.gov/trade-agreements/free-trade-agreements/transatlantic-trade-and-investment-partnership-t-tip/t-tip> (last visited Oct. 21, 2017).

<sup>11</sup> Elfriede Bierbrauer, *The Transatlantic Trade and Investment Partnership (TTIP): The Sluggish State of Negotiations* 5 (2015), [http://www.europarl.europa.eu/RegData/etudes/IDAN/2015/549074/EXPO\\_IDA\(2015\)549074\\_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/IDAN/2015/549074/EXPO_IDA(2015)549074_EN.pdf).

<sup>12</sup> UNITED STATES-EUROPEAN UNION HIGH LEVEL WORKING GROUP ON JOBS AND GROWTH FINAL REPORT, OFFICE OF THE U.S. TRADE REPRESENTATIVE (Feb. 11, 2013), [http://trade.ec.europa.eu/doclib/docs/2013/february/tradoc\\_150519.pdf](http://trade.ec.europa.eu/doclib/docs/2013/february/tradoc_150519.pdf).

<sup>13</sup> THE TRANSATLANTIC COLOSSUS: GLOBAL CONTRIBUTIONS TO BROADEN THE DEBATE ON THE EU-US FREE TRADE AGREEMENT 4-5 (Daniel Cardoso et al. eds., 2014).

<sup>14</sup> OFFICE OF THE U.S. TRADE REPRESENTATIVE, *supra* note 12.

aforementioned promises are not clearly explained and are supported by only one study provided by the Centre for Economic Policy Research (CEPR),<sup>15</sup> a London based think tank.<sup>16</sup>

During the 2013 State of the Union Address, President Obama stated that the reason why his administration took the initiative to launch negotiations for a bilateral trade and investment agreement with the EU was because free and equitable trade across the Atlantic would ensure jobs for millions of Americans.<sup>17</sup> Through TTIP, the USA and the EU intend to deal with domestic regulations in a completely novel way.<sup>18</sup> Prior to TTIP, trade negotiations usually dealt with domestic regulations as a trade barrier in a narrow way. This time the negotiating partners want to make the reduction of regulatory barriers a priority.<sup>19</sup> President Obama stated that TTIP talks will aim to make regulations between the USA and the EU more uniform.<sup>20</sup> TTIP is a colossal project and if successfully concluded it will be the world's largest free trade area ever established.<sup>21</sup>

The debate around TTIP involves various issues, the most dominant are: agriculture and food, public health, labour and enterprise, dispute settlement, regulatory cooperation and public procurement. The negotiating partners claim that TTIP will substantially improve the aforementioned issues.<sup>22</sup> Conversely, it is feared that TTIP could be a threat<sup>23</sup> to sectors such as public health and agriculture.<sup>24</sup> The new dispute settlement mechanism proposed in the agreement, which bears a lot of resemblance to the highly controversial investor-state dispute settlement (ISDS) mechanism, has also been the subject of debate.<sup>25</sup>

Since the announcement of the trade partnership, there have been an unprecedented number of protests across Europe.<sup>26</sup> This controversy can be

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<sup>15</sup> Joseph Francois et al., *Reducing Transatlantic Barriers to Trade and Investment: An Economic Assessment* (2013), [http://trade.ec.europa.eu/doclib/docs/2013/march/tradoc\\_150737.pdf](http://trade.ec.europa.eu/doclib/docs/2013/march/tradoc_150737.pdf).

<sup>16</sup> Cardoso, et al., *supra* note 13.

<sup>17</sup> Barack Obama, President of the U.S., State of the Union Address (Feb. 12, 2016).

<sup>18</sup> See generally Marise Cremona, *Negotiating the Transatlantic Trade and Investment Partnership (TTIP)*, 52 COMMON MKT. L. REV. 352 (2015).

<sup>19</sup> Simon Lester & Inu Barbee, *The Challenge of Cooperation: Regulatory Trade Barriers in the Transatlantic Trade and Investment Partnership*, 16 J. INT. ECON. L. 847, 847-48 (2013).

<sup>20</sup> Barack Obama, President of the U.S., Remarks by the President at Meeting with the President's Export Council (Feb. 13, 2013).

<sup>21</sup> Cardoso, et al., *supra* note 13.

<sup>22</sup> OFFICE OF THE U.S. TRADE REPRESENTATIVE, *supra* note 10.

<sup>23</sup> See generally Holly Jarman, *Public Health and the Transatlantic Trade and Investment Partnership*, 24 EUR. J. PUB. HEALTH 181 (2014).

<sup>24</sup> Phillip Inman, *Prospect of TTIP Already Undermining EU Food Standards, Say Campaigners*, THE GUARDIAN (Oct. 17, 2015), <http://www.theguardian.com/business/2015/oct/18/prospect-ttip-deal-undermining-eu-food-standards-gmos>.

<sup>25</sup> Joseph H.H. Weiler, *Guest Editorial: Ten Years of ESIL – Reflections; European Hypocrisy: TTIP and ISDS; Masthead Changes; Roll of Honour; In this Issue; Christmas Reading? Christmas Gifts? Some Suggestions from the Editor-in-Chief*, 25 EUR. J. INT'L L. 961, 964 (2014).

<sup>26</sup> Graham Vanbergen, *Mass European Protest Against TTIP Corporate Takeover: EU Commission Sanctions "Revolution Against Law"*, GLOBAL RESEARCH (Nov. 5, 2015), <http://www.globalresearch.ca/mass-european-protest-against-ttip-corporate-takeover-eu-commission-sanctions-revolution-against-law/5486736>.

attributed to the secretive nature of TTIP negotiations<sup>27</sup> and the allegations that TTIP is a threat to both democracy and the sovereignty of states to the benefit of corporations.<sup>28</sup> Conversely, proponents argue that such contentions are not reflective of the impact of TTIP, which will be beneficial to both the EU and the USA.<sup>29</sup>

TTIP is likely to reshape the multilateral trading system, and in the process, the World Trade Organisation (WTO).<sup>30</sup> Opinions on this matter diverge. Some believe that TTIP will not only benefit the EU and the USA but also developing countries,<sup>31</sup> while others are more sceptical and argue that TTIP will surpass the WTO thereby weakening its influence.<sup>32</sup> Critics also contend that TTIP will negatively impact developing countries<sup>33</sup>, believing that one of the main reasons motivating TTIP is to deter the rising influence of Brazil, Russia, India, China and South Africa (BRICS).<sup>34</sup>

The growing speculation about TTIP is partly because the agreement is still being negotiated. The negotiations must be completed and the trade deal must show the world its worth before a judgement can be made. Consequently, this article analyses the impact of specific chapters of TTIP and its effect on specific sectors if it were implemented today.<sup>35</sup> It assesses the impact of TTIP on the EU and the USA in terms of the claimed benefits and drawbacks gleaned from available research. The impact of the TTIP on key sectors of the economy such as public health, agriculture, labour and enterprise, and issues relating to specific chapters dealing with regulatory cooperation, the dispute settlement mechanism and public procurement are also analysed. These issues were chosen as they are the most important and the most difficult issues to negotiate.<sup>36</sup> The impact of the trade deal

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<sup>27</sup> Tara Donaldson, *EU Calls for Greater Transparency in TTIP Talks*, SOURCING JOURNAL (July 17, 2014), <https://sourcingjournalonline.com/eu-calls-greater-transparency-ttip-talks/>.

<sup>28</sup> Gabriel Siles-Brügge & Nicolette Butler, *Regulatory Chill? Why TTIP Could Inhibit Governments from Regulating in the Public Interest*, LONDON SCH. OF ECON.: EUROPP BLOG (Jun. 9, 2015), <http://bit.ly/1JBOXpg>.

<sup>29</sup> Mark O'Mahoney, *We Believe Fears About the TTIP Are Unfounded – We Need to Break Down Barriers to Business*, THE JOURNAL.IE (Jun. 11, 2015), <http://www.thejournal.ie/readme/fears-about-the-ttip-are-unfounded-2153881-Jun2015/>.

<sup>30</sup> See generally Gary Clyde Hufbauer & Cathleen Cimino-Isaacs, *How Will TPP and TTIP Change the WTO System?*, 18 J. INT'L ECON. L. 681 (2015).

<sup>31</sup> Deborah Elms, *Why Asia's TTIP Fears Are Groundless*, FRIENDS OF EUROPE (July 14, 2015), <http://europesworld.org/2015/07/14/asias-ttip-fears-groundless/#.VkSXbHYrK00>.

<sup>32</sup> CATALYST? TTIP'S IMPACT ON THE REST 2, 14, 16 (Mehmet Sait Akman, et al. eds., 2015) (ebook).

<sup>33</sup> Franza Drechsel & Ska Keller, *The EU-US Free Trade Agreement: Bad Prospects for the Global South*, GREEN EUR. J. (July 24, 2013), <http://www.greeneuropeanjournal.eu/the-eu-us-free-trade-agreement-bad-prospects-for-the-global-south/>.

<sup>34</sup> Michelle Offik, *Doha, the BRICS, and Debt are the Main Motives for TTIP*, ATLANTIC COMMUNITY (Nov. 25, 2014), <http://www.atlantic-community.org/-/doha-the-brics-and-debt-are-the-main-motives-for-ttip>.

<sup>35</sup> Research completed on 15 October 2016.

<sup>36</sup> Tyson Barker & Garrett Workman, *The Transatlantic Trade and Investment Partnership: Ambitious but Achievable: A Stakeholder Survey and Three Scenarios 5* (Atlantic Council & Bertelsmann Foundation, 2013), [http://www.bfna.org/sites/default/files/TTIPReport\\_web.pdf](http://www.bfna.org/sites/default/files/TTIPReport_web.pdf).

on the international trading system and developing countries is also discussed.<sup>37</sup> Recommendations aimed at improving both the negotiation process and the agreement itself are discussed throughout the article.

### I. THE IMPACT OF TTIP ON THE EU AND USA

As mentioned above, while TTIP is presented by proponents as the panacea for the economic challenges faced by the EU and the USA, conflicting opinions have been expressed as to its likely impact. While proponents believe it will solve the economic issues faced by the EU and the USA,<sup>38</sup> concerns have been expressed about the negative impact it could have on the EU, the USA<sup>39</sup> and the rest of the world, especially on developing countries.<sup>40</sup> Both camps point to empirical research to support their positions. For example, the authors of the CEPR study believe that once TTIP is implemented it will generate an estimated €68-120 billion for the EU and €50-95 billion for the USA.<sup>41</sup> They assert that the economic gains brought by TTIP would represent an increase of 0.5% for the EU's GDP and 0.4% for the USA's GDP by 2027.<sup>42</sup> The study also points out that the reduction of non-tariff barriers (NTBs) is the main factor that will allow the aforementioned economic gains. According to the authors, nearly 80% of the predicted gains come from the reduction of costs imposed by unnecessary regulations and bureaucracy, as well as from loosening restrictions on trade in services and government procurement.<sup>43</sup>

It is contended that TTIP will bolster trade across the Atlantic by increasing EU exports to the USA by 28%, which roughly represents goods and services amounting to €187 billion and USA exports to the EU will also be subject to an increase of €159 billion. In addition, supporters of TTIP claim that the overall total exports would most probably increase by 6% in the EU and 8% in the USA and that the EU will experience a significant boost in terms of exports outside the single market, especially in goods such as metal, motor vehicles and processed foods. Moreover, it is argued that the implementation of TTIP will be beneficial for both skilled and less skilled workers' remunerations as both will increase by approximately 0.5% and that the agricultural, fisheries and forestry sectors will experience a slight increase in output of 0.06%.<sup>44</sup> Furthermore, in relation to the impact of TTIP on other countries, proponents of the trade agreement affirm that TTIP would positively impact trade and income in many other countries outside the EU and the USA. It is believed that the trade deal would benefit the EU's and the USA's trade partners by increasing their GDP up to €100 billion. Advocates of the trade agreement point out that the GDP of high-income Organisation for Economic

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<sup>37</sup> Hufbauer & Cimino-Isaacs, *supra* note 30, at 679.

<sup>38</sup> Francois, et al., *supra* note 15, at 1-3.

<sup>39</sup> Hamilton & Pelkmans, *supra* note 5, at 244-46.

<sup>40</sup> Mehmet Sait Akman et al., *supra* note 31, at 28-29.

<sup>41</sup> Francois, et al., *supra* note 15, at 95.

<sup>42</sup> *Id.* at 33-36.

<sup>43</sup> *Id.* at vii.

<sup>44</sup> *Id.* at 3, 38-40, 60, 71-72.

Co-operation and Development (OECD) economies would collectively experience an increase of €36 billion and the GDP of low-income countries would experience a €2.4 billion increase.<sup>45</sup>

The picture painted by the supporters of TTIP is a very optimistic one and suggests that the trade agreement is the answer to the world's contemporary economic issues. However, others do not share this point of view and characterise the arguments and statistics of the supporters of TTIP as inaccurate,<sup>46</sup> unrealistic<sup>47</sup> and overly optimistic.<sup>48</sup> For instance, Siles-Brügge and De Ville argue that the CEPR's predictions are based on the assumption that 100% of tariffs, 25% of goods and services NTBs and 50% of public procurement restrictions will be quashed.<sup>49</sup> According to the authors, this prediction is virtually impossible to implement in a real-life scenario for two main reasons. The first reason being the fact that the European Commission, in a report,<sup>50</sup> stated that only 50% of NTBs are 'actionable' i.e. NTBs that can legally be eliminated.<sup>51</sup> Siles-Brügge and De Ville assert that TTIP would have to dismantle 50% rather than only 25% of NTBs, which according to them is not an easy task.<sup>52</sup> The second reason is that in order for the claimed benefits to be implemented in a real life scenario, all sectors of the economy must be liberalised from NTBs as the interlinking of sectors has a significant effect on the overall results.<sup>53</sup> Therefore, unless liberalisation is applied to all sectors, the economic benefits from TTIP are most probably going to be significantly smaller than predicted by the CEPR study.<sup>54</sup>

Myant and O'Brien also adopt a less optimistic view than proponents of TTIP. The authors analysed the most promising results of the CEPR study, pointing out that it was commissioned by the European Commission to showcase the alleged economic benefits of TTIP.<sup>55</sup> They believe that the 28% increase in goods and services exported from the EU to the USA and the 5.9% increase in exports to the

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<sup>45</sup> *Id.* at 96.

<sup>46</sup> Martin Myant, *TTIP: Exaggerated Benefits and Shaky Estimations*, ATLANTIC COMMUNITY (Oct. 24, 2014), <http://www.atlantic-community.org/-/ttip-exaggerated-benefits-and-shaky-estimations>.

<sup>47</sup> Dean Baker, *Why Is It So Acceptable to Lie to Promote Trade Deals?*, CTR. FOR ECON. & POLICY RESEARCH: BEAT THE PRESS (May 30, 2014), <http://cepr.net/blogs/beat-the-press/why-is-it-so-acceptable-to-lie-to-promote-trade-deals>.

<sup>48</sup> See generally Gabriel Siles-Brügge & Ferdi De Ville, *The Transatlantic Trade and Investment Partnership and the Role of Computable General Equilibrium Modelling: An Exercise in 'Managing Fictional Expectations'*, 20 NEW POL. ECON. 653 (2015).

<sup>49</sup> Gabriel Siles-Brügge & Ferdi De Ville, *The Potential Benefits of a US-EU Free Trade Deal for Both Sides May be Much Smaller Than We Have Been Led to Believe*, LONDON SCH. ECON.: USAPP (Dec. 17, 2013), <http://blogs.lse.ac.uk/usappblog/2013/12/17/eu-us-free-trade/>.

<sup>50</sup> European Commission Staff, *Impact Assessment Report on the Future of EU-US Trade Relations* 6-7 (European Commission, Working Paper, March 12, 2013), [http://trade.ec.europa.eu/doclib/docs/2013/march/tradoc\\_150759.pdf](http://trade.ec.europa.eu/doclib/docs/2013/march/tradoc_150759.pdf).

<sup>51</sup> *Id.* at 6.

<sup>52</sup> Siles-Brügge, *supra* note 49.

<sup>53</sup> KOEN G. BERDEN ET AL., *NON-TARIFF MEASURES IN EU-US TRADE AND INVESTMENT – AN ECONOMIC ANALYSIS* 27 (2009).

<sup>54</sup> Siles-Brügge, *supra* note 49.

<sup>55</sup> European Commission Staff, *supra* note 50, at 35-36, 38, 42-43.

rest of the world stated in the CEPR study<sup>56</sup> does not represent any significant gain for the EU, as the imports to the EU from the USA and from other parts of the world would be more significant than the increase in exports. The EU will still gain from this, but the amount is likely to be very small, the same applies for the USA.<sup>57</sup> Concerning disposable income, the authors contend that the predictions of the CEPR study are inaccurate. The CEPR claims that a family of four in the EU will see their disposable income increase by €545 annually and €655 per annum in the USA.<sup>58</sup> The authors claim that the figures are not trustworthy as they were not obtained from statistics on households consisting of four individuals but rather by calculating the average figure per individual and then multiplying that figure by four in order to obtain the alleged increase in disposable income that a family of four would benefit. While EU and USA leaders aim to improve the freedom of movement in terms of direct investment through TTIP which will reinforce the bargaining power of the financial sector and multinational corporations (MNCs), they believe it will not do much for labour and most likely negatively affect the share of wages and salaries below that of productivity.<sup>59</sup>

The authors also contend that the reduction of NTBs by 25% predicted by the CEPR study<sup>60</sup> is not likely to happen in a real-life scenario because such assumptions suggest that within ten years both the EU and the USA will have achieved full economic integration. They argue that such a thing is impossible due to the differences in terms of regulatory approaches in important areas and also because of the various technical standards between the EU and the USA.<sup>61</sup> They conclude that the CEPR study is very complex, borderline incomprehensible and that the reliability of the study as a whole solely depends on the strength of the data that was used and that the theories and assumptions formulated are merely guesses and estimates.<sup>62</sup> In order to genuinely understand the impact of TTIP,<sup>63</sup> they point to the fact that one must only rely on independent and detailed technical assessments of the EU-USA trade deal and not one-sided studies such as the CEPR's.<sup>64</sup>

Despite such a scathing critique of the CEPR study,<sup>65</sup> it was referred to by other commentators such as Pelkmans et al.,<sup>66</sup> Cernat and Sousa,<sup>67</sup> or Fontagné et

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<sup>56</sup> Francois et al., *supra* note 15, at 54-55.

<sup>57</sup> Frank Ackerman & Kevin Gallagher, *The Shrinking Gains From Global Trade Liberalization in Computable General Equilibrium Models: A Critical Assessment*, 37 INT'L. J. POL. ECON. 50, 57 (2008).

<sup>58</sup> Francois et al., *supra* note 15, at 47.

<sup>59</sup> Martin Myant & Ronan O'Brien, *The TTIP's Impact: Bringing in the Missing Issue* 13 (European Trade Union Inst., Working Paper No. 2015.01, 2015).

<sup>60</sup> Francois et al., *supra* note 15, at 61.

<sup>61</sup> Myant & O'Brien, *supra* note 59, at 11-12.

<sup>62</sup> LANCE TAYLOR & RUDIGER VON ARNIM, *MODELLING THE IMPACT OF TRADE LIBERALISATION: A CRITIQUE OF COMPUTABLE GENERAL EQUILIBRIUM MODELS* 7 (Oxfam Int'l, 2006).

<sup>63</sup> Myant & O'Brien, *supra* note 59, at 10.

<sup>64</sup> WERNER RAZA ET AL., *ASSESS TTIP: ASSESSING THE CLAIMED BENEFITS OF THE TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP (TTIP)* 3 (Austrian Found. for Dev. Research, 2014).

<sup>65</sup> GABRIEL FELBERMAYR ET AL., *DIMENSIONEN UND AUSWIRKUNGEN EINES FREIHANDLSABKOMMENS ZWISCHEN DER EU UND DEN USA* (Ifö Inst. ed., 2013); KOEN G. BERDEN ET

al., who use the predictions, tables and figures of the CEPR study in their work.<sup>68</sup> For instance, Fontagné et al. confirmed the findings of the CEPR about the fact that the negotiating partners would have to do more than just remove tariffs or partially remove NTBs in order for TTIP to have a significant impact on the EU and the USA.<sup>69</sup>

Hamilton and Blocksmans offer a balanced assessment of the trade deal by acknowledging its positive effects and exposing its flaws. The authors remark that the concept of the TTIP dates back to at least twenty years, but EU and USA leaders delayed serious negotiations as they were concerned about the probable negative impact that such a partnership could have on the multilateral trading system.<sup>70</sup> Other reasons for the delayed negotiations were contentions such that a transatlantic trade deal would be insignificant because tariffs and trade barriers between the EU and USA are not significant and that the trade agreement would encompass far too many issues both in the EU and the USA.<sup>71</sup>

While many reasons may be cited for delaying the talks, it is clear that TTIP is not a typical trade agreement. Primarily concerned with issues relating to market access such as tariffs, the reduction of NTBs and the recognition of essential equivalence in terms of regulations and the alignment of standards and norms relating to issues such as dispute settlement and investment, it's a novel way of negotiation which, according to Hamilton and Blocksmans, aims to reposition the EU and the USA in a world where rising powers such as China and India are increasingly competitive.<sup>72</sup> While the TTIP is an ambitious enterprise which will deepen economic integration and boost trade, the EU and the USA will have to yield a phenomenal effort to deal with issues relating to regulatory convergence. Focusing on regulatory cooperation would maximise their chances of increasing employment rates and growth rather than only focusing on trade.<sup>73</sup> Due to the impressive size of the transatlantic economy, every tariff reduction, even the smallest, could have a much more significant effect on both economies instead of more important tariff cuts in smaller markets. The ISDS mechanism under TTIP, discussed further below, is cited as potentially the biggest flaw of the trade deal, with a lobby of populists and sovereigntists both in the EU and the USA claiming

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AL., NON-TARIFF MEASURES IN EU-US TRADE AND INVESTMENT – AN ECONOMIC ANALYSIS (ECORYS Nederlands BV ed., 2009).

<sup>66</sup> Jacques Pelkmans et al., *The Impact of TTIP: The Underlying Economic Model and Comparisons* (Ctr. for European Policy Studies, Working Paper No. 93, 2014).

<sup>67</sup> Lucian Cernat & Nuno Sousa, *TTIP: A Transatlantic Bridge for Worldwide Gains* 15 CESIFO FORUM 32, 34 (2014).

<sup>68</sup> LIONEL FONTAGNÉ ET AL., *TRANSATLANTIC TRADE: WHITHER PARTNERSHIP, WHICH ECONOMIC CONSEQUENCES?* (CEPR, 2013).

<sup>69</sup> *Id.* at 4.

<sup>70</sup> Daniel Hamilton & Steven Blocksmans, *The Geostrategic Implications of TTIP 2* (Ctr. for European Policy Studies & Ctr. For Transatlantic Relations, Working Paper No. 105, 2015).

<sup>71</sup> Peter Mandelson, Keynote Address at the University of Edinburgh (May 2, 2014).

<sup>72</sup> Hamilton & Blocksmans, *supra* note 70, at 3-4.

<sup>73</sup> Peter Chase & Jacques Pelkmans, *This Time it's Different: Turbo-Charging Regulatory Cooperation in TTIP* 26 (Ctr. for European Policy Studies & Ctr. For Transatlantic Relations, Working Paper No. 110, 2015).

that the ISDS mechanism under TTIP will cause frivolous claims and arbitrary judicial actions.<sup>74</sup> However, it seems that such a mechanism is essential for an agreement of this calibre as it will confirm the role of the EU and the USA as regulatory rule-setters.<sup>75</sup>

The way BRICS nations decide to interact with the transatlantic partners will largely depend on how the EU and the USA decide to engage with them.<sup>76</sup> If the EU and the USA present TTIP in a non-threatening way, contrary to how the TTIP is currently perceived, it is more likely that the rising powers will display less resistance to the TTIP once it is effective between the transatlantic partners.<sup>77</sup> Russia views TTIP as a threat to its personal geopolitical agenda<sup>78</sup> and has realised that the Eurasian Economic Union (EEU) is not as appealing as the EU's trade initiatives<sup>79</sup> and added to that many Eastern European countries have the perception that TTIP could be more advantageous to them.<sup>80</sup> The transatlantic trade deal is also causing Brazil to reconsider its role and position in the global trading system.<sup>81</sup> The impact of TTIP on Sub-Saharan Africa, discussed further below, could be beneficial as the area badly needs access to developed consumer markets in order to attract investments, especially in the labour-intensive export sectors which would greatly help them get out of poverty.<sup>82</sup>

The road to successfully negotiating TTIP is still long and not without obstructions. The remaining tariff barriers between the EU and the USA, more specifically in agriculture, are the most difficult to remove and issues relating to food safety and environmental standards are very sensitive and would be the most difficult to tackle.<sup>83</sup> The findings of three impact studies relating to TTIP, namely the CEPII study,<sup>84</sup> the Bertelsmann report<sup>85</sup> and the GDEI report,<sup>86</sup> are particularly

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<sup>74</sup> Hamilton & Blocksmans, *supra* note 70, at 2-13.

<sup>75</sup> Lauge Poulsen et al., *Transatlantic Investment Treaty Protection* (Ctr. for European Policy Studies & Ctr. For Transatlantic Relations, Working Paper No. 102, 2015).

<sup>76</sup> Stuart E. Eizenstat, Remarks at the Woodrow Wilson International Center for Scholars:

Transatlantic Trade and Investment Partnership (Mar. 21, 2013) (transcript available at <http://www.transatlanticbusiness.org/wp-content/uploads/2014/05/TTIP-Eizenstat-Remarks-Woodrow-Wilson-Center-3-21-13.pdf>).

<sup>77</sup> Hamilton & Blocksmans, *supra* note 70, at 6.

<sup>78</sup> Edward Lucas, *TTIP, Central and Eastern Europe, and Russia*, in *THE GEOPOLITICS OF TTIP: REPOSITIONING THE TRANSATLANTIC RELATIONSHIP FOR A CHANGING WORLD* 49, 52-53 (Daniel S. Hamilton ed., 2014).

<sup>79</sup> Steven Blocksmans et al., *Towards a Eurasian Economic Union: The Challenge of Integration and Unity* 29 (Ctr. for European Policy Studies, Working Paper No. 75, 2012).

<sup>80</sup> Daniel S. Hamilton, *Transatlantic Challenges: Ukraine, TTIP and the Struggle to be Strategic*, 52 *J. COMMON. MKT. STUD.* 25, 32 (2014); Tamas Novák, *TTIP's Implications for the Global Economic Integration of Central and Eastern Europe*, in *THE GEOPOLITICS OF TTIP: REPOSITIONING THE TRANSATLANTIC RELATIONSHIP FOR A CHANGING WORLD* 57, 61 (Daniel S. Hamilton ed., 2014).

<sup>81</sup> Vera Thorstensen & Lucas Ferraz, *The Impact of TTIP on Brazil*, in *THE GEOPOLITICS OF TTIP: REPOSITIONING THE TRANSATLANTIC RELATIONSHIP FOR A CHANGING WORLD* 137, 141 (Daniel S. Hamilton ed., 2014).

<sup>82</sup> Eveline Herfkens, *TTIP and Sub-Saharan Africa: A Proposal to Harmonize EU and U.S.*

*Preferences*, in *THE GEOPOLITICS OF TTIP: REPOSITIONING THE TRANSATLANTIC RELATIONSHIP FOR A CHANGING WORLD* 151, 152 (Daniel S. Hamilton ed., 2014).

<sup>83</sup> Hamilton & Blocksmans, *supra* note 70, at 13.

<sup>84</sup> FONTAGNE ET AL., *supra* note 68.

revealing when considering divergent views on the likely impact of the TTIP. As mentioned, the negotiating partners emphasise the reduction of NTBs as tariff barriers between the EU and the USA are relatively low. Therefore, most of the aforementioned studies assess the impact of NTBs on the EU and the USA, and also attempt to quantify the effects that the reduction of NTBs will have on the negotiating partners. The first impact study relating to NTBs between the negotiating partners was published by Ecorys<sup>87</sup> in 2009.<sup>88</sup>

The CEPII study is mostly based on the findings of the Ecorys study, except for the measurement of cross-border trade and investment protection which was measured by using a quantity-based approach from a pool of 65 countries and 9 service sectors. In this study, the authors assess the way TTIP will affect various sectors by 2025 and how the trade deal will gradually eliminate tariffs and NTBs. They assert that agriculture will experience a significant growth in terms of exports, and that services will not experience a significant increase in the first year of TTIP if the market is not fully liberalised. The study portrays a relatively positive picture of TTIP.<sup>89</sup> It should be noted that the CEPII study uses the Computable General Equilibrium (CGE) to predict the impact of TTIP. The use of CGE models gives rise to relatively serious issues. The CGE models were developed during the 80s and 90s, therefore, they do not consider issues such as production delocalisation and the changes in relation to the way trade is done in the 21<sup>st</sup> century.<sup>90</sup>

The Bertelsmann report takes a closer look at the impact of TTIP on specific EU member states such as Greece, Italy, Ireland, Portugal and Spain (GIIPS) in relation to bilateral trade. The report specifies that cuts in tariffs will not have a significant impact on trade and that trade flows between more stable and prosperous EU economies such as Germany and weaker EU economies like GIIPS will drop due to TTIP. The report also states that Britain will suffer from a decrease in trade from EU member states such as France and Germany. However, the report also states that trade between GIIPS and the USA will increase sharply.<sup>91</sup> Even though the Bertelsmann report gave a relatively balanced assessment of the impact of TTIP, the predictions formulated by the authors are not based on chapters that are currently being negotiated but instead they are a compilation of scenarios and standard econometric exercises.<sup>92</sup>

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<sup>85</sup> See generally, GABRIEL FELBERMAYR ET AL., *TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP (TTIP): WHO BENEFITS FROM A FREE TRADE DEAL?* (Glob. Econ. Dynamics ed., 2013).

<sup>86</sup> Jeronim Capaldo, *The Trans-Atlantic Trade and Investment Partnership: European Disintegration, Unemployment and Instability* (Glob. Dev. & Env't Inst., Working Paper No. 14-03, 2014).

<sup>87</sup> BERDEN ET AL., *supra* note 65.

<sup>88</sup> Oana-Antonia Colibasaru & Victor Vlad Grigorescu, *The Trans-Atlantic Trade and Investment Partnership – A Challenge for the European Union?* 15 ROM. J. EUR. AFF. 57, 60 (2015).

<sup>89</sup> Fontagné et al., *supra* note 68, at 7-9.

<sup>90</sup> Colibasaru & Grigorescu, *supra* note 88.

<sup>91</sup> FELBERMAYR ET AL., *supra* note 85, at 17.

<sup>92</sup> Colibasaru & Grigorescu, *supra* note 88, at 62.

The author of the GDEI report states that other impact studies such as the CEPII and the Bertelsmann report did not consider important factors such as income distribution and macroeconomic adjustment. In an attempt to fill the lack of information on those factors, the author used the United Nations Global Policy Model (GPM) to assess the impact of TTIP on exports, GDP, public finance and income distribution.<sup>93</sup> The author argues that TTIP will have a significantly negative impact on the labour share in GDP, which will ultimately cause a transfer of income from wages to profits with unfavourable consequences for the labour class in the EU.<sup>94</sup> The main issue with regard to the method used in this report is that the GPM uses data that involves an analytical structure composed of countries that have similar patterns. In cases where the countries do have similar patterns such a method can produce interesting results. However, the EU and the USA do not have similar patterns and this can be seen when analysing the integration or disintegration of the labour markets which lead to the socio-economic issues stated in the study.<sup>95</sup>

There is one striking issue that arises from analysing the three impact studies; all three studies have their own method of predicting the effects of reducing NTBs on investment and trade. There is currently no agreed-upon method of calculating such effects. Therefore, the results produced by the studies cannot be considered as absolute and no one study can be said to be the most accurate.<sup>96</sup> However, the input-output analysis method could be an alternative to the aforementioned methods. The input-output analysis method is defined as a technique that calculates the effects that changes in different sectors have on the economy of a country. The main issues with the previously mentioned methods are their complexity and lack of transparency. The input-output analysis method offers both ease of use and transparency.<sup>97</sup>

#### A. *The claimed benefits of TTIP for the EU and the USA*

Proponents claim that TTIP would be the catalyst for the revival of the transatlantic economy, enabling the EU and the USA to establish better standards in relation to capital flows which in turn will open markets in different parts of the world.<sup>98</sup> TTIP would enable EU and USA firms to reduce their costs of production, leading to an increase in their profit margin, and also facilitate the exchange of

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<sup>93</sup> Capaldo, *supra* note 86, at 10.

<sup>94</sup> *Id.* at 19-20.

<sup>95</sup> *Id.* at 63.

<sup>96</sup> *Id.* at 60.

<sup>97</sup> QUEENS LAND GOV'T STATISTICIAN'S OFFICE, OVERVIEW OF SOME ALTERNATIVE METHODOLOGIES FOR ECONOMIC IMPACT ANALYSIS 1-2 (2012).

<sup>98</sup> BERNARD HOEKMAN, BUSINESS AND TRANSATLANTIC TRADE INTEGRATION 28-29, 31 (CESifo Forum ed., 2013).

skills, ideas<sup>99</sup> and innovation relating to the production of goods.<sup>100</sup> If TTIP is successfully negotiated, it could become a rule maker for global standards.<sup>101</sup>

Felbermayr and Larch are of the opinion that TTIP would have a significantly positive impact for welfare in the EU and the USA. For instance, it is suggested that the USA and the UK will experience an increase of 13.4% and 9.7% in GDP, respectively. The reason for such an increase can be attributed to two sources. Firstly, TTIP will increase the availability of foreign products and also new varieties of products which in turn will have a positive effect on welfare. Secondly, lower trading costs would reduce retail prices which would decrease the consumer price index thus increasing the purchasing power of income.<sup>102</sup>

Furthermore, they suggest that the reduction of NTBs, such as bureaucracy and regulations will generate a total gain of 80%, boosting growth for both partners and reduce costs for exporters from the EU and the USA who do business across the Atlantic.<sup>103</sup> The authors also argue that the reduction of tariffs and NTBs will lead to a deeper integration of both markets,<sup>104</sup> resulting in increased competitiveness, which in turn would create more jobs and increase productivity, especially for EU member states that are still suffering from the 2008 crisis.<sup>105</sup> Former British Prime Minister David Cameron contended that TTIP would generate an additional £10 billion to the British economy, £63 billion to the USA's economy and €100 billion to the rest of the world.<sup>106</sup> Moreover, Aldien argues that negotiations of that calibre have the ability to update and bring back into context rules relating to labour rights and standards in order to ensure that MNCs do not have the ability to bring frivolous claims or attempt to dispute the validity of legitimate public regulations. If TTIP is properly negotiated, labour rights and standards both in the EU and the USA could be considerably strengthened.<sup>107</sup>

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<sup>99</sup> Thomas Straubhaar, *TTIP: Don't Lose Momentum!*, in *THE GEOPOLITICS OF TTIP: REPOSITIONING THE TRANSATLANTIC RELATIONSHIP FOR A CHANGING WORLD* 43-44 (Daniel S. Hamilton ed., 2014).

<sup>100</sup> Kurt Hübner, *TTIP and CETA. Remaking of the Atlantic Economy?*, in *THE TTIP: THE TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP BETWEEN THE EUROPEAN UNION AND THE UNITED STATES* 47-48 (Joaquín Roy & Roberto Domínguez ed., 2014).

<sup>101</sup> JIM KOLBE, *ALICE IN TRADE-LAND: THE POLITICS OF TTIP 2* (GMF ed., 2014).

<sup>102</sup> GABRIEL FELBERMAYR & MARIO LARCH, *THE TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP (TTIP): POTENTIALS, PROBLEMS AND PERSPECTIVES* (CESifo Forum ed., 2013).

<sup>103</sup> LUCIAN CERNAT & NUNO SOUSA, *TTIP: A TRANSATLANTIC BRIDGE FOR WORLDWIDE GAINS* 34 (CESifo Forum ed., 2014).

<sup>104</sup> DANIEL GROS & CINZIA ALCIDI, *THE GLOBAL ECONOMY IN 2030: TRENDS AND STRATEGIES FOR EUROPE* 93 (European Union ed., 2013).

<sup>105</sup> Johanna Körnig & Claudia Schmucker, *TTIP: A Chance for Europe*, *WORLD AFF. J.* (May 22, 2014), <http://www.worldaffairsjournal.org/content/ttip-chance-europe>.

<sup>106</sup> David Cameron, *A British-American Tax and Trade Agenda*, *WALL ST. J.* (May. 12, 2013), <https://www.wsj.com/articles/SB10001424127887324216004578478652537662348>.

<sup>107</sup> Edward Aldien, *The Case for TTIP*, *POLITICO* (Oct. 6, 2015, 1:36 PM), <http://www.politico.eu/article/the-case-for-ttip/>.

## 1. Benefits of TTIP for specific EU member states

The American Chamber of Commerce to the European Union (AmChamEU) commissioned a study<sup>108</sup> from the World Trade Institute on the impact of TTIP for all twenty-eight EU member states. Taking four of the least wealthy EU member states discussed in the study, namely Hungary, Slovakia, Lithuania and Malta, demonstrates the positive impact of TTIP on the EU in terms of wages, consumer goods and exports.

### a. *Wages*

It is expected that TTIP will strengthen the economic relationship between the selected EU member states and the USA by having a positive effect on wages. The EU-USA trade deal will reinforce the economic relationship between Hungary and the USA by contributing to higher income for both low and high skilled labour in Hungary. Low and high skilled Hungarian workers will benefit from an increase of 0.9% and 0.21% respectively.<sup>109</sup> The same applies for Slovakia as the country has a strong economic relationship with the USA; both low and high skilled Slovakian workers will see their wages increase by 0.34% and 0.36% respectively.<sup>110</sup> Even though Lithuania and Malta do not have a very strong economic relationship with the USA, that will not deter the positive impact that TTIP will have on wages for those EU member states. In Lithuania, the salary of low skilled workers will increase by 1.42% and high skilled workers will increase by 1.32%<sup>111</sup> and in Malta, both low and high skilled labour will experience an increase in wages of 0.69%.<sup>112</sup>

### b. *Consumer goods*

The study predicts that TTIP will have a positive impact for consumers living in the selected EU member states, as it is expected that the trade deal would decrease the prices of consumer goods. TTIP is expected to decrease the price of an average car by -0.8%, transport equipment by -0.6% and consumer prices by -0.1% in Hungary.<sup>113</sup> Lithuanian consumers will also pay less for cars as TTIP will decrease the price of an average car by -3.8% and consumer goods in the country will decrease by -0.9%.<sup>114</sup> In the case of Malta, consumer prices will be lowered by -0.2%, the price of an average car will experience a reduction of -0.7% and the prices of chemicals will go down by -0.6%.<sup>115</sup> Finally, the EU-USA trade deal will

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<sup>108</sup> KOEN BERDEN & JOSEPH FRANCOIS, TTIP AND THE EU MEMBER STATES: AN ASSESSMENT OF THE ECONOMIC IMPACT OF AN AMBITIOUS TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP AT EU MEMBER STATE LEVEL (World Trade Institute 2016).

<sup>109</sup> *Id.* at 103.

<sup>110</sup> *Id.* at 143.

<sup>111</sup> *Id.* at 121.

<sup>112</sup> *Id.* at 124.

<sup>113</sup> *Id.* at 103.

<sup>114</sup> *Id.* at 121.

<sup>115</sup> *Id.* at 124.

reduce the price of an average car and transport equipment by -0.8% and -1.8%, respectively in Slovakia.<sup>116</sup>

### c. Exports

It is expected that TTIP will increase the exports from the selected EU member states to the USA and boost growth and economic activity in such states. Hungarian exports to the USA are expected to increase by 36%. The top five industries in Hungary that are expected to reap significant gains from TTIP are the automotive, electrical machinery, machinery, chemical and pharmaceutical and manufacturing industries. The aforementioned industries combined will bring an additional €726 million to the Hungarian economy.<sup>117</sup> In the case of Lithuania, exports to the USA are expected to increase by 18%, more specifically due to an increase in activity in the chemical and pharmaceutical, manufacturing, wood and paper products, processed foods and machinery industries amounting to an additional €121 million for Lithuania.<sup>118</sup> Malta's exports to the USA will increase by 23%. The industries that are expected to generate the most gains are the electrical machinery, chemical and pharmaceutical, manufacturing, machinery and financial services industries. The aforementioned industries alone are expected to generate an additional €66 million for Malta.<sup>119</sup> The study predicts that Slovakia's exports to the USA will increase by 116%. The Slovakian automotive industry alone will reap significant gains representing €860 million. Other industries such as the manufacturing, machinery and electrical machinery will generate a combined €123 million to the Slovakian economy.<sup>120</sup>

## 2. Benefits of TTIP for specific U.S. states

The Atlantic Council, the Bertelsmann Foundation, and the British Embassy in Washington financed a study<sup>121</sup> on the impact of TTIP for all fifty U.S. states. Five states, namely Colorado, Minnesota, Montana, New York and Texas, representing different geographical parts of the country, demonstrate the positive impact of TTIP on the U.S. economy in terms of wages, consumer goods and exports.

### a. Employment

The effects of TTIP on the employment rate in the selected states looks very promising. For the state of Colorado, TTIP is expected to create 13,180 jobs in business services, communications services, financial services and the

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<sup>116</sup> *Id.* at 143.

<sup>117</sup> *Id.* at 103.

<sup>118</sup> *Id.* at 121.

<sup>119</sup> *Id.* at 124.

<sup>120</sup> *Id.* at 143.

<sup>121</sup> TYSON BARKER & ANNE COLLETT ET AL., JOBS AND GROWTH FROM COAST TO COAST: TTIP AND THE FIFTY STATES (The Atlantic Council et al. eds., 2013).

manufacturing industry.<sup>122</sup> Minnesota is expected to experience job growth in sectors such as personal services and the construction industry amounting to the creation of 15,170 jobs.<sup>123</sup> In the case of Montana, it is anticipated that TTIP will not have a very significant effect on job growth as the trade deal will only create 2,390 jobs.<sup>124</sup> Finally, New York and Texas are the big winners in terms of job growth as the trade deal is expected to generate 50,520 jobs in New York<sup>125</sup> and 67,780 jobs in Texas.<sup>126</sup>

b. *Exports*

It is estimated that Colorado's exports to the EU will increase by 20.1%. Exports in sectors such as the automotive, chemical and the metal industry will significantly increase, generating gains of more than \$714 million to the state. In addition, the reduction of tariff barriers and NTBs will increase Colorado's electrical machinery exports by 44.1%.<sup>127</sup> Minnesota is expected to experience an increase in exports to the EU of 38.5% representing an overall gain of \$2.6 billion. The state's automotive industry alone will possibly generate an estimated \$1.7 billion representing an increase of 350% for this sector. It should be noted that this is mostly due to the reduction of tariff barriers and NTBs.<sup>128</sup> The report predicts that Montana's exports to the EU will increase by 19.1%. Products related to the machinery, metal and agricultural industries are expected to experience an increase in exports amounting to gains of more than \$94 million. The reduction of tariff barriers and NTBs will also potentially increase the state's chemical exports by 34.2%.<sup>129</sup> In the case of New York, it is anticipated that the state's exports to the EU will increase by 24.4% generating approximately \$7.6 billion. More than half of the state's expected financial gains will come from the exportation of chemicals, metal products and motor vehicles to the EU.<sup>130</sup> Finally, due to TTIP, Texas is expected to experience an increase in exports to the EU of 24.3%. Much like New York, most of Texas' expected gains will come from the exportation of motor vehicles, metal products and chemicals to the EU. It is anticipated that Texas' exports to the EU will generate more than \$10 billion.<sup>131</sup>

The ultimate conclusion of the evidence discussed is that the export boom that TTIP would bring if successfully negotiated and implemented would revive both the EU's and the USA's economy, but most importantly it will significantly boost the employment rate in every EU member state and in every state in the U.S.

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<sup>122</sup> *Id.* at 13.

<sup>123</sup> *Id.* at 30.

<sup>124</sup> *Id.* at 33.

<sup>125</sup> *Id.* at 39.

<sup>126</sup> *Id.* at 50.

<sup>127</sup> *Id.* at 13.

<sup>128</sup> *Id.* at 30.

<sup>129</sup> *Id.* at 33.

<sup>130</sup> *Id.* at 39.

<sup>131</sup> *Id.* at 50.

### B. *The claimed flaws and drawbacks of TTIP for the EU and the USA*

Some commentators disagree that TTIP would boost the economy of the negotiating partners. According to Capaldo, the trade deal would cause major losses in terms of GDP especially for France, Germany, UK, Italy and other Northern European countries with losses of 0.48%, 0.29%, 0.07%, 0.03% and 0.50%, respectively. Capaldo also contends that TTIP would cause losses of labour income for EU member states such as, France, UK, Germany, Italy and other Northern European countries with losses of €5,518, €4,245, €3,402, €661, €4,848 per worker, respectively.<sup>132</sup>

The majority of studies<sup>133</sup> that assessed the impact of TTIP have estimated the effects of removing NTBs. It is suggested that those estimations are questionable as it is very difficult to calculate such effects. Differing regulations cannot be measured as they do not come in measurable form. Attempts at such calculations rely solely upon guesswork and not solid facts.<sup>134</sup> Raza et al. supports this contention by pointing out that quantifying the social costs of regulatory changes is very difficult.<sup>135</sup>

It is contended that a major issue arising from TTIP will be the social cost for the EU of the large restructurings that would arise from the mergers, acquisitions, closures and privatisations brought about by the completion of a single transatlantic market. In a system where prices for goods and services are uniform, wages and profits have a tendency to converge. Unemployment is high in Europe and labour prices will potentially experience a significant decrease, which will most probably lead the EU to follow the unequal income trend established in the USA.<sup>136</sup> It is suggested that TTIP will have a minor impact on growth and also be a major obstacle for the overall harmony of the EU, and most probably destabilise the multilateral trading system.<sup>137</sup>

Another social cost that has not been considered is the inclusion of the ISDS mechanism in TTIP<sup>138</sup>, discussed further below. It is suggested that governments might hold back from adopting new policies in the interest of its citizens which could upset powerful investors and lead to costly legal procedures

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<sup>132</sup> Capaldo, *supra* note 86, at 2-3.

<sup>133</sup> Francois et al., *supra* note 15; FONTAGNÉ ET AL., *supra* note 68; FELBERMAYR ET AL., *supra* note 85.

<sup>134</sup> MARTIN MYANT, THE TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP: EXAGGERATED HOPES FROM THE LIBERALISING AGENDA? 2 (2014).

<sup>135</sup> RAZA ET AL., *supra* note 64, at 19-21.

<sup>136</sup> ROBERT KUTTNER & CONNY REUTR ET. AL., TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP: FLAWS AND FALLACIES UNCOVERED 20 (Solidar 2015).

<sup>137</sup> PIERRE DEFRAIGNE, The Future of EU-US Relations: Political and Economic Reflections on the TTIP AGREEMENT 4 (2014).

<sup>138</sup> GIOVANNI COZZI, TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP: ANOTHER FREE TRADE CHARADE? 1 (2014).

and high compensation costs, financed with public budgets, under the ISDS mechanism.<sup>139</sup>

It appears that the EU is not ready for TTIP as not all EU member states enjoy the same level of economic stability. Member states that are very competitive such as Germany are eager to complete the deal while others such as Portugal and France are not as enthusiastic as they have to make a lot of concessions.<sup>140</sup> Another social cost outlined by Stiglitz is that through TTIP, trade representatives, on behalf of MNCs, will most likely lower or at least attempt to lower important standards relating to labour, health and the environment.<sup>141</sup>

### C. *The impact of TTIP on specific sectors*

#### 1. Public health

The European Commission asserts that public health standards and EU laws relating to the protection of public health will not be affected by TTIP.<sup>142</sup> Jarman claims that the negotiating partners are inducing the public in error by making false promises. Jacobsen supports Jarman's argument by stating that regulatory cooperation between the EU and the USA will force the EU to lower its health standards in order to be in line with the way the USA deals with health issues.<sup>143</sup> Jarman also adds that TTIP would greatly harm public health protections and threaten fundamental principles such as access to medical treatment and vital medications along with proper regulations on tobacco products and alcohol.<sup>144</sup>

TTIP opponents believe that the agreement will greatly facilitate the process of privatisation of health care services resulting in the irreversible extinction of public health services. The main concern is that citizens who cannot pay for health care would be marginalised and left without treatment,<sup>145</sup> effectively generating more health inequalities and widening the social gap between the wealthy and the less

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<sup>139</sup> WERNER RAZA & BERNHARD TRÖSTER, *THE BLIND SPOTS OF TTIP – TRADE IMPACT ASSESSMENT: MACROECONOMIC ADJUSTMENT COSTS AND THE SOCIAL COST OF REGULATORY CHANGE 21-22* (Austrian Foundation for Development Research 2014).

<sup>140</sup> Uri Dadush, *Cold Water for Hot Trade Deals*, CARNEGIE ENDOWMENT FOR INT'L PEACE (May 13, 2013), <http://carnegieendowment.org/2013/05/13/cold-water-for-hot-trade-deals/g39c>.

<sup>141</sup> Joseph Stiglitz, *The Free-Trade Charade* (July 4, 2013), <https://www.project-syndicate.org/commentary/transatlantic-and-transpacific-free-trade-trouble-by-joseph-e--stiglitz?barrier=accessreg>.

<sup>142</sup> European Commission, *EU-US Transatlantic Trade and Investment Partnership: Trade Cross-cutting Disciplines and Institutional Provisions*, EURACTIV (2013), <http://www.euractiv.com/section/trade-society/news/ttip-health-sector-braced-for-damage-control/>.

<sup>143</sup> Henriette Jacobsen, *TTIP: Health Sector Braced for 'Damage Control'*, EURACTIV (Oct. 7, 2013), <http://www.euractiv.com/section/trade-society/news/ttip-health-sector-braced-for-damage-control/>.

<sup>144</sup> Holly Jarman, *Public Health and the Transatlantic Trade and Investment Partnership*, 24 EUR. J. PUB. HEALTH. 181, 181 (2014).

<sup>145</sup> Neil Bennet, *HEALTH CONCERNS RAISED OVER EU-US TRADE DEAL*, 384 No. 9986 THE LANCET 843, 843-44 (2014).

fortunate.<sup>146</sup> Hilary supports this argument by stating that TTIP will not only increase the costs of medications and health services in Europe but it will also more aggressively enforce property rights in order for private pharmaceutical corporations to make more profit by forcing public health systems to pay for proprietary drugs which are more expensive, rather than generic drugs which are typically cheaper.<sup>147</sup> Weiss blames the negotiating partners, especially the EU, for not mentioning in their reports and impact studies that TTIP may cause such inequalities.<sup>148</sup> A report published by Oxfam states that the controversial Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) will have a dedicated chapter in TTIP named TRIPS-plus.<sup>149</sup> Weiss argues that by promoting TRIPS-plus provisions in TTIP the negotiating partners are focusing on the financial interest of the pharmaceutical industry instead of prioritising the welfare of its citizens, with the likelihood of a significant increase in the costs of medications.<sup>150</sup>

As explained previously, the main objective of TTIP is to eliminate unnecessary regulations that prevent the liberalisation of trade and investment.<sup>151</sup> The problem with eliminating so-called unnecessary regulations is that essential protective measures are at risk of being eliminated because they might be regarded as obstacles. For instance, the field of occupational health and safety would be at risk if such a thing should happen, because the elimination of measures and protections in the aforementioned field would not allow member states to adopt higher standards and levels of protection that surpasses the minimum standards established by EU law.<sup>152</sup>

## 2. Labour and enterprise

The EU and the USA have to make a critical choice, to disregard labour standards and labour rights by lowering wages and promoting an unequal transatlantic treaty, or focusing on making labour rights and labour standards

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<sup>146</sup> See generally, ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, IN IT TOGETHER: WHY LESS INEQUALITY BENEFITS ALL (2015).

<sup>147</sup> John Hilary, *The Transatlantic Trade and Investment Partnership and UK Healthcare*, 349 THE BMJ 1, 1-2 (2014).

<sup>148</sup> MARK WEISS ET AL., TRADING HEALTH? UK FACULTY OF PUBLIC HEALTH POLICY REPORT ON THE TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP 10 (UK Faculty of Public Health 2015).

<sup>149</sup> SOPHIE BLOEMEN & TESSEL MELLEMA, TRADING AWAY ACCESS TO MEDICINES 3 (2014).

<sup>150</sup> Mark Weiss John Middleton et al, *Warning: TTIP Could be Hazardous to your Health* 37 J. PUB. HEALTH 367, 367-68 (2015).

<sup>151</sup> European Commission Press Release IP/13/1091, EU and US Conclude Second Round of TTIP Negotiations in Brussels (Nov. 15, 2013).

<sup>152</sup> *European Economic, Employment and Social Policy TTIP: Fast Track to Deregulation and Lower Health and Safety Protection for EU Workers*, at 1-2 (2015), <https://www.etui.org/Publications2/Policy-Briefs/European-Economic-Employment-and-Social-Policy/TTIP-fast-track-to-deregulation-and-lower-health-and-safety-protection-for-EU-workers>.

better, leading to a fair and equitable transatlantic agreement.<sup>153</sup> Trade unions in Europe such as GMB, a British trade union with more than 630,000 members,<sup>154</sup> and detractors of TTIP are of the opinion that the trade deal will ruin decades of hard-won labour rights and that the EU will be forced to lower its labour standards to satisfy avaricious American MNCs.<sup>155</sup> Trade Unions also fear that the European Commission may try to connect the Regulatory Fitness and Performance Programme (REFIT) to TTIP. Even though the Commission claims that REFIT aims to simplify EU law and reduce regulatory costs,<sup>156</sup> critics claim that REFIT will be used to promote and implement TTIP. According to them, REFIT would exacerbate TTIP's negative effects on the health and safety of workers in Europe.<sup>157</sup>

Conversely, Workman comments that TTIP will have a chapter dedicated to SMEs that will facilitate SMEs exports, leading to a boost in their income. By increasing regulatory convergence in the field of safety protections, SMEs would be able to focus their attention on innovation and product development which would make them more effective and boost their sales as their products would be innovative and of a high standard.<sup>158</sup> According to the European Commission, the boost to household income that would be occasioned by TTIP<sup>159</sup> would generate more sales for SMEs as the purchase power of citizens in the EU and the USA would increase.<sup>160</sup>

Khorana believes that since no draft of TTIP was made available, the Comprehensive Economic and Trade Agreement (CETA), which is a trade agreement between the EU and Canada,<sup>161</sup> is probably the best alternative for one to get an understanding of labour provisions in TTIP. Article 3 of chapter 24 of CETA states that the negotiating partners, being members of the International Labour Organisation (ILO) shall comply with the fundamental labour standards of the organisation, i.e., the four core labour standards detailed in the ILO

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<sup>153</sup> Lance Compa, *Labor Rights and Labor Standards in Transatlantic Trade and Investment Negotiations: An American Perspective* 5 LAB. & GLOBALIZATION 120, 120-21 (Ed. Christoph Scherrer, 2014).

<sup>154</sup> GMB, *About GMB* (2016), <http://www.gmb.org.uk/> (last visited Sep. 23, 2017).

<sup>155</sup> GABRIEL SILES-BRÜGGE & FERDI DE VILLE, *TTIP: THE TRUTH ABOUT THE TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP* 20 (Polity Press 2016).

<sup>156</sup> European Commission, *REFIT – Making EU Law Simpler and Less Costly*, [http://ec.europa.eu/smart-regulation/refit/index\\_en.htm](http://ec.europa.eu/smart-regulation/refit/index_en.htm).

<sup>157</sup> Claude Serfati, *The Transatlantic Trade and Investment Partnership (TTIP): A Controversial Agreement and Dangerous for Workers* 22-23 (Eur. Trade Union Inst., Working Paper No. 2015.07, 2015).

<sup>158</sup> Garrett Workman, *The Transatlantic Trade and Investment Partnership: Big Opportunities for Small Business* 6-9 (Nov. 2014), [http://www.eaccny.com/wp-content/uploads/2013/08/TTIP\\_SME\\_Report.pdf](http://www.eaccny.com/wp-content/uploads/2013/08/TTIP_SME_Report.pdf).

<sup>159</sup> Francois, et al., *supra* note 15, at 47.

<sup>160</sup> EUROPEAN COMMISSION, *IN FOCUS: TRADE AND INVESTMENT PARTNERSHIP (TTIP), QUESTIONS AND ANSWERS* (2015), <http://ec.europa.eu/trade/policy/in-focus/ttip/questions-and-answers/>.

<sup>161</sup> *See generally*, EUROPEAN Commission, *Comprehensive Economic and Trade Agreement (CETA)* (last updated Sept. 20, 2017), <http://ec.europa.eu/trade/policy/in-focus/ceta/>.

Declaration.<sup>162</sup> It is contended that TTIP will most likely follow the same trend as both the EU and USA are members of the ILO.<sup>163</sup> Along the same line of thought, Kraatz believes that TTIP has the potential to establish standards in relation to the inclusion of labour rights provisions in the main body of the agreement as it has been done in previous trade agreements such as CETA.<sup>164</sup>

However, De Ville argues that even though the EU and Canada included labour rights provisions in CETA and also agreed to respect and implement the ILO core conventions, the chapter on labour protections is not enforceable before CETA's dispute settlement mechanism as stated in article 11 of chapter 23 of the agreement. Hence, the labour provisions in CETA serves no purpose and can be qualified as rights without remedies, as the agreement does not impose any obligation on the trade partners to take labour rights violations into account.<sup>165</sup> In the event that the labour chapter in TTIP follows the same trend as the one in CETA, the concerns that TTIP would undermine labour rights and labour standards would be legitimate. It is therefore essential that the negotiating partners, especially the EU, learn from past errors by making sure that TTIP does not undermine labour rights and labour standards.

### 3. Agriculture and food

Progress on issues relating to agriculture and food will depend on how seriously the EU and the USA decide to deal with them. On the one hand, if they are dealt with lightly, the treaty is likely to consist of narrow or even inadequate commitments on food regulations and agricultural market access. Conversely, if they are dealt with seriously, it should rectify a number of flaws in the field of food regulations and agricultural policy.<sup>166</sup>

Currently, meat treated with certain growth hormones<sup>167</sup> is banned in the EU, and strict regulations apply for genetically modified (GM) crops. All those restrictions arise from the fact that the EU deems that those methods of producing food are hazardous for the human body. The USA has voiced out against those

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<sup>162</sup> International Labour Organization, *ILO Declaration on Fundamental Principles and Rights at Work and its Follow-up - Adopted by the International Labour Conference at its Eighty-Sixth Session, Geneva*, (June 18, 1998), <http://www.ilo.org/declaration/lang--en/index.htm>.

<sup>163</sup> SANGEETA KHORANA, *THE TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP (TTIP) NEGOTIATIONS BETWEEN THE EU AND THE USA: CAUGHT BETWEEN MYTH AND REALITY* 88 (Barcelona Centre for International Affairs 2015).

<sup>164</sup> Susan Kraatz, *The Transatlantic Trade and Investment Partnership (TTIP) and Labour* (2014) (European Parliament, Briefing Paper No. 536.315), [http://www.europarl.europa.eu/RegData/etudes/BRIE/2014/536315/IPOL\\_BRI\(2014\)536315\\_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/BRIE/2014/536315/IPOL_BRI(2014)536315_EN.pdf).

<sup>165</sup> Ferdi De Ville, *In Pursuit of a Consistent European Parliament Position on Two Transatlantic Trade Agreements* 13-14 (2016).

<sup>166</sup> Tim Josling & Stefan Tangermann, *Agriculture, Food and the TTIP: Possibilities and Pitfalls* 1-2, (Centre for Europ. Pol'y Stud., Working Paper No. 99/2014, 2014).

<sup>167</sup> Council Directive 81/602/EEC, 1981 O.J. (L222) 32; Directive 2003/74/EC, of the European Parliament and of the Council of 22 September 2003 and amending Council Directive 96/22/EC concerning the prohibition on the use in stockfarming of certain substances having a hormonal or thyrostatic action and of beta-agonists 2003 O.J. (L262) 17.

regulations, arguing that the EU is using a protectionist strategy to prevent USA farms from selling their products in the EU and that GM crops and growth hormones were not proven scientifically to be dangerous for the human body.<sup>168</sup> In 2014, fifty U.S. senators signed a letter to the U.S. Trade Representative and U.S. Secretary of Agriculture expressing their fears that the EU would use TTIP to weaken American farmers' competitiveness by imposing unnecessary restrictions, acting as trade barriers, on the use of common food names.<sup>169</sup> On the European side, detractors of TTIP claim that the treaty would lower food and agriculture standards in the EU by allowing the importation and sale of the aforementioned products exposing the population of the EU to serious health risks.<sup>170</sup> Added to that, the Centre for International Environmental Law (CIEL) argues that TTIP would considerably lower standards on pesticides that are in force in the EU and in some U.S. states.<sup>171</sup>

It has been suggested that some EU farmers fear that TTIP would terminate the protection that EU law offers to EU farmers in relation to the production of regional food specialties. Three EU schemes, namely protected designation of origin (PDO), protected geographical indication (PGI) and traditional speciality guaranteed (TSG), promote and protect names of quality agricultural products and foodstuffs.<sup>172</sup> EU farmers say that if TTIP is implemented 'Europe [will start] importing Nuremberg pork sausages from Kentucky or allowing U.S. food companies to export parmesan cheese even when the milk has not been produced in Italy'.<sup>173</sup> They contend that TTIP would not only allow lower quality products to enter the EU market but also significantly reduce the income of EU farmers.<sup>174</sup>

In an attempt to reassure the public that TTIP would not undermine any standards relating to agriculture and food, the European Commission stated that TTIP will not terminate any EU regulation relating to the protection of regional food specialties.<sup>175</sup> The UK Government adopted the same discourse by stating in a Parliamentary Questions session that TTIP would be beneficial to UK agriculture

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<sup>168</sup> Letter from Ambassador Demetrios Marantis, Acting US Trade Representative to the Honorable John Boehner, Speaker of the House of Representatives (Mar. 20, 2013) (on file with the Exec. Off. of the President).

<sup>169</sup> Letter from 50 U.S. Senators to Tom Vilsack, Secretary of Agriculture, and Michael Froman, United States Trade Representative (Mar. 11, 2014) (on file with the U.S. Senate).

<sup>171</sup> DOMINIC WEBB, *THE TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP Briefing*, HC, Paper No. 06688 at 16-17 (UK).

<sup>171</sup> ERICA SMITH, DAVID AZOULAY ET AL., *LOWEST COMMON DENOMINATOR: HOW THE PROPOSED US-EU TRADE DEAL THREATENS TO LOWER STANDARDS OF PROTECTION FROM TOXIC PESTICIDES 2-5* (Center for International Environmental Law, 2015).

<sup>172</sup> *Agriculture and Rural Development: EU quality logos*, EUR. COMM'N (last visited: Sept. 23, 2017), [http://ec.europa.eu/agriculture/quality/schemes/index\\_en.htm](http://ec.europa.eu/agriculture/quality/schemes/index_en.htm).

<sup>173</sup> Robin Emmott, *EU says German sausages not at risk in U.S. trade deal*, REUTERS, (Jan. 6, 2015, 8:46 AM), <http://www.reuters.com/article/us-eu-usa-trade-idUSKBN0KF18320150106>.

<sup>174</sup> *Id.*

<sup>175</sup> *Intellectual Property Rights (IPR) and Geographical Indications (GIs) in TTIP*, EUR. COMM'N, [http://trade.ec.europa.eu/doclib/docs/2015/january/tradoc\\_153020.7\\_IPR\\_GIs\\_2.pdf](http://trade.ec.europa.eu/doclib/docs/2015/january/tradoc_153020.7_IPR_GIs_2.pdf).

and that the trade deal would not prevent them from implementing their own domestic regulatory standards concerning agriculture and foodstuffs.<sup>176</sup>

#### D. Regulatory cooperation

Transatlantic regulatory cooperation is not a new topic of debate. In 1995, the Trans-Atlantic Business Dialogue, now the Trans-Atlantic Business Council (TABC), was established in an attempt to converge business interests across the Atlantic in order to allow goods that were approved in one place to be certified in another and to deal with excessive regulations and differences in the regulatory systems of the EU and the USA.<sup>177</sup> The TABC managed to align regulations on both sides of the Atlantic in areas such as telecommunications equipment and certain types of medical devices.<sup>178</sup> Moreover, in 2008 the USA–EU High Level Regulatory Cooperation Forum was also established to align regulatory differences between the EU and the USA.<sup>179</sup>

According to a survey conducted by the Atlantic Council and the Bertelsmann Foundation 80% of welfare gains from TTIP will come from the reduction of tariffs and NTBs. The survey states that regulatory cooperation would be a significant challenge during the negotiation rounds of the trade deal. However, they also affirm that regulatory convergence is the most important aspect of the agreement.<sup>180</sup>

The reason why regulatory issues are very important is because a significant portion of EU-USA trade is intra-industry and intra-firm, meaning that TTIP will reshape existing value chains for both negotiating partners.<sup>181</sup> It is clear that tariffs are not the only barriers to trade, bureaucratic red-tape occasioned by inadequate regulations significantly slow down the free movement of goods and services between the EU and the USA.<sup>182</sup> Regulatory convergence has the potential to benefit all firms regardless of their geographical location, because in theory, regulations exist to enhance quality and standards and should not be used in a discriminatory way.<sup>183</sup> Disparities in terms of regulations do not always reflect divergence in objectives such as consumer protection or the safety of products.<sup>184</sup> The fact that the EU and the USA have relatively the same level of consideration

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<sup>176</sup> 30 Oct. 2014, Parl. Deb HC (2014) col. 375 (UK).

<sup>177</sup> MICHELLE EGAN, *CONSTRUCTING A EUROPEAN MARKET* 256 (Oxford University Press, 2001).

<sup>178</sup> 1999 O.J. (L 31/3) 31.

<sup>179</sup> *Europe: United States-European Union High-Level Regulatory Cooperation Forum*, OFFICE OF MGMT. & BUDGET, [https://obamawhitehouse.archives.gov/omb/oira/irc\\_europe](https://obamawhitehouse.archives.gov/omb/oira/irc_europe), (last visited Sep. 15, 2016).

<sup>180</sup> Barker & Workman, *supra* note 36, at 4.

<sup>181</sup> OECD TRADE AND AGRICULTURE DIRECTORATE, *THE TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP: WHY DOES IT MATTER?* 3 (2013), <http://www.oecd.org/trade/TTIP.pdf>.

<sup>182</sup> Lester & Barbee, *supra* note 19, at 849-50.

<sup>183</sup> See generally Bernard Hoekman, *International Regulatory Cooperation in a Supply Chain World*, in 6 *REDESIGNING CANADIAN TRADE POLICIES FOR NEW GLOBAL REALITIES* (Stephen Tapp et al. eds., 2016).

<sup>184</sup> Bernard Hoekman, *Fostering Transatlantic Regulatory Cooperation and Gradual Multilateralization*, 18 J. INT'L ECON. L. 609, 609-12 (2015).

for consumer protection and the safety of products should facilitate regulatory convergence which would lead to the reduction of regulatory trade costs.<sup>185</sup>

In order for the negotiating partners to align their regulations, they have to first identify the causes of regulatory disparities. Four causes of regulatory divergences exist, namely accidental regulatory divergences, disparate risk assessments, disparate risk tolerances and political considerations.<sup>186</sup>

Typically, accidental regulatory divergences are the result of a lack of synchronisation between the negotiating partners who are planning to adopt mutual regulations. This lack of communication may in some cases cause the regulators to unintentionally implement differing approaches.<sup>187</sup> Disparate risk assessments may also cause regulatory disparities. First of all, risk assessment refers to a systematic process that aims to quantify and evaluate risks that may take place. Disparate risk assessment arises when one of the negotiating partners relies on more advanced studies than their counterpart(s) elsewhere and because of that regulations may differ.<sup>188</sup> Another cause of regulatory disparity may arise with disparate risk tolerances. Risk tolerance refers to the process of using the information gathered during the risk assessment process combined with relevant policy considerations in order to determine the level of risk society is more comfortable with and what regulations are more suitable to achieve the preferred level of risks.<sup>189</sup> It should be noted that the aforementioned process is subjective and is therefore different for every country, which in many cases causes regulatory disparities.<sup>190</sup> Finally, political considerations may also be a cause of regulatory divergence as they are very different in each country. For instance, in the USA regulations may be influenced by politics in two ways. First, all agency powers originate from authorising statutes.<sup>191</sup> Secondly, Congress is not obliged to carry out a thorough risk assessment and risk tolerance process before enacting a statute.<sup>192</sup> The aforementioned factors affect the USA and may not directly affect other countries such as EU member states, for instance.

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<sup>185</sup> Cecilia Malmström, Commissioner for Trade, European Commission, TTIP: What consumers have to gain 3 (Jan. 23, 2016), [http://trade.ec.europa.eu/doclib/docs/2016/january/tradoc\\_154173.pdf](http://trade.ec.europa.eu/doclib/docs/2016/january/tradoc_154173.pdf); MEETING MINUTES OF UNITED STATES—EUROPEAN COMMISSION, HIGH-LEVEL REGULATORY COOPERATION FORUM: 10<sup>TH</sup> MEETING [https://obamawhitehouse.archives.gov/sites/default/files/omb/oira/irc/hlref\\_summary\\_report\\_june\\_2011.pdf](https://obamawhitehouse.archives.gov/sites/default/files/omb/oira/irc/hlref_summary_report_june_2011.pdf) [hereinafter REGULATORY FORUM 10TH MEETING]

<sup>186</sup> Reeve T. Bull, *Developing a Domestic Framework for International Regulatory Cooperation*, 78 L. CONTEM. PROBS. 49, 55-56 (2015).

<sup>187</sup> *Id.* at 15.

<sup>188</sup> Donald A. Brown, *Superfund Cleanups, Ethics and Environmental Risk Assessment*, 16 B.C. ENVTL. AFF. L. REV. 181, 197 (1988).

<sup>189</sup> Joel D. Smith, *Massachusetts v. EPA: A Change of Climate at EPA Clouds the DC Circuit's Review of Risk-Based Policy Decisions*, 33 ECOL L.Q. 653, 664 (2006).

<sup>190</sup> Carl F. Cranor, *Science Courts, Evidentiary Procedures, and Mixed Science Policy Decisions*, 4 RISK: ISSUES IN HEALTH AND SAFETY 113, 126-28 (1993).

<sup>191</sup> CHARLES H. KOCH, 1 ADMINISTRATIVE LAW AND PRACTICE 39 (West Pub. Co., 1985).

<sup>192</sup> RICHARD PARKER & ALBERTO ALEMANNI, TOWARDS EFFECTIVE REGULATORY COOPERATION UNDER TTIP: A COMPARATIVE OVERVIEW OF THE EU AND US LEGISLATIVE & REGULATORY SYSTEMS 22-32 (2014).

Furthermore, the negotiating partners in close collaboration with the HLWG have identified five basic components that would allow TTIP to deal with issues relating to regulatory cooperation. First, a sanitary and phytosanitary (SPS) plus chapter will be included in TTIP in order to deal with regulations relating to SPS issues. The chapter aims to reinforce important WTO principles relating to SPS, such as the requirement that both the EU's and the USA's SPS measures be based on science and on international standards or scientific risk assessments and also be applied solely for the purpose of protecting human, animal, or plant life. The chapter will basically be an improved version of the WTO SPS Agreement. Secondly, a technical barrier to trade (TBT) plus chapter will be included in TTIP. The chapter aims to reduce unnecessary testing and inappropriate certification requirements, and also promote transparency and convergence in regulatory approaches. This chapter will basically be an improved version of the WTO Agreement on TBT. Thirdly, sectoral annexes would contain commitments for specific goods and the services sectors in order to reduce costs. Fourthly, TTIP will also adopt new methods of dealing with regulatory coherence that are cost-effective and more efficient in order to implement adequate regulations for goods and services. Finally, TTIP will include a structure that will identify opportunities for guiding future regulatory cooperation.<sup>193</sup> It should be noted that this structure is not final and may change at any point. However, the aforementioned components were closely followed during the first nine rounds of the TTIP negotiations.<sup>194</sup>

The process of aligning regulations on both sides of the Atlantic will consist of two phases. The first phase will involve important commitments in relation to the way states conduct national regulatory activities; more specifically, TTIP will require a broad domestic commitment to stakeholder consultation and impact assessments. The second phase involves the creation of new institutions and for that two scenarios were proposed. In the first scenario regulators in the EU and the USA will be expected to engage in a bilateral mechanism. This mechanism is initiated by way of request from a state party along with their stakeholders. Once the request is made, regulators will be expected to engage in a bilateral exchange with regard to the proposed policy activities. In the second scenario, TTIP is set to establish its very own institution which would consist of an expert body called the Regulatory Cooperation Council (RCC).<sup>195</sup> This novel mechanism will make TTIP an agreement that updates itself. The RCC will allow regulators to capitalise on opportunities to align regulatory approaches that achieve common objectives.<sup>196</sup>

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<sup>193</sup> *Working Group on Jobs*, *supra* note 11, at 4; *Fact Sheet: United States to Negotiate Transatlantic Trade and Investment Partnership with the European Union* (Feb. 13, 2013), <https://ustr.gov/about-us/policy-offices/press-office/fact-sheets/2013/february/US-EU-TTIP> (last visited Sept. 17, 2017).

<sup>194</sup> Alberto Alemanno, *The Regulatory Cooperation Chapter of the Transatlantic Trade and Investment Partnership: Institutional Structures and Democratic Consequences*, 18 J. OF INT'L ECON. L. 627 (Aug. 27, 2015).

<sup>195</sup> Marija Bartl, *TTIP's Regulatory Cooperation and The Politics of Learning*, SOCIAL EUROPE (Nov. 26, 2015), <http://www.social-europe.eu/2015/11/ttips-regulatory-cooperation-and-the-politics-of-learning/>.

<sup>196</sup> Lester & Barbee, *supra* note 19, at 865.

The extent of the powers of the RCC has not been clearly explained by the negotiating partners, but the latter assures that all those changes will not negatively affect the way states legislate on domestic rules and regulations. They affirm that the regulatory and legislative system of both the EU and the USA will not be altered. However, from a realistic point of view, the regulatory cooperation mechanism proposed in TTIP will unavoidably limit the regulatory autonomy of the negotiating partners.<sup>197</sup>

For instance, the way regulations are made in the EU are already changing. In May 2015, the Commission announced the launch of a new law-making process which requires that non-legislative procedures be subject to impact assessments. The aforementioned procedural modification appears to be the Commission's response to claims from the USA that the EU regulatory process lacks transparency and regulatory impact assessments. In this particular case, it is clear that the USA has had an influence on the EU's regulatory process. Whether or not TTIP is successfully negotiated and implemented, the way the EU regulates has already been subject to modifications. Hence, it is important that the Commission determines how such changes may affect the EU's mechanisms of democratic oversight and institutional balances.<sup>198</sup>

The regulatory chapter proposed in TTIP must focus on principles and practices such as transparency, quality impact assessments, stakeholder participation and most importantly the negotiating partners must make sure that the regulatory system in TTIP is a democratically accountable one.<sup>199</sup> This should not be complicated to draft as the EU and the USA have done this on two occasions. The first time was in 2002 with the *Guidelines on regulatory cooperation and transparency*<sup>200</sup>, and the second was in 2011 with the *High-Level Regulatory Cooperation Forum*.<sup>201</sup>

The negotiating partners are now focusing their efforts on a new chapter of regulatory cooperation named the horizontal regulatory cooperation chapter. The horizontal chapter will require that the EU and the USA's federal government exchange a list of planned legislative acts that will be evaluated in relation to their possible implications on transatlantic trade. The horizontal chapter would also consist of a Regulatory Cooperation Body (RCB) that would institutionalise stakeholders into the regulatory process.<sup>202</sup> It is suggested that the aforementioned

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<sup>197</sup> Alberto Alemanno, *The Transatlantic Trade and Investment Partnership (TTIP) and Parliamentary Regulatory Cooperation* 44-45 EUR. PARL. POL'Y. REP. (April 10, 2014), [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2423562](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2423562).

<sup>198</sup> Joana Mendes, *Regulatory Cooperation under TTIP: Democracy on this Side of the Bridge*, BLOGACTIVE.EU (Oct. 5, 2015), <https://acelg.blogactiv.eu/2015/10/05/regulatory-cooperation-under-ttip-democracy-on-this-side-of-the-bridge/>.

<sup>199</sup> Chase & Pelkmans, *supra* note 73, at 15.

<sup>200</sup> OFFICE OF MGMT. & BUDGET, GUIDELINES ON REGULATORY COOPERATION AND TRANSPARENCY (2002), <https://obamawhitehouse.archives.gov/sites/default/files/omb/oir/2002-guidelines-on-reg-coop-and-transparency.pdf>.

<sup>201</sup> REGULATORY FORUM 10TH MEETING, *supra* note 185.

<sup>202</sup> *Regulatory cooperation in TTIP Cutting red tape for EU firms –without cutting corners*, EUR. COMM'N (2015), [http://trade.ec.europa.eu/doclib/docs/2015/january/tradoc\\_153002.1%20RegCo.pdf](http://trade.ec.europa.eu/doclib/docs/2015/january/tradoc_153002.1%20RegCo.pdf).

procedures would trigger a regulatory chill, meaning that governments would back down from implementing new regulations that could threaten the interests of MNCs.<sup>203</sup> With such measures, the government in the USA and the governments of EU member states would not be able to regulate in the interest of the public as they would be at risk of legal actions from MNCs.<sup>204</sup>

Even though regulatory cooperation is a key component of TTIP, and the negotiating partners are putting a lot of effort to converge and unify their regulations and practices, they face four main challenges that might prevent them from achieving their goal. First, corporations are not satisfied with the way the negotiating partners have dealt with regulatory cooperation in the past. Corporations expect that TTIP will significantly align regulations across the Atlantic.<sup>205</sup> Secondly, civil society groups in the EU and the USA fear that the process of converging regulations will be used by corporations to weaken the significance of regulatory protections.<sup>206</sup> Thirdly, regulators and public interest groups are concerned about the fact that TTIP will add new requirements in relation to international consultation and trade impact analysis that will negatively impact regulatory processes.<sup>207</sup> Finally, due to the secrecy surrounding TTIP negotiations, the general public fear that regulatory convergence will lower standards both in the EU and in the USA.<sup>208</sup>

It is clear that regulatory convergence is a major issue for the negotiating partners. The method adopted by the EU and the USA to deal with this issue is certainly not the most effective. The vagueness surrounding the negotiation of the regulatory chapter in TTIP has exacerbated the concerns of civil society groups and the general public. The EU and the USA must come up with more convincing proposals and not just vague schemes such as the RCC. If the negotiating partners fail to properly resolve this issue, the potential gains from TTIP would be significantly lower than predicted.<sup>209</sup>

#### E. *The implications of an ISDS mechanism in TTIP*

The ISDS mechanism refers to an arbitration instrument that allows a foreign investor to bring a court action against a foreign government. The proceedings are

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<sup>203</sup> Martin Myant, *TTIP: What it will mean for us and what is the alternative?* 13 (Eur. Social Observatory, Working Paper No. 11, 2015), [http://www.ose.be/files/publication/OSEPaperSeries/Myant\\_2015\\_OSEBriefingPaper11\\_nov2015.pdf](http://www.ose.be/files/publication/OSEPaperSeries/Myant_2015_OSEBriefingPaper11_nov2015.pdf).

<sup>204</sup> Siles-Brügge & Butler, *supra* note 28.

<sup>205</sup> Chase & Pelkmans, *supra* note 73, at 12.

<sup>206</sup> Richard W. Parker, *Four Challenges for TTIP Regulatory Cooperation*, 22 COLUM. J. EUR. L. 6 (2016), [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2769528](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2769528).

<sup>207</sup> *TTIP: Regulatory cooperation is the ultimate tool to prevent or weaken future public interest standards for citizens, workers, consumers, and the environment*, HEALTH AND ENVIRONMENT ALLIANCE (2015), [https://corporateeurope.org/sites/default/files/statement\\_regulatory\\_cooperation\\_feb\\_2015\\_2.pdf](https://corporateeurope.org/sites/default/files/statement_regulatory_cooperation_feb_2015_2.pdf).

<sup>208</sup> Thomas B. Edsall, *Free Trade Disagreement*, N.Y. TIMES (Feb. 2, 2014), [http://www.nytimes.com/2014/02/05/opinion/edsall-free-trade-disagreement.html?\\_r=0](http://www.nytimes.com/2014/02/05/opinion/edsall-free-trade-disagreement.html?_r=0).

<sup>209</sup> Lester & Barbee, *supra* note 20, at 866-67.

usually conducted in an international private tribunal.<sup>210</sup> The proposed chapter on investment protection in TTIP has caused a lot of controversy due to the proposed inclusion of an ISDS mechanism which would settle disputes through international arbitration. The ISDS mechanism in TTIP would allow international investors to initiate legal proceedings against the state(s) they invested in for reasons such as unindemnified acquisition of their investments or discriminatory treatment.<sup>211</sup>

Proponents of TTIP argue that the agreement offers a unique chance for the EU and the USA to significantly reform the ISDS mechanism. They assert that by including an ISDS chapter in TTIP, the negotiating partners could more effectively protect foreign direct investments (FDI) against unjustifiable political interferences while at the same time not preventing the host state from regulating. Moreover, in order for the ISDS chapter proposed in TTIP to be fully effective it must be a binding, transparent and impartial system of arbitration that also includes an independent appellate body.<sup>212</sup>

A trade deal without an ISDS mechanism is unlikely to be approved by Congress in the USA and might even jeopardise the whole negotiation process of TTIP. Negotiators in the USA emphasise the fact that it is essential for a contemporary trade deal to have a viable protection mechanism for investors such as the ISDS mechanism. However, such a mechanism should in no case interfere in a state's domestic regulatory process.<sup>213</sup> On the European side, the European Commission has stated that in recent years ISDS mechanisms have occasioned litigation against governments such as the *Vattenfall* case in Germany<sup>214</sup>. Nevertheless, the Commission affirms that an ISDS chapter is very important in an agreement of that calibre as it would protect European investors from discrimination such as pork-barrel politics, favouritism and padded contracts when investing in the USA.<sup>215</sup>

The business community both in the EU and in the USA strongly supports the inclusion of an ISDS chapter in TTIP.<sup>216</sup> For instance, AmCham EU calls for

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<sup>210</sup> LISE JOHNSON, LISA SACHS, ET AL., INVESTOR-STATE DISPUTE SETTLEMENT, PUBLIC INTEREST AND U.S. DOMESTIC LAW 2 (Colom. Ctr. on Sustainable Inv., 2015), <http://ccsi.columbia.edu/files/2015/05/Investor-State-Dispute-Settlement-Public-Interest-and-U.S.-Domestic-Law-FINAL-May-19-8.pdf>.

<sup>211</sup> HUSSEIN HAERI & DAVID WALKER, CENTS AND SENSIBILITY: DISPUTING THE TTIP 2 (World Commerce Review, 2015), [http://www.worldcommercereview.com/publications/article\\_pdf/930](http://www.worldcommercereview.com/publications/article_pdf/930).

<sup>212</sup> Reinhard Quick, *Why TTIP Should Have an Investment Chapter Including ISDS*, 49 J. WORLD TRADE 199 (2015).

<sup>213</sup> Leif Johan Eliasson, *What is at Stake in the Transatlantic Trade and Investment Partnership (TTIP)? Assessing Challenges and Possible Compromises* 12 (Saar Expert Papers, Working Paper No. 2/2014, 2014), [http://jean-monnet-saar.eu/wp-content/uploads/2013/12/10\\_07\\_14\\_TTIP-Eliasson.pdf](http://jean-monnet-saar.eu/wp-content/uploads/2013/12/10_07_14_TTIP-Eliasson.pdf).

<sup>214</sup> *Vattenfall AB, Vattenfall Eur. AG., Vattenfall Eur. Generation AG v. Federal Republic of Germany*, ICSID Case No. ARB/09/6, Award (Mar. 11, 2011).

<sup>215</sup> Karel De Gucht, Trade Commissioner, EU, Statement on the launch of a public consultation on investment protection TTIP (Mar. 27, 2014), [http://europa.eu/rapid/press-release\\_STATEMENT-14-85\\_en.htm](http://europa.eu/rapid/press-release_STATEMENT-14-85_en.htm).

<sup>216</sup> CHRISTIANE GERSTETTER & NILS MEYER-OHLENDORF, INVESTOR-STATE DISPUTE SETTLEMENT UNDER TTIP – A RISK FOR ENVIRONMENTAL REGULATION? 18 (Ecologic Inst., 2013).

regulatory and legal certainty in TTIP's relation to investment.<sup>217</sup> In the same vein, Business Europe, a lobby group representing businesses in the EU, demands that a state-of-the-art ISDS mechanism is included in TTIP.<sup>218</sup> BDI, an organisation comprising leading German business associations, also supports an ISDS chapter in TTIP and points out that it is high time for an overall remodelling of the ISDS mechanism. The organisation indicates that while the ISDS chapter protects the interests of investors, it must also prevent frivolous claims, provide explicit definitions of important concepts and ensure that the proceedings are conducted in absolute transparency.<sup>219</sup>

The point of view of civil society groups in relation to an ISDS chapter in TTIP is the complete opposite of those of the business community. In 2013, more than 200 civil society organisations from both the EU and the USA signed a letter addressed to the former EU Trade Commissioner, Karl de Gucht, expressing their concerns about the proposed ISDS chapter in TTIP.<sup>220</sup>

In the letter, the civil society groups claimed that the ISDS mechanism proposed in TTIP will force states to use taxpayers' money to pay compensation to MNCs due to the implementation of policies that are in the interests of the public, such as better regulations on public health or environmental laws, but which may alter the plans of those MNCs to make more profit.<sup>221</sup> The civil society groups state that governments must not fear MNCs and implement any policy that is in the interests of the public.<sup>222</sup> Wallach supports this argument by stating that an ISDS mechanism constitutes an attack on domestic judicial systems as it permits companies to initiate legal actions against states outside the court system.<sup>223</sup> Furthermore, consumer groups in the USA are concerned about the fact that the ISDS chapter proposed in TTIP would provide more judicial rights and legal possibilities to foreign companies, therefore having a discriminatory effect on American companies.<sup>224</sup>

In an effort to justify the inclusion of an ISDS chapter in TTIP, the OECD argues that the risk for public health and environmental regulations arising from ISDS provisions should be balanced against the potential benefits that an ISDS chapter would bring. The OECD states that investors would be willing to invest in

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<sup>217</sup> AM. CHAMBER OF COMMERCE TO THE EUROPEAN UNION, AMCHAM EU'S REPLY TO USTR'S REQUEST FOR COMMENTS CONCERNING PROPOSED TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP 28 (2013).

<sup>218</sup> Markus J. Beyrer, BusinessEurope Director General, *A New Era for EU-US Trade* (Oct. 7, 2013), <https://www.business-europe.eu/sites/buseur/files/media/imported/2013-01044-E.pdf>.

<sup>219</sup> Schutzmechanismus gegen ungerechtfertigte Klagen BDI (2014), <http://bdi.eu/artikel/news/schutzmechanismus-gegen-ungerechtfertigte-klagen/>.

<sup>220</sup> GERSTETTER & MEYER-OHLENDORF, *supra* note 215, at 19.

<sup>221</sup> Philip Morris Asia Limited v. the Commonwealth of Australia, UNCITRAL, PCA Case No. 2012-12 (2012).

<sup>222</sup> SEATTLE TO BRUSSELS NETWORK, STATEMENT AGAINST INVESTOR PROTECTION IN TTIP, CETA, AND OTHER TRADE DEALS 2 (2016).

<sup>223</sup> Lori Wallach, Trade Agreements 101: Introduction for Consumer Organizations and Advocates as U.S.-EU TAFTA Negotiations Start (2013) (unpublished article).

<sup>224</sup> Andrew Erwin, *Trading away Democracy*, FOREIGN POLICY IN FOCUS (Mar. 21, 2014), <http://fpif.org/trading-away-democracy/>.

the EU and the USA as TTIP would provide a viable and efficient ISDS mechanism that would protect their rights and financial interests.<sup>225</sup> The ISDS mechanism has often been compared to an international court with no enforcement power but with the ability to exercise judicial control over the actions of states.<sup>226</sup> Bubrowski claims that another benefit of an ISDS chapter in TTIP is that governments would not have to worry anymore about taking actions on behalf of their investors vis-à-vis a host state.<sup>227</sup>

Those who are against an ISDS chapter in TTIP emphasise that apart from an ISDS mechanism, investors already have access to a plethora of dispute resolution mechanisms available to them such as conciliation or mediation. In cases where investors are concerned about political interferences, they have the ability to protect themselves by taking private insurance policies which will compensate them regardless of whether the host country is willing to cover damages. Investors can also rely on international institutions such as the Multilateral Investment Guarantee Agency (MIGA) to finance their legal proceedings.<sup>228</sup> It is argued that an ISDS mechanism in TTIP would privilege specific parts of society with disastrous effects for democratic politics. It appears that there is a missing balance in the ISDS mechanism which tends to favour the economic interest of foreign investors over the interest of domestic investors by providing foreign investors with specific rights that are not available to domestic investors.<sup>229</sup> Moreover, it is contended that the ISDS chapter in TTIP would have a negative effect on the EU. A probable political cost could be the fact that high-profile cases against EU member states could potentially incite controversy within national political systems. Litigation resolved through the ISDS mechanism may be the cause of public controversy more so if the litigation is perceived as a threat to the policy space of governments.<sup>230</sup>

Initially, the ISDS mechanism was created to protect the interests of investors against arbitrary decisions in host countries where there was little legal certainty. However, this is not the case for the EU and the USA as both have very solid legal systems. Added to that, both share various legal concepts and theories of law. The Commission promised that the proposed ISDS mechanism in TTIP had been amended in a lot of different ways in order to prevent any type of abuse and that it will in no case prevent governments from regulating on issues relating to public health, the environment, security and safety.<sup>231</sup> However, civil society groups

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<sup>225</sup> INVESTOR-STATE DISPUTE SETTLEMENT: PUBLIC CONSULTATION 21 (OECD, 2012), <http://www.oecd.org/investment/internationalinvestmentagreements/50291642.pdf>.

<sup>226</sup> ELVIRE FABRY & GIORGIO GARBASSO, *ISDS IN THE TTIP THE DEVIL IS IN THE DETAILS* 13 (Notre Europe, 2015).

<sup>227</sup> Helene Bubrowski, *Schiedsgerichte sind gerechter*, FRANKFURTER ALLGEMEINE ZEITUNG (Jan. 25, 2014, 4:32 PM), <http://www.faz.net/aktuell/politik/staat-und-recht/freihandelsabkommen-schiedsgerichte-sind-gerechter-12768294.html>.

<sup>228</sup> FABRY & GARBASSO, *supra* note 226.

<sup>229</sup> Thomas Dietz & Marius Dotzauer, *Political Dimensions of Investment Arbitration: ISDS and the TTIP Negotiations* 10-11 (Zentra Working Paper in Transnational Studies, Working Paper No. 48/2015, 2015), [http://papers.ssrn.com/sol3/Papers.cfm?abstract\\_id=2562916](http://papers.ssrn.com/sol3/Papers.cfm?abstract_id=2562916).

<sup>230</sup> Poulsen et al., *supra* note 75, at 17.

<sup>231</sup> EUROPEAN COMM'N, *INVESTMENT PROTECTION AND INVESTOR-TO-STATE DISPUTE SETTLEMENT IN EU AGREEMENTS* 7 (2013).

raised doubts about the fact that the ISDS mechanism proposed in TTIP would live up to the Commissions' promises.<sup>232</sup>

In an attempt to appease the concerns of the general public and civil society groups regarding the potential threat that an ISDS mechanism could pose on the right of governments to legislate in the interests of the public, the European Parliament (EP), in July 2015, recommended that the ISDS mechanism in TTIP be excluded from the agreement and replaced by a new system for resolving disputes between investors and states. The EP stated that the new dispute settlement system has to be subject to scrutiny and democratic principles. They stressed that the new dispute settlement system has to include an appellate body and most importantly it has to prevent the private interests of corporations from undermining public policy. The EP also stated that all proceedings have to be treated transparently by publicly appointed, independent judges.<sup>233</sup> Following the recommendation of the EP, the European Commission announced the Investment Court System (ICS) as a replacement for the ISDS mechanism. The Commission emphasised the fact that through the ICS, investors would be allowed to bring court actions against governments only in exceptional circumstances such as in cases of racial discrimination. The Commission also stated that the ICS will be composed of both a first instance tribunal and an appeal tribunal, and that the proceedings would be handled by publicly appointed judges.<sup>234</sup>

It is clear that the ICS proposed by the EU is more democratic than the former ISDS mechanism proposed in TTIP. Such an attack on democracy was simply unacceptable; a trade deal should in no case have provisions that could potentially threaten democracy. If implemented, the ICS will give the negotiating partners a unique chance of reshaping the way investor-state disputes are resolved. However, some academics argue that the ICS proposed by the EU will not garner sufficient political support from the U.S. Congress as the proposed ICS will make it very difficult for American investors to bring claims against EU member states.<sup>235</sup>

#### F. Public Procurement

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<sup>232</sup> Marika Armanovica & Roberto Bendini, *Civil Society's Concerns About the Transatlantic Trade and Investment Partnership* 13-14 (Directorate-General for External Policies, Working Paper No. DG EXPO/B/PolDep/Note/2014\_118, 2014), [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2516037](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2516037).

<sup>233</sup> Resolution of 8 July 2015 containing the European Parliament's recommendations to the European Commission on the negotiations for the Transatlantic Trade and Investment Partnership (TTIP), EUR. PARL. DOC. P8\_TA 15 (2015), <http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//NONSGML+TA+P8-TA-2015-0252+0+DOC+PDF+V0//EN>.

<sup>234</sup> Commission proposes new Investment Court System for TTIP and other EU trade and investment negotiations, EUROPEAN COMM'N (Sept. 16, 2015), [http://europa.eu/rapid/press-release\\_IP-15-5651\\_en.htm](http://europa.eu/rapid/press-release_IP-15-5651_en.htm).

<sup>235</sup> TRANSATLANTIC CONSUMER DIALOGUE, RESPONSE TO THE EUROPEAN COMMISSION'S INVESTOR-STATE DISPUTE SETTLEMENT "REFORM" PROPOSAL 1-2 (2016); AM. CHAMBER OF COMMERCE TO THE EUROPEAN UNION, *supra* note 216, at 3.

Public procurement refers to a procedure followed by public bodies when contracting with private companies for the procurement of goods and services.<sup>236</sup> Since the year 2000, the inclusion of public procurement provisions in bilateral trade agreements between the EU and third countries has considerably increased, it is therefore not surprising that a public procurement chapter is proposed in TTIP.<sup>237</sup>

The negotiations on the inclusion of a public procurement chapter in the TTIP has attracted a lot of controversy, mainly because the market for public contracts is very significant, approximately 15-20% of a country's GDP.<sup>238</sup> The European Commission affirms that 10-15% of the EU's financial gains from TTIP depend on greater access to the USA public procurement market.<sup>239</sup> Yet, some fear that the public procurement chapter might lead to the privatisation of important public services such as health care.<sup>240</sup>

Foreign firms can obtain public contracts through three modalities of procurement. The first modality is direct cross-border international procurement, whereby a foreign firm submits a bid overseas and wins a public contract from that country. Secondly, through commercial presence procurement, a domestic subsidiary of a foreign corporation can win public contracts. Finally, through value-added indirect international procurement a foreign firm may indirectly benefit from public contracts by supplying goods and services to a domestic or foreign firm that obtained the public contracts.<sup>241</sup> In 2014, two cases of public procurement made the headlines. The first one concerned the advertisement and award of a \$1.2 billion California High-Speed Rail Authority contract to a U.S. subsidiary of a Spanish firm.<sup>242</sup> The second concerned the advertisement and award of a £500 million Department for Work and Pensions contract to a U.S. company.<sup>243</sup>

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<sup>236</sup> ROBERT D. ANDERSON, ANNA CAROLINE MÜLLER ET AL., *Government Procurement Provisions in Regional Trade Agreements: A Stepping Stone to GPA Accession?*, in THE WTO REGIME ON GOVERNMENT PROCUREMENT: CHALLENGES AND REFORM 561-566 (Sue Arrowsmith & Robert D. Anderson eds., 2011).

<sup>237</sup> Lucian Cernat & Zornitsa Kutlina-Dimitrova, *International Public Procurement: From Scant Facts to Hard Data*, CHIEF ECONOMIST NOTE 6 (Apr. 2015).

<sup>238</sup> Asako Ueno, *Multilateralising Regionalism on Government Procurement* 7-8 (OECD Trade Paper, Working Paper No. 151, 2013), [http://www.oecd-ilibrary.org/trade/multilateralising-regionalism-on-government-procurement\\_5k4618vvq2np-en;jsessionid=22r7a9umw3qg4.x-oecd-live-02](http://www.oecd-ilibrary.org/trade/multilateralising-regionalism-on-government-procurement_5k4618vvq2np-en;jsessionid=22r7a9umw3qg4.x-oecd-live-02).

<sup>239</sup> Letter from EU Trade Commissioner Cecilia Malmström, Dep't. for Bus. Innovation and Skills, NHS and TTIP (Jan. 28, 2015) (available at [https://www.gov.uk/government/publications/nhs-and-ttip-letter-from-eu-trade-commissioner-cecilia-malmstrom](https://www.gov.uk/government/publications/nhs-and-ttip-letter-from-eu-trade-commissioner-cecilia-malmstrom/nhs-and-ttip-letter-from-eu-trade-commissioner-cecilia-malmstrom)).

<sup>240</sup> KHORANA, *supra* note 163, at 61.

<sup>241</sup> Cernat & Kutlina-Dimitrova, *supra* note 236, at 15.

<sup>242</sup> AFP, *Spain's ACS wins 1.2bn dollar high-speed train contract in US*, THE DAILY MAIL (Dec. 12, 2014), <http://www.dailymail.co.uk/wires/afp/article-2872221/Spains-ACS-wins-1-2bn-dollar-high-speed-train-contract-US.html>.

<sup>243</sup> Press Release, Department of Work and Pensions, MAXIMUS Appointed to Carry out Health Assessments for the Department for Work and Pensions (Oct. 30, 2014), available at <https://www.gov.uk/government/news/maximus-appointed-to-carry-out-health-assessments-for-the-department-for-work-and-pensions>.

Before engaging in a detailed discussion regarding the public procurement chapter proposed in TTIP, it is important to discuss the existing EU and the USA regulatory systems on public procurement and the WTO's Agreement on Government Procurement (GPA)<sup>244</sup> to appreciate the context within which the negotiations on this chapter are taking place.

### 1. Regulatory systems on public procurement

The EU's regulatory system on public procurement requires that contracts that are of sufficient cross-border interest should be procured as per the rules and principles of EU laws such as articles 28-37 and 56-62 of the Treaty on the Functioning of the European Union,<sup>245</sup> that aim to protect the four freedoms of the single market. Four core procedural directives, namely Public Procurement Directive 2014/24/EU,<sup>246</sup> the Utilities Directive 2014/25/EU,<sup>247</sup> the Concessions Directive 2014/23/EU,<sup>248</sup> and the Defence and Security Directive 2009/81/EC<sup>249</sup> regulate public procurement in the EU. <sup>250</sup>It should be noted that each of these directives are very complex and are supported by other directives which review procurement decisions and offer remedies in cases of breach of procurement law.<sup>251</sup>

In the U.S., the federal regulatory system on public procurement is governed by the Federal Acquisition Regulation (FAR).<sup>252</sup> As per 48 C.F.R. 2.101(b),<sup>253</sup> the rules and regulations of the FAR are also applicable to most executive branch agencies such as military and executive departments as well as independent establishments as stated in 5 U.S.C. 101, 102, and 104(1)<sup>254</sup> and also government owned corporations as defined in 31 U.S.C. 9101.<sup>255</sup> The objectives of public procurement regulations in the U.S. are very different from the ones that are in

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<sup>244</sup> AGREEMENT ON GOVERNMENT PROCUREMENT, Apr. 15, 1994, reprinted in OFFICE OF THE U.S. TRADE REPRESENTATIVE, URUGUAY ROUND OF MULTILATERAL TRADE NEGOTIATIONS GENERAL AGREEMENT ON TARIFF AND TRADE (1994).

<sup>245</sup> Consolidated Version of the Treaty on the Functioning of the European Union, arts. 28-37, 56-62, Oct. 26, 2012, 2012 O.J. (C 326) 13-16, 24-25.

<sup>246</sup> Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on Public Procurement and Repealing Directive 2004/18/EC Text with EEA Relevance, 2014 O.J. (L 94) 65.

<sup>247</sup> Directive 2014/25/EU of the European Parliament and of the Council of 26 February 2014 on Procurement by Entities Operating in the Water, Energy, Transport and Postal Services Sectors and Repealing Directive 2004/17/EC Text with EEA Relevance, 2014 O.J. (L 94) 243.

<sup>248</sup> Directive 2014/23/EU of the European Parliament and of the Council of 26 February 2014 on the Award of Concession Contracts Text with EEA Relevance, 2014 O.J. (L 94) 1.

<sup>249</sup> Directive 2009/81/EC of the European Parliament and of the Council of 13 July 2009 on the Coordination of Procedures for the Award of Certain Works Contracts, Supply Contracts and Service Contracts by Contracting Authorities or Entities in the Fields of Defence and Security, and Amending Directives 2004/17/EC and 2004/18/EC (Text with EEA relevance), 2009 O.J. (L 216) 76.

<sup>250</sup> *New Rules on Public Contracts and Concessions: Simpler and More Flexible*, at 7, COM (2014) 45535 final (2014) [hereinafter *New Rules*].

<sup>251</sup> KHORANA, *supra* note 163, at 63.

<sup>252</sup> *Id.*

<sup>253</sup> 48 C.F.R. § 2.101(b) (1985).

<sup>254</sup> 5 U.S.C. §§ 101, 102, 104(1) (2012).

<sup>255</sup> 31 U.S.C. § 9101 (2012).

force in the EU. In the U.S., the FAR, for instance, affirms that its aim is to satisfy customers to the fullest by making sure that the products and services that are proposed to them are of the highest standard while at the same time ensuring that public policy objectives are successfully fulfilled.<sup>256</sup> The USA's public procurement regulatory system is as complicated as the EU's with its numerous supplementing statutes and exemptions. Added to that, each of the fifty U.S. states is responsible for drafting their own rules which makes this system even more complex as rules and regulations vary from state to state.<sup>257</sup>

The GPA is a plurilateral agreement that regulates market access in public procurement between the EU and the USA. Being a plurilateral agreement the GPA does not concern every member state of the WTO. Only members that chose to sign up are concerned with the agreement. The EU has had a very important role in the development of the GPA rules<sup>258</sup> and therefore the GPA rules are based on general EU law principles such as fairness, transparency, and non-discrimination.<sup>259</sup> It should be noted that annexes to the GPA are very important as they specify to "each signatory state, the extent of the agreement's coverage concerning construction, goods, services, sub-central government entities, central government entities and financial thresholds."<sup>260</sup>

## 2. Objectives and issues

Through the public procurement chapter proposed in TTIP, the European Commission aims to negotiate GPA-plus provisions with the USA.<sup>261</sup> The GPA-plus provisions would consist of improved GPA rules that would deal with contemporary issues that were previously not included in earlier versions of the GPA rules, such as environmental procurement and procurement via public-private partnerships, and most importantly improved coverage of market access rules to the public sector in the USA.<sup>262</sup> The negotiating partners may also possibly add more details to existing GPA provisions, more specifically with regard to technical specifications, qualification, short listing and award of public contracts.<sup>263</sup>

The main issue for the EU is to successfully negotiate the further opening of the USA's public procurement market. The EU is ready to open up to 15% GDP of its' public procurement market to the USA under the GPA. Currently, only 3.2%

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<sup>256</sup> 48 C.F.R. § 1.102(a) (1985).

<sup>257</sup> KHORANA, *supra* note 163, at 63-64.

<sup>258</sup> *Id.* at 64.

<sup>259</sup> WORLD TRADE ORGANISATION, *supra* note 244, art. IV.

<sup>260</sup> KHORANA, *supra* note 163, at 64.

<sup>261</sup> EUROPEAN COMMISSION, *supra* note 250, at 8.

<sup>262</sup> Richard Craven, *EU-US Transatlantic Trade and Investment Partnership Agreement: The European Commission's Negotiating Position on Public Procurement*, 3 PUB. PROC. L. REV. NA63, NA65-76 (2014).

<sup>263</sup> KHORANA, *supra* note 163, at 64.

GDP of the USA's public procurement market is open to the EU.<sup>264</sup> The discrepancy is significant and as mentioned above 10-15% of the EU's potential gains from TTIP depend on more access to the USA's public procurement market.<sup>265</sup> It is therefore clear that if the USA does not make serious compromises and give the EU greater access to its procurement market, the significance of TTIP for the EU would be seriously diminished.<sup>266</sup>

On the American side, the concerns are very different. The USA is mainly concerned about the way public procurement is practiced in certain EU member states. In a 2015 report, the Office of the US Trade Representative stated that there are a number of issues relating to discrimination, transparency and corruption in Portugal, Romania, Lithuania, Poland, France, Italy, Hungary, Greece, the Czech Republic and Bulgaria. The USA fears that American firms would be subjected to discrimination in relation to the acquisition of public contracts in the aforementioned member states.<sup>267</sup> The report also indicates that the EU proposed a set of regulations establishing new rules on the access of third country goods and services in the EU.<sup>268</sup> The proposed regulations are a response to the reluctance of the USA to give the EU greater access to its public procurement market. The measures proposed by the EU might have a negative impact on US firms willing to do business in the EU as such measures are clearly restrictive and protectionist.<sup>269</sup> However, some academics argue that USA firms will still be able to reap significant gains from the EU procurement market even with new procurement rules, provided that they are not too restrictive.<sup>270</sup>

## II. THE IMPACT OF TTIP ON THE INTERNATIONAL TRADING SYSTEM AND DEVELOPING COUNTRIES

### A. *The impact of TTIP on the international trading system*

For many years, the multilateral trading system has facilitated unparalleled economic growth for both OECD countries and emerging economies making it possible for millions of people to get out of poverty. Even though everything was

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<sup>264</sup> European Comm'n, *Trade and Investment Barriers Report 2011: Engaging our strategic economic partners on improved market access: priorities for action on breaking down barriers to trade* 2-10 (2011), [http://trade.ec.europa.eu/doclib/docs/2011/march/tradoc\\_147630.pdf](http://trade.ec.europa.eu/doclib/docs/2011/march/tradoc_147630.pdf).

<sup>265</sup> EUROPEAN UNION SUBCOMMITTEE ON EXTERNAL AFFAIRS: TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP WRITTEN EVIDENCE VOLUME, 2013-14, HL 179, <https://www.parliament.uk/documents/lords-committees/eu-sub-com-c/TTIP/TTIPwrittenevidencevolumeFINAL.pdf>.

<sup>266</sup> THE TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP: EUROPEAN UNION COMMITTEE, H.L. REP. NO. 2, 128 (2014), <http://www.parliament.uk/documents/The-Transatlantic-Trade-and-Investment-Partnership.pdf>.

<sup>267</sup> AMBASSADOR MICHAEL B.G. FROMAN, *2015 National Trade Estimate Report on Foreign Trade Barriers*, 144-46 (2015) <https://ustr.gov/sites/default/files/2015%20NTE%20Combined.pdf>.

<sup>268</sup> *Id.* at 144.

<sup>269</sup> KHORANA, *supra* note 163, at 68-69.

<sup>270</sup> LUCIAN CERNAT & ZORNITSA KUTLINA-DIMITROVA, *TTIP and Public Procurement: Going Beyond the tip of the iceberg*, 339 CEPS POL'Y BRIEF 1, 6 (2016).

not perfect, the multilateral trading system did more good than harm. In the 1990s, the end of the cold war and the establishment of the WTO was the signal that economically advanced nations and emerging economies were ready to cooperate. Unfortunately, only a decade after the establishment of the WTO, the willingness to cooperate declined very rapidly, and similar to the 1930s the global economy, is now divided into blocs.<sup>271</sup> The negotiations of recent mega-regional trade agreements such as TTIP, TPP and the Regional Comprehensive Economic Partnership (RCEP) have reshaped the way preferential trade agreements (PTAs) are negotiated and in the process questioned the relevance of the WTO and the significance of multilateralism.<sup>272</sup> It was the incompetence of the WTO that caused the existence of such mega-regional trade agreements.<sup>273</sup>

As previously stated, the main objective of TTIP is to reduce trade barriers, harmonise regulations between the EU and the USA and be a rule-setter for the 21<sup>st</sup> century.<sup>274</sup> In 2013, the former European Trade Commissioner made it clear that through TTIP the EU and USA aim to be the leaders in the development of global norms and standards.<sup>275</sup> TTIP might be the last chance for the EU and the USA to establish international trade rules and have a major impact on the international trading system.<sup>276</sup> Critics of the trade deal claim that TTIP is a power struggle of western societies who are desperately trying to re-assert their position in an increasingly competitive world.<sup>277</sup> Geopolitical rivalry may lead to divergences and significantly reduce trade flows between countries or groups of countries.<sup>278</sup> It is suggested that due to TTIP other regions might align their own regulations in order to compete with the EU and the USA and thus abandon the multilateral approach promoted by the WTO to the benefit of a bilateral preferential approach. This could possibly have a negative effect on many low-income developing countries, which are protected by WTO rules.<sup>279</sup>

In order for the WTO to have relevance two things must be done. First, it must focus on the reduction of tariffs internationally and principles such as transparency

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<sup>271</sup> Heribert Dieter, *The Return of Geopolitics Trade Policy in the Era of TTIP and TPP*, 3 (2014).

<sup>272</sup> Akman et al., *supra* note 32, at 13-15.

<sup>273</sup> Gabriel Siles-Brugge, *Global Trade Politics and the Transatlantic Trade and Investment Partnership*, E-INT'L RELATIONS (2016), <http://www.e-ir.info/2014/05/05/global-trade-politics-and-the-transatlantic-trade-and-investment-partnership/>.

<sup>274</sup> Peter van Hamm, *The Geopolitics of TTIP*, CLINGENDAEL POL'Y BRIEF 1-2 (2013), <https://www.clingendael.nl/sites/default/files/The%20Geopolitics%20of%20TTIP%20-%20Clingendael%20Policy%20Brief.pdf>.

<sup>275</sup> Gucht, *supra* note 215.

<sup>276</sup> Dennis Novy, *TTIP has the Potential to be a Forum Which sets 21st Century Trade Rules, but it Needs more Attention and Support from the Highest Levels of Government*, EUR. POL. & POL'Y (2014), <http://blogs.lse.ac.uk/europpblog/2014/07/22/tip-has-the-potential-to-be-a-forum-which-sets-21st-century-trade-rules-but-needs-more-attention-and-support-from-the-highest-levels-of-government/>.

<sup>277</sup> *TTIP, TPP and the Rise of Mega-Regionals: Consequences for the World Trading System*, FRIEDRICH EBERTS STIFTUNG SYMPOSIUM AND PANEL DISCUSSION 1 (2015).

<sup>278</sup> Akman et al., *supra* note 32, at 13-14.

<sup>279</sup> FERNANDO PERREAU DE PINNINCK, *IMPACT OF TTIP ON OTHER COUNTRIES AND THE INTERNATIONAL TRADING SYSTEM* (2015).

and national treatment which all 162 WTO members usually agree upon.<sup>280</sup> Secondly, the organisation has to open its very successful dispute settlement body to regional and bilateral trade agreements, especially those being negotiated by developing countries such as the RCEP.<sup>281</sup>

Proponents of the trade deal assert that TTIP, compared to first-generation free trade agreements (FTAs) will not constitute a threat to the multilateral trading system but instead force everyone to re-think the functioning of the WTO.<sup>282</sup> Some academics argue that the WTO is the victim of its own success, as the organisation has very successfully dealt with the lowering of tariffs, encouraging the EU and the USA to pursue negotiations on the elimination of regulatory barriers. In light of the aforementioned argument, it can be said that through TTIP the EU and the USA are only following the trend paved by the WTO.<sup>283</sup> It is contended that the negotiation of deep PTAs such as TTIP will in no case deter the influence of the WTO. Instead of labelling FTAs and PTAs as detrimental to the multilateral system, it would be better if a new type of division of labour was created between FTAs and the WTO.<sup>284</sup> Since 1995, the rules that dictate international trade have not been significantly updated even though the way business is done now has changed considerably. Supporters of TTIP argue that the EU and the USA should not miss the opportunity to free up trade across the Atlantic just because the WTO has issues adapting to novel ways of doing business, new technologies that are reshaping international commerce and the rise of new economic giants such as China and India.<sup>285</sup> Moreover, proponents of the EU-USA trade deal argue that TTIP is the only way for the negotiating partners to deal with the global deadlock that was occasioned by the lack of progress in the Doha round.<sup>286</sup>

Even though a number of academics believe that TTIP would be beneficial to the global trading system, others tend to believe that the contrary is more likely to happen. The ability of TTIP to create new global standards is limited. In fact, the trade deal might be a threat to the promotion of higher standards in relation to the environment or civil societies. Detractors of TTIP claim that the EU and the USA are not trying to improve the global trading system and promote multilateralism and globalisation, but instead they are doing everything to secure global market shares. Weinhardt and Bohnenberger argue that by promoting TTIP, the EU and the

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<sup>280</sup> Joost Pauwelyn, *New Trade Politics for the 21st Century*, 11 J. INT'L ECON. L. 559, 567 (2008), <http://jiel.oxfordjournals.org/content/11/3/559.abstract>.

<sup>281</sup> Hufbauer & Cimino-Isaac, *supra* note 30, at 681.

<sup>282</sup> Pauwelyn, *supra* note 279.

<sup>283</sup> Petros C. Mavroidis, *Dealing With PTAs in the WTO: Falling Through the Cracks Between 'Judicialization' and 'Legalization'*, 14 WORLD TRADE REV. 107, 114 (2015), <http://journals.cambridge.org/action/displayAbstract?fromPage=online&aid=9813900>.

<sup>284</sup> Pauwelyn, *supra* note 280, at 567.

<sup>285</sup> Katinka Barysch & Michael Heise, *Will TTIP Harm the Global Trading System?*, YALEGLOBAL ONLINE (2014), <http://yaleglobal.yale.edu/content/will-ttip-harm-global-trading-system>.

<sup>286</sup> Bernard Hoekman, *The WTO won't be killed by all these regional trade deals*, FRIENDS OF EUROPE (Oct. 4, 2016), <http://www.friendsofeurope.org/global-europe/why-the-wto-wont-be-killed-by-all-these-regional-trade-deals>.

USA are clearly rejecting the WTO and dissociating themselves with multilateralism.<sup>287</sup>

In an attempt to predict the effects of TTIP on the global trading system, Draper formulated three scenarios; namely building blocks, stumbling blocks and crumbling blocks. The building blocks scenario is a utopia. In this scenario TTIP is successfully negotiated, the concerns of developing countries are addressed and trade and investment are liberalised in a morally acceptable way. In relation to the regulatory agenda of TTIP, the negotiating partners decide to incorporate it into the WTO through inclusive plurilateral arrangements based on the Special and Differential Treatment provisions of the WTO Trade Facilitation Agreement, which is a set of GATT provisions that exempts developing countries and least developed countries from stringent WTO trade rules imposed on developed countries. For example, through the aforementioned provisions, developing countries and least developed countries are given longer time periods to implement agreements and commitments.<sup>288</sup>

Out of the three, stumbling blocks is the most realistic scenario. The author predicts that the primacy of the EU and the USA in the international trading system will not be completely reinstated giving rise to leadership ambiguity which will potentially have a negative effect for the EU and the USA in the long run, as it may give rising powers such as China or India the opportunity to gain the leadership of the international trading system. Faced with the waves of criticism and public outrage on specific chapters of TTIP, the negotiating partners will have to make a number of compromises. However, the efforts of the EU and the USA would be enough to persuade developing countries, especially India and China, to converge with the outcomes of TTIP. Finally, the highly probable crumbling blocks scenario, suggests that the negotiation rounds of TTIP could go on for years just like it is the case for the Doha rounds. If this scenario becomes a reality, the primacy of the EU and the USA in the international trading system would be jeopardised and would probably be beneficial to China's and India's accession to the position of leaders in the sphere of international trade.<sup>289</sup>

It is clear that the future of the WTO looks bleak and uncertain. The organisation is in the middle of fierce power struggles between the West and the East that will certainly last for decades and occasion further distortions in the global trading system. It is not possible to give a definitive verdict on the fate of the WTO as the negotiation rounds of TTIP has not concluded.<sup>290</sup>

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<sup>287</sup> Clara Weinhardt & Fabian Bohnenberger, *TTIP vs. WTO: Who Sets Global Standards?*, EURACTIV (Oct. 4, 2016), <http://www.euractiv.com/section/sustainable-dev/opinion/ttip-vs-wto-who-sets-global-standards/>.

<sup>288</sup> Trade & Development Committee, *Special and Differential Treatment Provisions*, WORLD TRADE ORGANIZATION (Oct. 18, 2016), [https://www.wto.org/english/tratop\\_e/devl\\_e/dev\\_special\\_differential\\_provisions\\_e.htm](https://www.wto.org/english/tratop_e/devl_e/dev_special_differential_provisions_e.htm).

<sup>289</sup> Peter Draper, *What is the future of the WTO?*, WORLD ECONOMIC FORUM (Sept. 15, 2015), <https://www.weforum.org/agenda/2015/09/how-can-the-wto-remain-relevant/>.

<sup>290</sup> *Id.*

## B. *The impact of TTIP on developing countries*

### 1. The removal of tariff barriers

The removal of tariff barriers proposed in TTIP will have some positive and negative effects on developing countries. It is contended that the growth and economic activity generated by the liberalisation of trade between the negotiating partners might potentially have a positive effect on developing countries. As the EU and the USA would experience more economic activity, the demand for goods produced by developing countries will most likely increase, thus boosting their economies.<sup>291</sup> However, the aforementioned will only be possible if the negotiating partners do not adopt an excessively restrictive approach with regard to rules of origin. The negotiating partners should refrain from using rules of origin where possible, as this could potentially result in a drastic decline of exports for developing countries, having a significantly negative impact on those countries' economies.<sup>292</sup> For example, Chinese exports would experience a significant decline amounting to approximately \$110 billion if restrictive rules were in place.<sup>293</sup> Another issue that may arise is that the removal of tariffs would make the negotiating partners' exports very competitive and therefore the EU and the USA would be in direct competition with developing countries causing a decline in the exports of those countries and reducing their overall share of world trade.<sup>294</sup> For instance, because of the removal of tariffs between the negotiating partners, Germany's imports from BRICS nations would potentially experience a decline, as Germany would rather import from the USA as American companies would become more competitive since tariffs would be removed.<sup>295</sup> If this happens, the advantages that developing countries obtain through a number of trade preferences schemes would be considerably reduced.<sup>296</sup> It should be noted that the aforementioned only concerns goods that can be manufactured in the EU and the USA.<sup>297</sup>

### 2. The reduction of NTBs

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<sup>291</sup> Manuel Manrique Gil, Marika Lerch, et al., *The TTIP's Potential Impact on Developing Countries: A Review of Existing Literature and Selected Issues*, EUR. PARL. 7 (Apr. 29, 2015), [http://www.europarl.europa.eu/RegData/etudes/IDAN/2015/549035/EXPO\\_IDA\(2015\)549035\\_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/IDAN/2015/549035/EXPO_IDA(2015)549035_EN.pdf).

<sup>292</sup> Axel Berger & Clara Brandi, *What Should Development Policy Actors Do About the Transatlantic Trade and Investment Partnership (TTIP)?*, GERMAN DEV. INST. 3 (2015), <https://www.die-gdi.de/uploads/media/BP1.2015.pdf>.

<sup>293</sup> Thieß Peterse, *Economic Consequences of a TTIP for Asia*, BERTELSMANN STIFTUNG 3-5 (2013) [https://www.bertelsmann-stiftung.de/fileadmin/files/user\\_upload/Asia\\_Policy\\_Brief\\_2013\\_05\\_e.pdf](https://www.bertelsmann-stiftung.de/fileadmin/files/user_upload/Asia_Policy_Brief_2013_05_e.pdf).

<sup>294</sup> Thorstensen & Ferraz, *supra* note 81.

<sup>295</sup> Felbermayr, et al., *supra* note 85.

<sup>296</sup> Kimberly Ann Elliott, *How Much "Mega" in the Mega-Regional TPP and TTIP: Implications for Developing Countries*, CTR. FOR GLOBAL DEV. 17 (2016), <http://www.cgdev.org/publication/how-much-mega-regional-tpp-and-ttip-implications-developing-countries>.

<sup>297</sup> Manrique Gil, et al., *supra* note 291, at 8.

The reduction of NTBs between the negotiating partners could potentially have a positive and also a negative effect on developing countries. The measures regarding NTBs proposed in TTIP would possibly enable developing countries to export to the EU and the USA by fulfilling compliance export procedures for only one country instead of doing the same thing twice, thus significantly reducing costs. However, in order for developing countries to benefit from that, the negotiating partners must explicitly include a section in TTIP that extends the principle of mutual recognition to third parties.<sup>298</sup> The removal of NTBs between the negotiating partners could lead to higher standards. If that is the case, developing countries would be required to adjust to the new standards imposed by TTIP which would most probably be very costly, and therefore be out of reach to poorer countries.<sup>299</sup>

### *C. The impact of TTIP on BRICS nations*

It is obvious that TTIP is a significant issue for BRICS nations. If the EU-US trade deal is successfully negotiated, BRICS countries would most certainly lose their newly gained influence in the sphere of international trade and geopolitics. For instance, as mentioned earlier, TTIP has the potential to jeopardise Russia's ambitions to establish a Eurasian Union. It is clear that if TTIP succeeds, the Eurasian economic and political landscape will be subject to some significant changes. The trade deal will most probably have a positive effect on the economic growth in Eastern Europe and thus potentially deter the influence of Russia in countries such as Belarus, Ukraine and Moldova. Added to that, the Russian economic model which mainly constitutes the gathering and distribution of natural resources and bureaucratic rents cannot rival the economic model proposed by the EU and the USA through TTIP, which promotes mutual benefits and a rule based framework for international cooperation.<sup>300</sup>

Faced with this harsh reality, the BRICS economies will have to act accordingly in order to maintain a position of power. The BRICS countries have two options that may help them not lose momentum even if TTIP succeeds. First, they could form an alliance with Latin American, African and Asian developing countries with the aim of reviving the WTO and promoting multilateralism. However, this is unlikely to happen as the BRICS nation's foreign economic policies are not totally unified. Secondly, faced with a fragmented multilateral trading system and a reluctance to cooperate, the BRICS economies might individually focus on their own political ambitions, which would inevitably lead to future alliances. This option is obviously less optimistic but is probably the most realistic one.<sup>301</sup>

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<sup>298</sup> Sinan Ülgen, *Locked In or Left Out? Transatlantic Trade Beyond Brussels and Washington*, CARNEGIE EUR. 11-12 (June 2014), [http://carnegieendowment.org/files/locked\\_in\\_left\\_out\\_ttip.pdf](http://carnegieendowment.org/files/locked_in_left_out_ttip.pdf).

<sup>299</sup> Manrique Gil, et al., *supra* note 291, at 9.

<sup>300</sup> Daniel S. Hamilton, *The Geopolitics of TTIP: Repositioning the Transatlantic Relationship for a Changing World*. CTR. FOR TRANSATLANTIC REL. 56 (Daniel S. Hamilton ed. 2014).

<sup>301</sup> Dieter, *supra* note 271.

Since TTIP was announced, a number of scholars and other commentators have argued that the trade deal is an attempt by the EU and USA to isolate the BRICS economies, especially China, from the international trading system in order to weaken their influence.<sup>302</sup> However, some academics argue that the economic relationship between BRICS nations such as China and the transatlantic partners prove that the EU and the USA show a lot of interest in engaging rising powers instead of attempting to marginalise them.<sup>303</sup>

Through TTIP, the EU and the USA might have an opportunity to expand the coverage of their regulations and standards, especially in relation to health and food safety, to the BRICS economies.<sup>304</sup> If the trade deal is successfully negotiated, the EU and the USA would be able to enter into trade talks with BRICS economies as one single entity instead of two separate blocs. Through TTIP, the EU and the USA have more chances of convincing the BRICS economies of implementing stricter regulations and standards with regard to health and food safety.<sup>305</sup>

#### *D. The impact of TTIP on the Asian continent*

TTIP would indirectly impose a number of constraints on the Asian continent.<sup>306</sup> As mentioned earlier, one of the main objectives of TTIP is to harmonise regulations and standards between the EU and the USA. If TTIP succeeds, every product that would be imported to the EU and the USA will have to satisfy new requirements. This would certainly be a real concern for Asian firms, as they would have to rapidly switch their manufacturing processes in order to be in line with TTIP regulations and standards. It is almost certain that TTIP standards and regulations will be very different from Asian domestic standards and therefore Asian firms would have to choose between manufacturing two sets of products, one which satisfies TTIP norms and another for the rest of the world or completely change their standards to be in line with TTIP. It is obvious that most Asian countries would rather adapt to the new EU-USA standards as manufacturing two sets of products would significantly increase their production costs.<sup>307</sup> In 2015, the IFO Institute for Economic Research published a study on the impact of TTIP on developing countries. The study states that Southeast Asia would be the region that would suffer most from TTIP, mainly because the region would lose its competitiveness as tariffs between the EU and the USA would be reduced, but

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<sup>302</sup> Alan Winters, *The Problem with TTIP*, VOX: EU (May 22, 2014), <http://voxeu.org/article/problem-ttip>.

<sup>303</sup> Daniel Hamilton, *TTIP: What Are the Implications for Emerging Powers and the International Order*, 3 BRIDGES AFRICA 10 (Dec. 1, 2014), <http://www.ictsd.org/bridges-news/bridges-africa/news/ttip-what-are-the-implications-for-emerging-powers-and-the>.

<sup>304</sup> Keller & Drechsel, *supra* note 33.

<sup>305</sup> Offik, *supra* note 34.

<sup>306</sup> Buhara Aslan, Merve Mavus Kutuk, et al., *Transatlantic Trade and Investment Partnership and Trans-Pacific Partnership: Policy Options of China*, 23 CHINA & WORLD ECON. 34-35 (2015).

<sup>307</sup> Elms, *supra* note 31.

tariffs for the region would remain unchanged.<sup>308</sup> However, some academics argue that harmonised rules and regulations between the EU and the USA might be beneficial for the Asian continent as the high costs associated with compliance to two different sets of regulations would be reduced, provided that the negotiating partners include a provision in TTIP that allows Asian exporters to benefit from that.<sup>309</sup>

#### *E. The impact of TTIP on the African continent*

If TTIP is successfully negotiated it could potentially have a negative impact on the African continent in three different ways; namely through trade diversion effects, the harmonisation of standards and rules of origin. The potential trade diversion effects occasioned by TTIP might have a negative impact on African nations as it would potentially complicate the process of goods and services that are exported to the EU and the USA from African countries. The elimination of tariffs and NTBs between the EU and the USA proposed in TTIP will have a negative effect on African countries as the barriers to market access for African exporters to the EU and the USA would increase significantly. The fact that TTIP would provide preferences to European firms exporting to the USA and vice-versa will seriously undermine African countries preferential access to the European and American market.<sup>310</sup>

The harmonisation of standards proposed in TTIP will possibly have an adverse effect on poorer African nations as higher standards would potentially marginalise African exporters, as it would be very difficult for them to comply with and implement the new and costly TTIP standards. Moreover, higher standards in the field of intellectual property rights might have an adverse effect on the production and supply of generic drugs to poorer African countries.<sup>311</sup>

The inflexible rules of origin proposed in TTIP would also make it more difficult for African nations that would like to evolve from producers of primary goods to manufacturers of finished products. For instance, under the rules of origin chapter proposed in TTIP, countries such as Ethiopia would have trouble exporting processed goods to the EU and the USA. The rules of origin chapter requires that at least 50% of the value added product has to be manufactured in the EU or the USA in order to benefit from tariff reductions. Therefore, if Ethiopia manufactures ready

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<sup>308</sup> Gabriel Felbermayr, Wilhelm Kohler, et al., *Potential Impact of the Transatlantic Trade and Investment Partnership (TTIP) on Developing and Emerging Countries*, IFO INSTITUT (Jan. 21, 2015), [http://www.cesifogroup.de/portal/page/portal/DocBase\\_Service/studien/studie-summary-2015-ttip-felbermayr.pdf](http://www.cesifogroup.de/portal/page/portal/DocBase_Service/studien/studie-summary-2015-ttip-felbermayr.pdf).

<sup>309</sup> Joakim Reiter, *The Effects of TTIP on Developing Countries*, CATO 4 (Jan. 2015), <http://www.cato.org/publications/cato-online-forum/effects-ttip-developing-countries>.

<sup>310</sup> Herfkens, *supra* note 82.

<sup>311</sup> Eveline Herfkens, *The Impact of TTIP on Sub-Saharan Africa* (2015), <http://www.queries-feeps.eu/the-impact-of-ttip-on-sub-saharan-africa/>.

to drink coffee by itself the country would not be able to export its ready to drink coffee to the EU and the USA under the stringent TTIP rules of origin.<sup>312</sup>

To conclude, the negotiating partners have to minimise the negative effects of TTIP on African nations as that would most certainly exacerbate poverty in this part of the world. The EU and the USA should consider extending their mutual recognition of standards to African countries and make the rules of origin less stringent. By doing so, the negative effects of trade diversion on African countries would be reduced and the transatlantic partners would prove to the detractors of TTIP that the trade deal is still committed to an open and equitable global trading system.<sup>313</sup>

### CONCLUSION

One of the negotiating partners' biggest mistakes was to set the completion date for TTIP negotiations by 2014. It was simply impossible for negotiators to successfully conclude negotiations in such a limited time frame. It appears that the EU and the USA were trying to hastily conclude the trade deal without taking into consideration the numerous implications of a trade agreement of that calibre. The unrealistic timetable set for the negotiation rounds has seriously undermined the credibility of the trade partnership and undoubtedly accentuated public concerns.<sup>314</sup>

Instead of trying to negotiate all the different chapters proposed in TTIP simultaneously, the negotiating partners should adopt a step by step approach which would consist of dealing with each chapter individually. This approach would give a reasonable deadline for the completion of the negotiation process of each chapter. The step by step approach would also divide the chapters into two categories: most important and least important. Categorising the chapters is an essential step towards a successful conclusion of the trade deal. Only then would the negotiating partners be able to identify what chapters would be most difficult to deal with and how much time it would take to successfully conclude the agreement.<sup>315</sup> A similar approach was proposed by Baker and Workman.<sup>316</sup> The authors based their study on a pool of trade experts both in the EU and the USA, who were requested to list a series of TTIP issues and classify them from most important to least important and then classify those same issues from most difficult to least difficult to resolve. The data obtained from the trade experts was then plotted on a graph. The degree of importance was tracked along the horizontal axis and the level of difficulty was tracked along the vertical axis. The graph (figure 1)

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<sup>312</sup> Hilke Fischer, *TTIP Talks - Africa Remains Left Out*, DEUTSCHE WELLE (Feb. 6, 2015), <http://www.dw.com/en/ttip-talks-africa-remains-left-out/a-18241309>.

<sup>313</sup> Philani Mthembu, *A Transatlantic Partnership with Ripples Across the Oceans: What Does Africa Stand to Gain or Lose?*, AFR. DEV. BANK GROUP (June 18, 2015), <http://www.afdb.org/en/blogs/integrating-africa/post/a-transatlantic-partnership-with-ripples-across-the-oceans-what-does-africa-stand-to-gain-or-lose-14442/>.

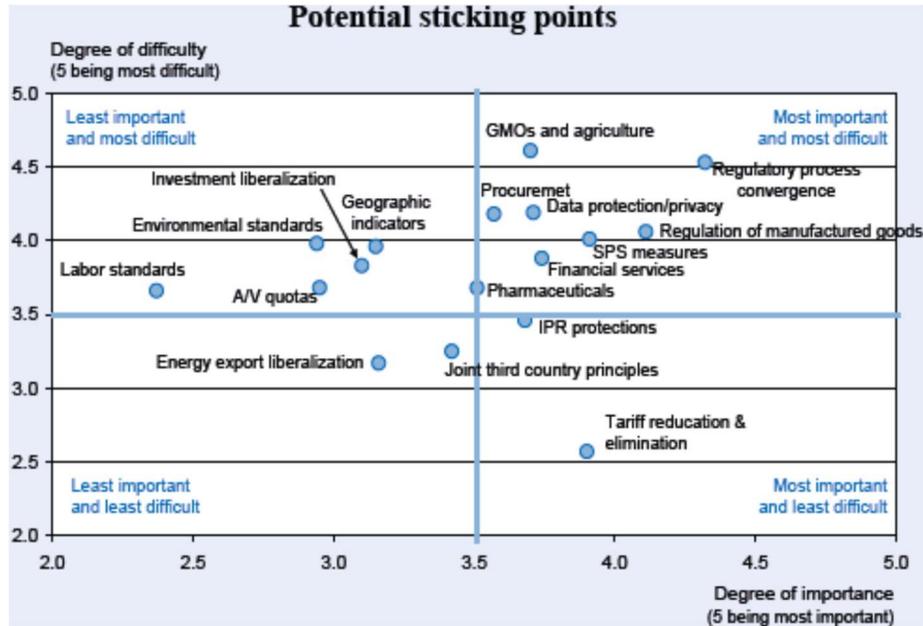
<sup>314</sup> Daniel Ikenson, *Fresh Ideas for a Successful Transatlantic Trade and Investment Partnership*, 4 CESIFO FORUM 24 (Dec. 2013), <http://www.cesifo-group.de/DocDL/forum4-13-focus3.pdf>.

<sup>315</sup> *Id.* at 24-25.

<sup>316</sup> Barker & Workman, *supra* note 36.

shows that most of the data obtained from the trade experts gravitated towards the quadrant where the issues were classified as most important and most difficult.<sup>317</sup>

Figure 1: TTIP Issues and Potential Sticking Points.<sup>318</sup>



The results from the graph clearly demonstrate that a 2014 deadline was unrealistic as 8 of the 17 issues fall into the 'most important and most difficult' quadrant. The negotiating partners should adopt the method outlined on the graph as it is an effective means of identifying the relevant issues to focus most attention on. This would enhance their capacity to make some significant progress in the negotiation of the trade deal.<sup>319</sup>

Even though the USA has launched a number of trade negotiations with different countries during the past three years, it has blatantly ignored its Northern American neighbours. Canada and Mexico already have very strong economic ties with the USA through various trade agreements such as the North American Free Trade Agreement (NAFTA),<sup>320</sup> which allows the free trade of billions of dollars in

<sup>317</sup> *Id.* at 3-4.

<sup>318</sup> *Id.* at 5.

<sup>319</sup> Ikenson, *supra* note 314, at 25.

<sup>320</sup> Michelle Egan, *Including Canada and Mexico in an EU-US Free Trade Agreement Would Create a Genuine Transatlantic Market that Would Deliver Significant Economic Benefits*, EUROPP (2013), <http://blogs.lse.ac.uk/europpblog/2013/09/10/including-canada-and-mexico-in-an-eu-us-free-trade-agreement-would-create-a-genuine-transatlantic-market-that-would-deliver-significant-economic-benefits/>

goods and services across the border on a daily basis. Not including Canada and Mexico in such an ambitious trade partnership would occasion trade diversions and represent a significant opportunity cost.<sup>321</sup> Including Canada and Mexico in TTIP would promote stronger regional integration between NAFTA partners and therefore prompt a significant economic growth for the region. It is also important to point out that both Canada and Mexico are the largest source of energy imports to the USA. As for the EU, including Canada and Mexico in TTIP would give them access to a larger market and thus potentially increase European exports.<sup>322</sup>

If the negotiating partners decide to include Canada and Mexico in TTIP, the two North American countries would gain major benefits from the trade deal and at the same time, their presence in TTIP negotiations would be beneficial to the EU and the USA. First, Canada and Mexico would be joining a trade partnership that promises high degrees of liberalisation and also one that would address issues relating to regulatory barriers in the North American market. Secondly, the inclusion of Canada and Mexico in the EU-USA trade deal would make TTIP a legitimate transatlantic trade agreement that has the ability to deliver major economic gains in terms of tariffs and rules of origin to the North American continent and the EU.<sup>323</sup>

The negotiating partners should first reach an agreement on issues which are not complicated to agree on, such as tariffs and industry standards. Complex issues such as health protection and food safety should be temporarily set aside because those issues are far too controversial and should be dealt with at a later stage of the negotiation process. It must be noted that the aforementioned issues were the main reasons why the progress of the trade deal has experienced a significant slow down in the past two years.<sup>324</sup>

A slimmed down version of TTIP would definitely create a new basis for the negotiations, offering the negotiating partners the ability to remedy the errors they committed in recent years such as the lack of transparency in the negotiation process. This version of TTIP would prioritise negotiating the least complex issues first such as reducing tariff barriers and then focus on more complex issues such as GMO's and agriculture at a later stage. The key for a fresh start in the negotiation process is more openness. The EU and the USA have to at least make some documents pertaining to the negotiation of TTIP available to the general public, such as the proposed chapters in the agreement and some information relating to the impact of those chapters for the EU and the USA, and also include all civil society organisations in the consultation process. If the EU and the USA reforms TTIP's negotiation and consultation processes as proposed above, the negotiating partners would help to restore the faith that the public had in them and also secure the benefits that a free trade agreement can offer minus the threat to democracy.

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<sup>321</sup> Ikenson, *supra* note 314, at 27.

<sup>322</sup> Egan, *supra* note 320.

<sup>323</sup> *Id.*

<sup>324</sup> Christoph Pauly, Michael Sauga, et al., *The TTIP Gap: How a Trans-Atlantic Trade Deal Can Still Be Fixed*, DER SPIEGEL (June 8, 2015), <http://www.spiegel.de/international/world/how-ttip-and-an-eu-us-free-trade-deal-can-be-fixed-a-1036831.html>.

The idea of a slimmed down TTIP has seduced both politicians and academics. Italian Prime Minister Matteo Renzi is of the opinion that the EU and the USA should emphasise negotiating less controversial issues. IFO Institute trade expert Felbermayr argues that a lighter version of TTIP would more likely secure 70-90% of the expected gains promised by the negotiating partners.<sup>325</sup>

The road towards a successful completion of TTIP is long and filled with obstacles. The colossal enterprise of the EU and the USA has caused a lot of debate and will probably continue to be at the centre of discussions for some time. In an attempt to ensure growth and prosperity across the Atlantic, the negotiating partners have occasioned three years of unsuccessful negotiations which has raised concern amongst civil societies both in the EU and the USA. For many, TTIP is too big, too soon, and the scope of the trade deal is very impressive and probably too ambitious. The number of controversial chapters proposed in the trade deal makes it nearly impossible to conclude. As stated previously, the negotiating partners have to find a way to break down the negotiation process and negotiate the trade deal chapter by chapter. Only then would they be able to make substantive progress and conclude the trade partnership successfully.

As discussed, TTIP is presented by proponents as the panacea for the economic predicaments faced by the EU and the USA. The CEPR study, which was used by the negotiating partners to showcase the benefits of the transatlantic partnership, was extensively criticised and even labelled unrealistic and misleading.<sup>326</sup> The study suggests that TTIP will deliver unprecedented economic gains to both the EU and the USA mainly through the reduction of tariffs and NTBs.<sup>327</sup> It is undeniable that some of the predictions are not the most accurate such as the fact that only 25% of goods and services NTBs remain to be eliminated. In this particular case it is more likely that 50% of NTBs rather than 25% will have to be dismantled. The predictions of the CEPR study with regards to the economic benefits of TTIP will only become a reality when all the sectors of the EU's and the USA's economy, without distinction, are liberalised from NTBs.<sup>328</sup> However, it is a little premature to claim that the findings of the CEPR are completely inaccurate and unrealistic.<sup>329</sup>

Even though some have claimed that the benefits of TTIP are far less significant than its negative consequences, it would be unreasonable not to acknowledge the possible gains of the trade deal. The fact that TTIP would allow the negotiating partners to establish new and better standards in relation to consumer goods and services<sup>330</sup> is a good thing. More homogeneity in terms of the quality of consumer goods and services would be beneficial to consumers. The fact that TTIP would increase the availability of foreign products and decrease the

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<sup>325</sup> *Id.*

<sup>326</sup> Myant, *supra* note 46.

<sup>327</sup> Francois, et al., *supra* note 15.

<sup>328</sup> Siles- Brügge & De Ville, *supra* note 49.

<sup>329</sup> Francois et al., *supra* note 15.

<sup>330</sup> Hoekman, *supra* note 98.

trading costs of foreign goods will also be advantageous to consumers as the latter will have a greater choice of products at very competitive prices.<sup>331</sup>

However, the concerns over the potential threat of TTIP on public health cannot be ignored. It is almost certain that if TTIP is successfully negotiated and implemented, health standards in the EU would be lowered and public health services privatised.<sup>332</sup> The privatisation of public health services would automatically lead to its extinction and the reason why this is a very serious issue is because individuals that do not have the means to pay for health care would not be able to access quality treatment.<sup>333</sup> With the way health standards negotiations are going, the EU runs the risk of exacerbating the gap between the rich and the poor, especially for poorer EU member states such as Greece and Portugal where the situation is already undesirable.<sup>334</sup>

As mentioned earlier, since 2013 the negotiating partners have focused their efforts on regulatory cooperation and public procurement. These areas are very controversial and have attracted a lot of attention and debate. Regulatory cooperation is essential in a trade deal of this magnitude. Without regulatory convergence the EU and the USA will never be able to effectively eliminate tariffs and NTBs. TTIP without a regulatory cooperation chapter would definitely not be able to deliver the unprecedented gains promised by the negotiating partners.<sup>335</sup> The EU and the USA have to be very cautious when dealing with such a chapter. Ensuring that stakeholders find it acceptable is important. The regulatory cooperation chapter has to cater for the needs of corporations while at the same time ensuring that the new regulatory cooperation provisions do not undermine regulatory protections and lower standards.<sup>336</sup>

Special attention should be given to the public procurement chapter as 10-15% of the EU's potential gains from TTIP depend on public procurement.<sup>337</sup> The EU has to make it a priority for the USA to give more access to EU firms to its public procurement market or else the significance of TTIP for the EU would be diminished.<sup>338</sup> In order to convince the USA to give greater access to EU firms, the EU must ensure that U.S. firms would not be discriminated against in the EU in relation to the acquisition of government contracts as has been the case in the past.<sup>339</sup> Both the EU and the USA must ensure that the process of acquiring public contracts would happen transparently without any political intervention.

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<sup>331</sup> Straubhaar, *supra* note 98, at 43-44.

<sup>332</sup> Jacobsen, *supra* note 142.

<sup>333</sup> Bennet, *supra* note 145, at 843-44.

<sup>334</sup> Hazel Sheffield, *TTIP Greenpeace Leak Shows How US Can Pressure EU to Compromise Health and the Environment Under Trade Deal*, THE INDEPENDENT (May 5, 2016), <http://www.independent.co.uk/news/business/news/ttip-leak-greenpeace-trade-deal-eu-us-tpp-ceta-health-environment-a7014731.html>.

<sup>335</sup> Francois, et al., *supra* note 15, at 33-36, 95.

<sup>336</sup> Edsall, *supra* note 207.

<sup>337</sup> EUROPEAN UNION SUBCOMMITTEE ON EXTERNAL AFFAIRS, *supra* note 265.

<sup>338</sup> *Id.* at ¶12841.

<sup>339</sup> OFFICE OF THE U.S. TRADE REPRESENTATIVE, *supra* note 10.

The main issue with the impact of TTIP on the international trading system is that it willingly or unwillingly has a significant potential to surpass and ultimately replace the WTO. The problem with that is twofold. On the one hand, the WTO is an intergovernmental organisation that aims to promote and regulate international trade amongst its 162 members, with each member being treated equally without distinction.<sup>340</sup> On the other hand, we have TTIP, a bilateral, preferential trade agreement that aims to promote trade between the EU and the USA.<sup>341</sup> The risk that TTIP represents for the international trading system is significant. A bilateral trade agreement, as big as it may be, will never effectively replace an international organisation. The nature of TTIP clearly shows that it cannot be an effective replacement for the WTO as it promotes trade and protects the interests of only two partners, therefore automatically excluding the rest of the world. However, if the influence of the TTIP undermines the effectiveness of the WTO or ultimately overshadows the working of the organisation, many developing countries which are protected by WTO rules would be negatively affected by this, widening the gap between high and low-income nations.<sup>342</sup>

The manner in which the EU-USA trade deal has been handled during the past three years suggests that the negotiating partners want to conclude the deal as quickly as possible in order to waste no time in regaining their position of power, and consequently weaken the growing influence of rising powers such as the BRICS nations in the international trade arena.<sup>343</sup> The geostrategic implications of TTIP are crystal clear. The EU and the USA are using TTIP as a means to marginalise the BRICS nations, especially China, who is undoubtedly one of the fiercest economic rivals that the EU and the USA have faced in decades. This could, as mentioned, also negatively affect developing and low-income countries.

Whether or not TTIP would deliver the economic gains promised by the EU and the USA would solely depend on how the negotiating partners handle the future negotiation rounds. It is undeniable that when the negotiations were launched the negotiating partners were overly hopeful. They thought that the trade deal would take between one to two years to conclude, but reality caught up with them and since 2013 the negotiation process is in a phase of stagnation. As the days pass, the general public and even some EU member states such as France are losing faith in TTIP, and the secrecy of the negotiation process has made things even worse. The negotiating partners must remedy this situation if they want the trade deal to become a reality. As proposed previously, breaking down the trade deal and

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<sup>340</sup> PETER VAN DEN BOSCHE & WERNER ZDOUC, *THE LAW AND POLICY OF THE WORLD TRADE ORGANISATION* 82-86 (3rd ed. 2015).

<sup>341</sup> Patrick Messerlin, *The Transatlantic Trade and Investment Partnership: The Services Dimension*, 1 CENTRE FOR EUROPEAN POLICY STUDIES (2015), <https://www.ceps.eu/system/files/SR106%20TTIP%20Services%20Messerlin%20.pdf>.

<sup>342</sup> Perreau de Pinninck, *supra* note 279.

<sup>343</sup> Winters, *supra* note 302.

negotiating chapter by chapter is the best possible way to ensure a successful completion of TTIP negotiations.







# CORPORATE SUSTAINABILITY REPORTING AND “MATERIAL INFORMATION:” AN EMPIRICAL STUDY OF MATERIALITY UNDER THE GRI AND <IR> FRAMEWORKS

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*Abstract*

*Corporate reporting is premised on the concept of the disclosure of “material” information, developed for financial reporting. The increase in sustainability reporting has seen the materiality concept migrate into non-financial reporting and resurfaced two issues with the concept. Sustainability reporting expands the traditional audience for information beyond shareholders, often resulting in lengthy reports that produce little return to the reporting companies. In addition, the two dominant sustainability reporting frameworks – the Global Reporting Initiative (GRI) and the International Integrated Reporting Council (IIRC) – continue the tradition of broad definitions of materiality. The promise of the materiality concept as a mechanism to improve disclosure to stakeholders remains unfulfilled. What is less clear is whether the disappointing track record is due to defects inherent in the concept itself or to shortcomings in its application. This Article describes the results of a global, cross-sector empirical study to test the adequacy of the GRI and <IR> materiality determination processes. The project analyzed reports prepared under each framework to discern how reporting companies operationalize the materiality concept in their sustainability reporting. The study shows that firms struggle with applying the materiality concept, often shortcutting the process and disconnecting the process from their stakeholders. A recommitment to rigorous application of the materiality concept could improve the effectiveness of sustainability reporting.*

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## INTRODUCTION

Corporate reporting has long been premised on the concept of the disclosure of “material” information. Materiality is critical to determining report content, i.e., what companies disclose and what they do not. Commentators have called materiality the “legal benchmark for determining the significance of information for disclosure purposes;”<sup>1</sup> the concept is embedded in securities disclosure laws.<sup>2</sup> The materiality concept poses two separate, but related, challenges for companies attempting to implement it. Since the concept originated in financial reporting, it has historically focused on investors as the audience for the information. This, in and of itself, is not objectionable, but it has implications for the definition of material information. Additionally, the legal definitions of material information developed under securities laws are notoriously hazy, with the contours of what qualifies as “material” information ill defined.<sup>3</sup>

The rise of sustainability reporting<sup>4</sup> saw the concept translated to the realm of non-financial reporting and resurfaced old issues. Sustainability reporting challenges the traditional audience for information by expanding the range of information users beyond shareholders. This expanded audience often results in lengthy reports that produce little return to the reporting companies.<sup>5</sup> At the same time, the two dominant sustainability reporting frameworks – the Global Reporting Initiative (GRI) and the International Integrated Reporting Council (IIRC) framework for Integrated Reporting (<IR>) – have continued the tradition of broad, general definitions of what constitutes “material” information. The two frameworks further complicate the field by utilizing different definitions of this key concept.<sup>6</sup>

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<sup>1</sup> Chloe Ghoogassian, *Evading the Transparency Tragedy: The Legal Enforcement of Corporate Sustainability Reporting*, 11 HASTINGS BUS. L. J. 361, 377 (2015) (quoting Joseph A. Franco, *Why Antifraud Prohibitions are not Enough: The Significance of Opportunism, Candor and Signaling in the Economic Case for Mandatory Securities Disclosure*, 2002 COLUM. B. L. REV. 223, 298-99 (2002)).

<sup>2</sup> See *infra* notes 12-30 and accompanying text.

<sup>3</sup> One commentator noted that the “facial simplicity of [materiality] masks the complexities” of applying it. Joan McLeod Heminway, *Materiality Guidance in the Context of Insider Trading: A Call for Action*, 52 AM. U. L. REV. 1131, 1139 (2003).

<sup>4</sup> The terms “sustainability,” “environmental, social and governance (ESG),” “corporate social responsibility,” “integrated reporting” or “non-financial” reporting have been used somewhat interchangeably in the past, to describe reports with different degrees of emphasis on environmental, social, or governance issues and to distinguish these reports from mandated financial disclosures. For simplicity, this article uses the term “sustainability reporting” to refer to reporting of non-financial information by a business entity.

<sup>5</sup> SUSTAINABILITY, SEE CHANGE: HOW TRANSPARENCY DRIVES PERFORMANCE 9 (2014), [http://10458-presscdn-0-33.pagely.netdna-cdn.com/wp-content/uploads/2016/07/see\\_change\\_how\\_transparency\\_drives\\_performance.pdf](http://10458-presscdn-0-33.pagely.netdna-cdn.com/wp-content/uploads/2016/07/see_change_how_transparency_drives_performance.pdf).

<sup>6</sup> See *infra* notes 50 and 73 and accompanying text.

The promise of the materiality concept as a mechanism to tighten disclosure efforts to communicate more effectively with stakeholders on critical issues would seem unfulfilled.<sup>7</sup> What is not clear is whether the disappointing track record of the materiality concept in sustainability reporting is due to defects inherent in the concept itself or due to shortcomings in its application.

This empirical study tests the adequacy of the GRI and <IR> definitions of materiality and the frameworks' materiality determination processes [MD Process] by analyzing reports prepared under each of these frameworks to discern how reporting companies interpret and operationalize the materiality concept for the purposes of sustainability reporting. The project studied reports from companies representing a range of industries and geographic regions in an attempt to answer several important questions related to companies' decisions on what to include in their sustainability reports: how do reporting companies interpret the definitions and concept of "material" information under the GRI and <IR> frameworks. How closely are firms adhering to the materiality determination processes set out in the frameworks? How do firms' stakeholder engagement processes affect the firm's identification of material topics? Does the materiality determination process receive sufficient attention from the highest decision-making levels within the company?

The study shows that, despite increased numbers of companies engaged in sustainability reporting under either the GRI or <IR> framework, companies struggle with implementing and articulating the process for determining report content. Sustainability reports increase in length, but do not necessarily provide report users with higher quality disclosure or information that is more useful.

Key findings of the study include:

#### INCOMPLETE/INCONSISTENT USE OF THE MD PROCESS

Approximately two-thirds of reports studied contain disclosures on only portions of the MD Process. Although both GRI and <IR> frameworks provide users with a specific process for determining material information (the MD Process), companies apply the MD Process incompletely and/or inconsistently. Only a small percentage of companies implements and discloses how they have implemented the relevant MD Process.

#### DISCONNECT BETWEEN STAKEHOLDER ENGAGEMENT ACTIVITIES AND THE MD PROCESS

Both the GRI and <IR> frameworks posit extensive interaction with a variety of stakeholders as part of identifying material information. While many companies reported impressive and robust stakeholder engagement processes, few connected their stakeholder engagement activities to the materiality concept or explained how their engagement activities affected how they defined material information.

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<sup>7</sup> SUSTAINABILITY, *supra* note 5, at 4, 12.

LACK OF DISCLOSURE ON INTERNAL GOVERNANCE OF MD PROCESS: Sustainability reporting is a voluntary activity, undertaken by companies at their discretion and with no official oversight of firms' reporting or materiality determination. Both the GRI and <IR> frameworks rely primarily on disclosure of firm's internal governance bodies and processes as accountability mechanisms for reporting under the framework. Our analysis of a variety of governance factors demonstrated lackluster disclosure on these issues, perhaps calling into question the integrity of reports prepared under these frameworks.

This Article begins by setting out the concept of "materiality" as applied to the selection of information for disclosure, both for financial and non-financial reporting, in Section II. Section III describes the study methodology, and Section IV provides analysis and discussion of major issues surfaced by the data analysis. The Article concludes with thoughts on the role of the materiality concept in sustainability reporting and suggestions for improved implementation of the concept.

## I. THE MATERIALITY CONCEPT IN CORPORATE DISCLOSURE

The concept of materiality is essentially a tool to determine the contours of corporate disclosure. No company can disclose literally everything about its current and future business, given the complexity of today's business world.<sup>8</sup> Business, therefore, needs a mechanism to determine what, from the universe of possible information, it ought to disclose. This mechanism is the materiality concept, which acts to set information disclosure thresholds.<sup>9</sup> Materiality separates what *should* be disclosed from what *could* be disclosed, from the perspective of its usefulness for the disclosure's audience.<sup>10</sup>

Unfortunately, the definition of materiality for disclosure purposes is not self-evident.<sup>11</sup> A review of efforts to define the term is important to understand the complexity of this seemingly simple word and the challenges of its use. This section provides an overview of the efforts to define materiality for financial reporting and, then, for sustainability reporting.

### A. Financial Reporting

The concept of the "materiality" of information has traditionally been associated with the field of securities regulation and corporate financial disclosure.<sup>12</sup> U.S. securities law provides a useful example of this key disclosure concept. The purpose of the disclosure provisions under U.S. securities laws is to

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<sup>8</sup> Amy Deen Westbrook, *Sunlight on Iran: How Reductive Standards of Materiality Excuse Incomplete Disclosure Under the Securities Laws*, 7 HASTINGS B. L. J. 13, 18 (2011).

<sup>9</sup> Robert G. Eccles & Tim Youmans, *Materiality in Corporate Governance: The Statement of Significant Audiences and Materiality* 4 (Harv. Bus. Sch., Working Paper No. 116-023, 2015).

<sup>10</sup> Westbrook, *supra* note 8, at 23. Westbrook calls materiality a "principle of distinction." *Id.*

<sup>11</sup> Eccles & Youmans, *supra* note 9, at 4 (noting that materiality forms the "conceptual bedrock" of corporate reporting but that the concept has no authoritative definition).

<sup>12</sup> Peter Jones, Daphne Comfort, & David Hiller, *Sustainability, materiality, assurance and the UK's leading property companies*, 17 J. OF CORP. REAL EST., no. 4, 282, 285 (2015).

promote transparency in the financial markets through complete and accurate disclosure of information.<sup>13</sup> The crash of the U.S. stock market in 1929 illustrated the risk of inadequate information and highlighted the benefit of consistent and government-enforced disclosure.<sup>14</sup> While too little information had undermined investor protection, too much information can make it difficult for investors to weed out useful information from unhelpful information.<sup>15</sup> The materiality concept promotes the cause of transparency by acting as a filter, winnowing out trivial or irrelevant information.<sup>16</sup> Materiality is a device that sorts information required to be disclosed from that which is not required to be disclosed.<sup>17</sup> Securities laws reflect this approach to information disclosure by premising disclosure obligations on whether information is material.<sup>18</sup>

### 1. Corporate Disclosure Requirements and Materiality

Under the 1934 Securities Exchange Act (1934 Act) and accompanying regulations, companies listed on U.S. stock exchanges are required to disclose annually and periodically information about the company.<sup>19</sup> While some of the required disclosure items are quantitative, other disclosure is qualitative and less precisely defined. One example of required qualitative disclosure is Item 303--Management's discussion and analysis of financial condition and results of operations, often referred to as "MD&A."<sup>20</sup> As the title implies, the MD&A is a narrative disclosure of a variety of factors related to company operations and finances, including company liquidity, capital resources, and off-balance sheet arrangements.<sup>21</sup> The MD&A relies heavily on the concept of materiality as a mechanism to guide firms' decisions on what information must be disclosed under Item 303. For example, the regulation requires that firms disclose trends, events, or uncertainties that may affect a firm's liquidity in a "material" way.<sup>22</sup> Other items

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<sup>13</sup> Richard C. Sauer, *The Erosion of the Materiality Standard in the Enforcement of the Federal Securities Laws*, 62 BUS. LAW. 317, 317 (2007); Heminway, *supra* note 3, at 1170.

<sup>14</sup> Adam Sulkowski & Sandra Waddock, *Beyond Sustainability Reporting: Integrated Reporting is Practiced, Required and More Would Be Better*, 10 U. ST. THOMAS L. J. 1060, 1062 (2014); *see also* MARY GRAHAM, INFORMATION AS RISK REGULATION: LESSONS FROM EXPERIENCE 5 (2001) (describing securities disclosure laws as "structured transparency" essential to investor confidence), <http://www.transparencypolicy.net/assets/information.pdf>.

<sup>15</sup> Alison B. Miller, *Navigating the Disclosure Dilemma: Corporate Illegality and the Federal Securities Laws*, 102 GEO. L. J. 1647, 1653 (2014); *see also* Yvonne Ching Ling Lee, *The Elusive Concept of "Materiality" Under U.S. Federal Securities Laws*, 40 WILLAMETTE L. REV. 661, 662 (explaining that materiality helps avoid a market saturated with "insignificant" information).

<sup>16</sup> Sauer, *supra* note 13, at 317-18.

<sup>17</sup> Heminway, *supra* note 3, at 1149.

<sup>18</sup> Miller, *supra* note 15, at 1652; Wendy Gerwick Couture, *Materiality and a Theory of Legal Circularity*, 17 U. PA. J. BUS. L. 453, 459 (2015).

<sup>19</sup> For an overview of disclosure requirements under U.S. securities laws, *see* Heminway, *supra* note 3, at 1170-71.

<sup>20</sup> 17 C.F.R. § 229.303 (2011).

<sup>21</sup> *Id.*

<sup>22</sup> 17 C.F.R. § 229.303(a)(1) (2011).

in the MD&A also incorporate the materiality concept in a similar vein,<sup>23</sup> as do several provisions related to the issuance of proxy statements and securities fraud.<sup>24</sup>

## 2. Defining Materiality

The definition of the term “material,” then, is critical for firms required to comply with SEC mandatory disclosure. Unfortunately, the 1934 Act does not itself define “material” information, nor is a definition provided in the rules and regulations associated with that statute.<sup>25</sup> It was inevitable, then, that the U.S. Supreme Court would have to confront the materiality discussion, in the form of lawsuits brought against corporations claiming they had failed to disclose “material” information required under securities laws. Two provisions of the 1934 Act in particular gave birth to a line of cases focused on the definition of materiality. Section 14 of the Act addresses the solicitation of proxy statements by registered companies and makes it illegal to make an untrue statement of “material fact” or to omit to state a “material fact” as part of a tender offer.<sup>26</sup> Section 10(b), the anti-fraud provisions of the Act, also incorporates the concept of materiality as part of the definition of deceptive devices. Rule 10(b)-5 makes it unlawful to make an untrue statement of a “material fact” or to omit a “material fact.”<sup>27</sup> In 1976, the Supreme Court articulated the materiality standard applicable to actions under Section 14 in *TSC Industries, Inc., et al. v. Northway, Inc. (TSC)*, which identified “material” information as information that the reasonable investor would consider significant as part of the “total mix of information” made available by the company.<sup>28</sup> Several years later, the Court extended this definition of materiality to fraud actions brought under Section 10(b).<sup>29</sup> The *TSC* definition of materiality remains the formulation in place for federal securities laws today.<sup>30</sup> Since the decision in *TSC*, both the Securities Exchange Commission (SEC) and the Financial Accounting Standards Board (FASB) have contributed to the implementation of the materiality concept in corporate reporting.<sup>31</sup>

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<sup>23</sup> See, e.g., 17 CFR § 229.303(a)(4) (2011). For discussion of other regulatory disclosure requirements related to the materiality concept, see Lee, *supra* note 15, at 670-73.

<sup>24</sup> See *infra* notes 26-27 and accompanying text.

<sup>25</sup> Heminway, *supra* note 3, at 1150.

<sup>26</sup> 15 U.S.C. § 78n(e) (2012). The corresponding regulation addresses the use of “material” nonpublic information in the process of making a tender offer. See 17 C.F.R. § 240.14e-3 (1980).

<sup>27</sup> 17 C.F.R. § 240.10b-5(b) (1951).

<sup>28</sup> *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438 (1976) [hereinafter *TSC*] (*TSC* involved a proposed merger between TSC Industries and another company. A TSC shareholder, Northway Inc., sued TSC alleging that the proxy statement issued to shareholders as part of voting on the proposed merger was materially misleading).

<sup>29</sup> See *Basic Inc. v. Levinson*, 485 U.S. 224 (1988) (*Basic*, like *TSC*, centered on a proposed merger situation where shareholders alleged that company management had made misleading statements about pre-merger discussions, which had artificially depressed the price of the stock).

<sup>30</sup> Sauer, *supra* note 13, at 320.

<sup>31</sup> The SEC issued a key bulletin in 1999, focused on clarifying the Commission’s interpretation of the concept and its use in identifying thresholds for preparation of financial statements. SEC, STAFF ACCOUNTING BULLETIN NO. 99 (Aug. 12, 1999) [hereinafter SEC BULLETIN]. The SEC Bulletin defined information as “material” if there was “a substantial likelihood that a reasonable person would consider [the matter] important”. *Id.* at 3; see also Sauer, *supra* note 13, at 336 (discussion of the SEC

The Supreme Court's definition of materiality displayed several characteristics that influenced the concept's interpretation for sustainability reporting. First, the definition recognizes the audience for the information involved (i.e., investors or users of financial statements) as an important factor in determining whether information is "material."<sup>32</sup> Further, the Court took the approach of eschewing a "bright line" definition of materiality in favor of a broader definition that requires the disclosing firm to exercise its judgment in deciding what information qualifies as "material."<sup>33</sup> While this flexibility recognized that "materiality" is context- and entity-specific,<sup>34</sup> it also resulted in a level of ambiguity that continues to generate frustration for reporting companies,<sup>35</sup> and spawned additional litigation.<sup>36</sup>

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Bulletin's approach to materiality). FASB is a non-profit organization that creates financial accounting and reporting standards, and is recognized by the SEC as the designated accounting standard setter for public companies. ABOUT THE FASB, FINANCIAL ACCOUNTING STANDARDS BOARD, <http://www.fasb.org/facts/> (last visited Oct. 21, 2017). FASB's formal contributions to the materiality discussion began in 2008 when it released its Concepts No. 2 statement in 2008. Concepts No. 2 defined and used the materiality concept as one of the qualitative characteristics of accounting information. STATEMENT OF FINANCIAL ACCOUNTING CONCEPTS NO. 2, FINANCIAL ACCOUNTING STANDARDS BOARD (2008), <http://www.fasb.org/cs/BlobServer?blobcol=urldata&blobtable=MungoBlobs&blobkey=id&blobwhere=1175820900526&blobheader=application%2Fpdf>. In 2010, FASB issued a new conceptual framework for reporting, part of which replaced Concepts No. 2 and its definition of materiality. STATEMENT OF FINANCIAL ACCOUNTING CONCEPTS NO. 8, FINANCIAL ACCOUNTING STANDARDS BOARD (Sept. 2010),

[http://www.fasb.org/jsp/FASB/Document\\_C/DocumentPage?cid=1176157498129&acceptedDisclaimer=true](http://www.fasb.org/jsp/FASB/Document_C/DocumentPage?cid=1176157498129&acceptedDisclaimer=true) [hereinafter CONCEPTS NO. 8]. Concepts No. 8 defined information as material if omitting or misstating it could influence decisions that users make on the basis of financial information. *Id.* at 17. As recently as 2015, FASB issued proposed revisions to its materiality definition. PROPOSED AMENDMENTS TO STATEMENT OF FINANCIAL ACCOUNTING CONCEPTS, EXPOSURE DRAFT, FINANCIAL ACCOUNTING STANDARDS BOARD (Sept. 2015), [http://fasb.org/jsp/FASB/Document\\_C/DocumentPage?cid=1176166402450&acceptedDisclaimer=true](http://fasb.org/jsp/FASB/Document_C/DocumentPage?cid=1176166402450&acceptedDisclaimer=true) [hereinafter FASB PROPOSED AMENDMENTS].

<sup>32</sup> Charles R. Korsmo, *The Audience for Corporate Reporting*, 102 IOWA L. REV. 1581, 1583 (2017) (calling the identification of the audience for reporting as "crucial" for determining report content); *see also* Eccles and Youmans, *supra* note 11. Eccles' Working Paper sets out the case for the connection between identifying audience and determining materiality.

<sup>33</sup> Lee, *supra* note 15, at 667. Both the SEC and FASB specifically rejected the idea of setting quantitative thresholds for when information is "material"; *See, e.g.*, SEC BULLETIN, *supra* note 31, at 2-5, and CONCEPTS NO. 8, *supra* note 31, at 17, ¶QC11. The Supreme Court argued against the use of a "bright line" rule distinguishing material from immaterial information, finding materiality determination too fact-specific to accommodate such a rule. Stefan J. Padfield, *Immaterial lies: Condoning Deceit in the Name of Securities Regulation*, 61 CASE W. RES. L. REV. 143, 154 (2010) (quoting *Basic Inc. v. Levinson*). The TSC materiality standard has been described as "establishing a framework for analysis rather than a formula for deciding specific cases." Sauer, *supra* note 13, at 321.

<sup>34</sup> CONCEPTS NO. 8, *supra* note 31, at 17, ¶QC11. Materiality has also been described as "inherently situational," Sauer, *supra* note 13, at 319, and "contextual and fact-specific," Couture, *supra* note 18, at 465.

<sup>35</sup> Sauer, *supra* note 13, at 321 (describing factors that contribute to confusing the process of applying the materiality definition). One major source of frustration is what is often referred to as the "ex post/ex ante" problem. This problem arises in litigation, where a court is passing judgment on a disclosure decision made at some prior time, i.e., some time before the litigation. "Courts must look back...to judge that decision...sometime after it was made – with changed knowledge making the decision look quite different." Thomas M. Madden, *Significance and the Materiality Tautology*, 10 J. BUS. & TECH. L. 217, 234 (2015) (quoting Jeffrey J. Rachlinski & Donald C. Langevoort, *Fraud by Hindsight*, 98 NW. U. L. Rev. 773, 774 (2004)). This phenomenon essentially leaves corporate

Although commentators have roundly criticized the concept of materiality as developed through financial reporting,<sup>37</sup> it is deeply embedded in financial reporting. As sustainability organizations began to construct disclosure frameworks, it was perhaps natural that the concept would migrate from financial reporting to sustainability reporting. Sustainability disclosure possesses some of the same goals and characteristics as financial disclosure in its quest for transparency. However, the institutional context of sustainability reporting is qualitatively different from that of financial reporting. Translation of the materiality concept from the regulated environment of financial reporting to the unregulated environment of sustainability reporting is the subject of this study and the remainder of this article.

### *B. Sustainability Reporting*

The purpose of the materiality construct in sustainability reporting is, as with financial reporting, to promote transparency in disclosure and to avoid misrepresentation.<sup>38</sup> However similar the goals, the paths to these objectives differ between financial and sustainability reporting. Financial reporting is characterized by a regulatory framework that defines materiality and adjudicates implementation of that definition.<sup>39</sup> Sustainability reporting has no “regulator” and, therefore, no body to determine what information firms should disclose, except as suggestions. The voluntary character of sustainability reporting frameworks leaves the determination of report content in the hands of the reporting company.<sup>40</sup> A

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reporters subject to the “dubious perspective of hindsight” of regulators and/or court if the company’s disclosure is challenged. Sauer, *supra* note 13, 319. A second source of frustration is that the definitions of materiality developed by the SEC and FASB were sometimes seen as not meshing with the Supreme Court’s definition. FASB recognized this fact when, in 2015, it proposed revisions to Concepts No. 8 that would define materiality in accordance with the Supreme Court’s definition. FASB PROPOSED AMENDMENTS, *supra* note 31.

Industry organizations have also weighed in with opinions on the implementation of various disclosure requirements, both existing and proposed, as well as on disclosure philosophy in general. *See, e.g.*, BUSINESS ROUNDTABLE, THE MATERIALITY STANDARD FOR PUBLIC COMPANY DISCLOSURE: MAINTAIN WHAT WORKS (2015) (criticizing Congress for attempting to use corporate disclosure in service of non-financial agendas).

<sup>36</sup> *See, e.g.*, Amgen, Inc. v. Conn. Ret. Plans & Trust Funds, 133 S. Ct. 1184 (2013); Erica P. John Fund v. Halliburton Co., 563 U.S. 804 (2011); Matrixx Initiatives, Inc. v. Siracusano, 563 U.S. 27 (2011).

<sup>37</sup> Critics have described materiality as “deceptively simple,” Couture, *supra* note 18, at 456, 464; “elusive,” Lee, *supra* note 15, at 663-664; and “notoriously slippery... unpredictable in application.” Sauer, *supra* note 13, at 319 (quoting SEC v. Bausch & Lomb Inc., 565 F.2d 8, 10 (2d. Cir. 1977)).

<sup>38</sup> GLOBAL REPORTING INITIATIVE (GRI), G4 SUSTAINABILITY REPORTING GUIDELINES, REPORTING PRINCIPLES AND STANDARD DISCLOSURES, 3 (2013) [hereinafter GRI PRINCIPLE]; INT’L INTEGRATED REPORTING COUNCIL (IIRC), THE INT’L <IR> FRAMEWORK 18, ¶3.14 (2013) [hereinafter <IR> FRAMEWORK].

<sup>39</sup> *See supra* notes 19-30 and accompanying text.

<sup>40</sup> GRI PRINCIPLES, *supra* note 38, at 28; STANDARD DISCLOSURE G4-18; GRI, G4 SUSTAINABILITY REPORTING GUIDELINES IMPLEMENTATION MANUAL 8 (2013) [hereinafter GRI IMPLEMENTATION MANUAL]; INT’L INTEGRATED REPORTING COUNCIL, MATERIALITY: BACKGROUND PAPER FOR <IR> 9, ¶36, AM. INST. OF CERTIFIED PUB. ACCT. (2012) [hereinafter <IR> BACKGROUND PAPER]; *see also*, Iris Chiu, *Standardization in Corporate Social Responsibility*

threshold issue for successful sustainability reporting, then, is *how* to determine the contents of the sustainability report.

Both the GRI and <IR> reporting frameworks invoke the concept of “materiality” of information as part of their reporting principles, requiring reporting companies to disclose “material” information. Materiality, thus, is the cornerstone of deciding report content. To aid in this critical decision-making, both frameworks have devised multi-step processes for reporting companies to utilize to determine the materiality of specific issues and information. The overarching approach to determining materiality is essentially the same under the two frameworks and consists of a series of steps to identify what *should* be disclosed from the universe of what *could* be disclosed. Both GRI and <IR> refer to this as the materiality determination process (MD Process) and it is the heart of sustainability reporting. A better understanding of firms’ interaction with this concept calls for a more detailed discussion of the two frameworks and their MD Processes.

### 1. Global Reporting Initiative

The Global Reporting Initiative (GRI) is a non-profit organization that has built the dominant standard for sustainability disclosure.<sup>41</sup> GRI was founded in 1997 with the objective of developing a business reporting framework that encompassed economic, environmental, social, and governance information.<sup>42</sup> The initial version of the reporting guidelines launched in 2000 as the first global framework for comprehensive sustainability reporting.<sup>43</sup> The reporting Guidelines have been through several revisions, via the GRI multi-stakeholder process; 2013 saw the release of the fourth generation of the Guidelines, the G4 Guidelines.<sup>44</sup>

The GRI reporting Guidelines are a principles-based reporting system. Rather than proscribing specific disclosure items, the Guidelines set out principles for

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*Reporting and a Universalist Concept of CSR – A Path Paved with Good Intentions?*, 22 FLA. J. INT’L L. 361, 379 (2010) (discussing the GRI framework).

<sup>41</sup> Sulkowski & Waddock, *supra* note 14, at 1064. The GRI database of reports includes documents from over 10,000 different organizations. The database contains over 41,000 reports, with more than 27,000 of them created “in accordance with” the GRI reporting framework. *Database*, GLOBAL REPORTING INITIATIVE, <http://database.globalreporting.org>.

<sup>42</sup> GRI’S HISTORY, GLOBAL REPORTING INITIATIVE, <https://www.globalreporting.org/information/about-gri/gri-history/Pages/GRI's%20history.aspx>. (last visited June 14, 2017). For discussion of the development of GRI from an organizations perspective, see Halina Szejnwald Brown, Martin deJong, & Teodorina Lessidrenska, *The Rise of the Global Reporting Initiative (GRI) as a Case of Institutional Entrepreneurship*, (John F. Kennedy Sch. of Gov’t, Harv., Working Paper No. 36 May 2007), [https://www.hks.harvard.edu/m-rcbg/papers/szejnwald\\_brown\\_april\\_07.pdf](https://www.hks.harvard.edu/m-rcbg/papers/szejnwald_brown_april_07.pdf).

<sup>43</sup> GRI’S HISTORY, *supra* note 42.

<sup>44</sup> *Id.* Since the promulgation of the G4 Guidelines, GRI has altered its approach to the framework and, in 2016, launched its reporting Standards. The new Standards will supersede all previous versions of the Guidelines as of July 1, 2018. FIRST GLOBAL SUSTAINABILITY REPORTING STANDARDS SET TO TRANSFORM BUSINESS, GLOBAL REPORTING INITIATIVE (Oct. 19, 2016), <https://www.globalreporting.org/information/news-and-press-center/Pages/First-Global-Sustainability-Reporting-Standards-Set-to-Transform-Business.aspx>. GRI reports reviewed for this study were prepared under either the G3.1 or G4 Guidelines.

reporting companies to use in creating their reports. The Guidelines are just that: guides for the firm's decision-making.<sup>45</sup> Companies have discretion to determine what and how to report, but must apply the Reporting Guidelines in doing so.<sup>46</sup> GRI's *Reporting Principles and Standard Disclosures (Reporting Principles)* govern reporting under the framework. As the name implies, this document sets out the general principles underlying GRI reporting and identifies GRI standard disclosures and the criteria for preparing a report "in accordance with" GRI Guidelines.<sup>47</sup>

### *GRI MD Process*

The G4 Guidelines included an increased emphasis on reporting that focused on topics material to a business and its stakeholders.<sup>48</sup> The *Reporting Principles* make this connection clear, by stating that "the core of preparing a sustainability report is a focus on the process of identifying material [topics] – based, among other factors, on the Materiality Principle."<sup>49</sup> The G4 Guidelines' Principles for Defining Report Content define "materiality" of information as topics that "reflect the organization's significant economic, environmental and social impacts; or substantively influence the assessment and decisions of stakeholders."<sup>50</sup> The *Reporting Principles* contain a summary overview of the four-step GRI MD Process,<sup>51</sup> but the main tool for understanding and operationalizing the MD Process is the *GRI Implementation Manual*. The *Implementation Manual* is part of the G4 Sustainability Reporting Guidelines, together with the *Reporting Principles*, and focuses on practical advice for implementation of the Principles, interpretation of GRI concepts, and preparation of a GRI report.<sup>52</sup>

The *Implementation Manual* sets out in detail the GRI MD Process, providing both broad guidance on application of the GRI principle of materiality as well as the specifics of the MD Process.<sup>53</sup> The GRI MD Process consists of four steps, of which the first two, identification and prioritization, are the most important for the Process. The basic process is essentially a funnel that begins with identification of all relevant topics for reporting.<sup>54</sup> "Relevant" topics are all those that are potentially important as related to the GRI definition of materiality.<sup>55</sup> The

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<sup>45</sup> GRI IMPLEMENTATION MANUAL, *supra* note 40, at 16.

<sup>46</sup> See, e.g., GRI IMPLEMENTATION MANUAL, *supra* note 40, at 6, 8. The Implementation Manual describes itself as providing "valuable information" on how to "understand, interpret, and implement" the concepts and principles of the Reporting Guidelines. *Id.* at 6.

<sup>47</sup> GRI PRINCIPLES, *supra* note 38, at 7.

<sup>48</sup> *Id.* at 3.

<sup>49</sup> *Id.* at 7. The purpose of materiality determination is for the firm to align both its reporting and its strategic decisions with the topics identified as material. SUSTAINABILITY, *supra* note 5, at 16.

<sup>50</sup> GRI PRINCIPLES, *supra* note 38, at 17. The Principle goes on to explain that "[o]rganizations are faced with a wide range of topics on which they *could* report. . . Materiality is the threshold at which Aspects become sufficiently important that they *should* be reported." [emphasis added].

<sup>51</sup> *Id.* § 6.9, at 90.

<sup>52</sup> GRI IMPLEMENTATION MANUAL, *supra* note 40, § 1 at 4.

<sup>53</sup> *Id.* §§ 3.1, 4.1, 11, 32.

<sup>54</sup> *Id.* at 32-39.

<sup>55</sup> *Id.* § 3.1, at 11.

determination of relevant topics is grounded in GRI Principles that emphasize the importance of stakeholder concerns to the company and of thinking broadly about the total impact (whether internal or external) of the company's operations, activities, products, and relationships.<sup>56</sup> This broad ranging identification process ordinarily results in a wide range of topics on which the company could report, a list that would be too long for all to be included in the report.<sup>57</sup> The critical second step is the MD Process is to cull out those topics "sufficiently important" that they should be reported – the "material" topics – from the relevant topics.<sup>58</sup> This "prioritization" step involves the company considering the significance of each topic's impact, or its influence on stakeholder decisions.<sup>59</sup> Once this analysis is complete, the company defines threshold criteria that make a "relevant" topic "material."<sup>60</sup> The prioritization process is represented in the Implementation Manual as a 2x2 matrix, with X and Y-axes reflecting the GRI definition of materiality (i.e., impact of issues on stakeholders and issues' influence on stakeholder decisions).<sup>61</sup> Plotting issues on the matrix against both axes provides a visual depiction of the relative importance among issues. GRI does not require that firms use a matrix, but just under one-half of GRI firms in this study employed a matrix as part of their MD Process.<sup>62</sup>

Last, the GRI framework indicates that firms should disclose key internal aspects of their application of the MD Process. Specifically, the framework charges firms to clearly define and communicate their thresholds and underlying criteria for materiality.<sup>63</sup>

## 2. International Integrated Reporting Council and <IR>

The International Integrated Reporting Council (IIRC) formed in 2010<sup>64</sup> and brought together a cross section of leaders from business, accounting, investment, academia, regulatory spheres, and civil society.<sup>65</sup> The objective of the IIRC was to develop a new kind of corporate reporting model that grounded disclosure around the firm's ability to create value over time.<sup>66</sup> After several years of development

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<sup>56</sup> *Id.* at 32.

<sup>57</sup> *Id.* § 3.1, at 11.

<sup>58</sup> *Id.*

<sup>59</sup> *Id.* at 35.

<sup>60</sup> *Id.* at 37.

<sup>61</sup> *Id.* at 12, 37.

<sup>62</sup> Twenty-one of the 46 GRI reports (or 45.6%) included a matrix. For analysis and critique of the GRI materiality matrix concept, see Mark W. McElroy, *Are Materiality Matrices Really Material?*, SUSTAINABLE BRANDS (Dec. 2, 2011) [http://www.sustainablebrands.com/news\\_and\\_views/articles/are-materiality-matrices-really-material](http://www.sustainablebrands.com/news_and_views/articles/are-materiality-matrices-really-material) (last visited 7/6/17).

<sup>63</sup> GRI IMPLEMENTATION MANUAL, *supra* note 40, at 37.

<sup>64</sup> Key organizations driving the creation of the IIRC were The Prince of Wales' Accounting for Sustainability Project, the Global Reporting Initiative, and the International Federal of Accountants. INTERNATIONAL INTEGRATED REPORTING COUNCIL, AM. INST. OF CERTIFIED PUB. ACCT. <https://www.aicpa.org/InterestAreas/BusinessIndustryAndGovernment/Resources/Sustainability/Pages/IntegratedReporting.aspx> (last visited 5/31/17).

<sup>65</sup> *Id.*; Peter A. Soyka, *The International Integrated Reporting Council (IIRC) Framework: Toward Better Sustainability Reporting and (Way) Beyond*, 23 ENVTL. QUALITY MGMT., no. 2, 2014, at 1-14.

<sup>66</sup> INTERNATIONAL INTEGRATED REPORTING COUNCIL, *supra* note 64.

activities, the International <IR> Framework was released at the close of 2013; it is the overarching governing document for integrated reporting.<sup>67</sup>

The <IR> Framework explicitly takes a principles-based approach to corporate reporting, aiming to “strike a balance between flexibility and prescription”<sup>68</sup> to accommodate variations in the individual circumstances of different reporting organizations. A key purpose of the Framework document was to establish the Guiding Principles that underpin creation of an integrated report.<sup>69</sup> Thus, the Framework stays away from dictating specific key performance indicators, measurement methods, or report content.<sup>70</sup> Instead, it recognizes that those with responsibility for report preparation must exercise judgment in determining what to report and how to report it.<sup>71</sup> That judgment is shaped and guided by the <IR> principles, chief among them the principle of materiality.<sup>72</sup>

#### <IR> MD Process

The <IR> Framework defines materiality by stating that an integrated report “should disclose information about matters that substantively affect the [firm’s] ability to create value over the short, medium and long term.”<sup>73</sup> The Framework

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<sup>67</sup> *Id.* Development of the Framework included an initial discussion paper of the integrated reporting concept and public consultation period on the paper, creation of a Prototype Framework along with a Pilot Programme of reporting using the prototype, further revisions to the Prototype Framework based on another round of public consultation, and finally, release of the official <IR> Framework. Lisa French, *From Framework inception to implementation: The IIRC’s history of consultation*, INT’L INTEGRATED REP. COUNCIL (Mar. 1, 2017), <http://integratedreporting.org/news/from-framework-inception-to-implementation-the-iircs-history-of-consultation/>; 5/31/17.

<sup>68</sup> <IR> FRAMEWORK, *supra* note 38, ¶ 1.9, at 7.

<sup>69</sup> *Id.* at 4.

<sup>70</sup> *Id.* ¶ 1.10, at 7.

<sup>71</sup> *Id.*

<sup>72</sup> So critical is the materiality concept that the IIRC canon on the topic incorporates several documents in addition to the Framework. *See, e.g.*, INT’L FED. OF ACCT., MATERIALITY IN <IR>: GUIDANCE FOR THE PREPARATION OF INTEGRATED REPORTS (2015); AM. INST. CERTIFIED PUB. ACCOUNTANTS (AICPA), MATERIALITY BACKGROUND PAPER FOR <IR> (2013).

<sup>73</sup> <IR> FRAMEWORK, *supra* note 38, ¶ 3.17, at 18. The IIRC’s approach to defining materiality evolved over time as part development of the framework. The earliest iteration appeared in a Prototype Framework document, circulated in late 2012. The Prototype Framework included a specific definition of materiality, as did the Consultation Draft of the Framework, published in early 2013. The formulation of “materiality” was fundamentally the same in these two early drafts. The Prototype Framework defined material matters as those of “such relevance and significance” that they could influence decisions by internal or external constituents, while the Consultation Draft defined them as those of “such relevance and importance” that they could influence decisions by internal or external constituents. INT’L INTEGRATED REP. COUNCIL, INTEGRATED REPORTING <IR> PROTOTYPE FRAMEWORK, 21 (2012); INT’L INTEGRATED REP. COUNCIL, CONSULTATION DRAFT OF INTERNATIONAL <IR> FRAMEWORK 26 (2013), available at <http://integratedreporting.org/wp-content/uploads/2013/03/Consultation-Draft-of-the-InternationalIRFramework.pdf>. In response to stakeholder feedback on the Consultation Draft, the final Framework changed direction in terms of defining materiality and connected the concept more specifically to the overarching idea behind integrated reporting: to report on matters that affect the firm’s ability to create value. For discussion and analysis of stakeholder comments on issues related to materiality, *see* INT’L INTEGRATED REP. COUNCIL, FRAMEWORK DEVELOPMENT: TECHNICAL AGENDA PAPERS, CONSULTATION QUESTION ANALYSIS FOR QUESTIONS 11 AND 12 (2013), available at <http://integratedreporting.org/wp-content/uploads/2013/10/QUESTION-11-and-12.pdf>; INT’L INTEGRATED REP. COUNCIL, SUMMARY OF

continues by outlining the materiality determination process for <IR>, which employs the same “funnel” concept as the GRI MD Process.

Identification of relevant topics is the starting point in the MD Process and focuses on cataloging matters that have a past, present, or future effect on the firm’s strategy, its business model, or on the different forms of capital it uses.<sup>74</sup> The Background Paper sets out specific minimum factors for consideration in identifying relevant topics, including the firm’s value drivers, matters identified during stakeholder analysis and engagement, and other external and internal factors.<sup>75</sup>

As with the GRI MD Process, the <IR> Process contemplates that the universe of relevant issues is far too broad for reporting purposes.<sup>76</sup> Thus, the second step in the MD Process is to winnow out material matters by assessing the importance of identified relevant topics. “Material” topics are those that are of such importance that they have the potential to substantively affect assessments of the firm’s ability to create value over time.<sup>77</sup> In assessing importance, the <IR> MD Process distinguishes between matters that are certain to occur and those that are uncertain to occur.<sup>78</sup> For matters that are certain to occur, importance is determined by looking at the magnitude of the matter’s effect on the firm’s ability to create value.<sup>79</sup> Where it is uncertain whether a matter will occur, firms should take both the magnitude of the effect and the likelihood of the event’s occurrence into consideration in assessing importance.<sup>80</sup> Finally, once the firm identifies the population of material topics, the firm prioritizes those topics based on the magnitude of their effect.<sup>81</sup> Matters with the greatest effect (or potential effect) on

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SIGNIFICANT ISSUES 25 (2013), available at <http://integratedreporting.org/resource/summary-of-significant-issues/>.

<sup>74</sup> <IR> BACKGROUND PAPER, *supra* note 40, ¶ 14, at 3.

<sup>75</sup> *Id.* ¶ 16, at 3-4. The external factors include “macro and micro economic changes, market forces, the speed and effect of technological changes, societal issues, environmental challenges, the legislative and regulatory environment, and matters identified by the organization’s risk management process.” *Id.* at 4. Internal factors include the “organization’s capacity to exert leverage on its relationships and the organization’s competence/capacity to respond to changing conditions.” *Id.* The goal of including these factors is to link the materiality determination process with the firm’s management processes. SUSTAINABILITY, *supra* note 5, at 16.

<sup>76</sup> <IR> FRAMEWORK, *supra* note 38, ¶ 3.24, at 19.

<sup>77</sup> <IR> BACKGROUND PAPER, *supra* note 40, ¶ 20, at 4.

<sup>78</sup> Examples of “certain” events are matters that are historically probable or events mandated by regulation. Uncertain events are primarily future events that may happen, but which are not necessarily indicated by an historical analysis. *Id.* ¶¶ 20, 27, at 4,6.

<sup>79</sup> <IR> FRAMEWORK, *supra* note 38, ¶ 3.24, at 19; <IR> BACKGROUND PAPER, *supra* note 40, ¶ 20, at 4. Magnitude is evaluated by determining “whether the matter’s effect on strategy, governance, performance or prospects is such that it has the potential to substantively influence value creation over time.” <IR> FRAMEWORK, *supra* note 38, at 19. The <IR> Background Paper describes a variety of quantitative and qualitative factors that firms should consider in assessing the magnitude of impact, including financial, operational, strategic, reputational and regulatory perspectives of the effects; the area of the effect (internal and external to the organization); and the timeframe of the effect. <IR> Background Paper, *supra* note 40, ¶ 25 at 5.

<sup>80</sup> <IR> BACKGROUND PAPER, *supra* note 40, ¶ 27 at 6.

<sup>81</sup> <IR> FRAMEWORK, *supra* note 38, ¶ 3.28 at 19.

the firm's value creation prospects have the greatest call to be included in the integrated report.<sup>82</sup>

The <IR> construct includes two additional disclosure items related to, but not specifically a part of, the MD Process. First, the Background Paper states a clear expectation that a firm's integrated report will disclose the materiality determination process it employed, including the process used to identify relevant matters and to narrow down relevant matters to material matters.<sup>83</sup> The <IR> Framework also identifies that an integrated report should disclose the internal parties charged with responsibility for the report.<sup>84</sup>

The academy shows a growing interest in various aspects of sustainability reporting, including materiality. However, most academic research to date has been theoretical, rather than applied.<sup>85</sup> Critics argue that the GRI and <IR> materiality definitions are broad<sup>86</sup> and difficult to implement.<sup>87</sup> However, only limited empirical research has been conducted to support these criticisms; the research that does exist is often focused on firms from specific countries.<sup>88</sup> This study aims to fill some of this empirical gap by investigating how companies have actually implemented the MD Processes delineated under the GRI and <IR> frameworks. Empirical study of materiality is important for two primary reasons. First, sustainability reporting is generally on the rise and the upward trajectory gives no hint of plateauing. The increase in GRI reports is illustrative: in 2007, companies submitted 986 reports to GRI. In 2011, this number rose to 3,922 and

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<sup>82</sup> <IR> BACKGROUND PAPER, *supra* note 40, ¶¶ 33-34, at 8.

<sup>83</sup> *Id.* ¶ 39, at 10.

<sup>84</sup> <IR> FRAMEWORK, *supra* note 38, ¶ 1.20, at 9.

<sup>85</sup> Instances of applied academic research are generally in one of two categories: research in the form of case studies under one of the reporting frameworks, or research around analytical tools for sustainability reporting. For examples of the first type see Chia-Wei Hsu et al., *Materiality Analysis Model in Sustainability Reporting: A Case Study at Lite-On Technology Corporation*, 57 J. OF CLEANER PROD. 142-51 (2013); María Jesus Muñoz-Torres et al., *Materiality Analysis for CSR Reporting in Spanish SMEs*, 1 INT'L J. OF MGMT., KNOWLEDGE & LEARNING 231-250 (2012); Hong Yuh Ching et al., *Analysis of Sustainability Reports and Quality of Information Disclosed of Top Brazilian Companies*, INT'L BUS. RES. October 2013, at 62-76. For an example of research on analytical tools, see Armando Calabrese et al., *A Fuzzy Analytic Hierarchy Process Method to Support Materiality Assessment in Sustainability Reporting*, 121 J. OF CLEANER PROD., 248-64 (2016).

<sup>86</sup> Chiu, *supra* note 40, at 378.

<sup>87</sup> DELOITTE, DISCLOSURE OF LONG-TERM BUSINESS VALUE: WHAT MATTERS? 9 (2012) (noting the difficulty in living up to the "spirit of the GRI guidelines").

<sup>88</sup> Practitioner communities, specifically accounting firms, are probably the leading producers of empirical research on implementation of the GRI and <IR> frameworks. For the most part, accounting firms focus on analyzing country-specific reporting. See, e.g., DELOITTE, ED. 3, INTEGRATED REPORTING: NAVIGATING YOUR WAY TO A TRULY INTEGRATED REPORT (2012) (explaining a limited study of South African <IR> reporting companies and their implementation of the <IR> reporting framework). An exception to this focused approach is a study conducted by the Association of Chartered Certified Accountants (ACCA) on materiality and conciseness in integrated reporting. See generally, ACCA, FACTORS AFFECTING PREPARERS' AND AUDITORS' JUDGMENTS ABOUT MATERIALITY AND CONCISENESS IN INTEGRATED REPORTING (2016) (this study included review of more than 200 <IR> reports and interviews with corporate personnel charged with preparing <IR> reports to gather data on implementation of <IR> principles).

the number for 2016 was 6,107.<sup>89</sup> At the same time that firms continue to invest resources in the preparation of sustainability reports, report users are dissatisfied with the results. Investors, in particular, continue to express unhappiness with the state of sustainability reporting.<sup>90</sup> This twin dynamic argues for studying sustainability reporting with an eye to improving reporting frameworks and company processes. Investigating actual application of key reporting frameworks will illuminate how firms can more effectively utilize their reporting resources to produce better quality information. Thus, empirical study of the reporting frameworks and the bedrock materiality concept is both timely and important.

## II. STUDY METHODOLOGY

This remainder of this article describes the results of an empirical study of the materiality determination process of 96 company sustainability or integrated reports, prepared under the GRI G4 Guidelines or the <IR> Framework. The focus of the study was on compliance with the materiality determination process of the reporting framework; the project also investigated additional factors related to the materiality concept.

### *A. Database Structure and Population*

The results in this study are based on examination of two datasets of sustainability reports, both constructed from publicly available reports. The first dataset is comprised of 50 <IR> reports from the IIRC Examples database, which the IIRC identified as exemplars of materiality statements. These reports were reviewed for industry and geographic distribution.<sup>91</sup> A comparison dataset of 46 reports was then constructed from GRI reports that replicated the geographic and industry distribution and which were prepared “in accordance” with GRI standards.<sup>92</sup>

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<sup>89</sup> GRI SUSTAINABILITY DISCLOSURE DATABASE, <http://database.globalreporting.org/> (accessed 7/6/17). A second non-profit organization, Corporate Register, currently has a repository of over 87,000 sustainability reports. CORPORATE REGISTER, <http://www.corporateregister.com/> (accessed 7/6/17).

<sup>90</sup> See, e.g., Emily Chasen, *Investors Want More From Sustainability Reporting, Says Former SEC Head*, WALL STREET JOURNAL: CFO JOURNAL (Nov. 15, 2015, 4:36 PM), <https://blogs.wsj.com/cfo/2015/11/12/investors-want-more-from-sustainability-reporting-says-former-sec-head/>; Michael Cohn, *Investors Want More Sustainability Info*, ACCOUNTING TODAY (July 22, 2015, 5:45 PM), <https://www.accountingtoday.com/opinion/investors-want-more-sustainability-info>. A study conducted in 2014 identified incongruities between stakeholder expectations and sustainability reports. Marianne Bradford et al., *Sustainability Reports: What Do Stakeholders Really Want?*, MGMT. ACCT. Q., Fall 2014, at 13-18.

<sup>91</sup> Data analysis did not reveal any disclosure patterns tied to specific industries or geographic regions. Neither the type of business the company engaged in nor the location of its operations affected whether or to what extent it disclosed information on its MD Process or any of the attendant coding items.

<sup>92</sup> All reports in the GRI dataset represented either the GRI G3.1 or G4 Reporting Guidelines. The MD Process is identical for the two iterations of the Guidelines.

### B. Content Analysis

The project utilized content analysis to assess the materiality disclosure of the sample reports. Content analysis is a research technique that uses a set of procedures to make replicable and valid inferences from text.<sup>93</sup> Content analysis is a method widely adopted in corporate disclosure studies.<sup>94</sup> The content analysis process for the study focused on reading and coding the reports to determine their adherence to the reporting framework's MD Process.

Coding instruments were created for each set of reports and were based primarily on the reporting frameworks' publicly available documents on the MD process.<sup>95</sup> The study also coded for items outside the published MD process but which are natural corollaries of a robust MD process. For example, stakeholder engagement is an important component of both the <IR> and GRI MD processes, though the frameworks contain only limited items related to stakeholder engagement. To obtain a better understanding of how companies operationalized stakeholder engagement and its connection to the MD process, coders reviewed reports for several items related specifically to the issue of stakeholder engagement. Coding items were divided into three categories: basic, mid-level, and high-level--to denote varying degrees of sophistication in discussion of the MD process.<sup>96</sup> These three levels roughly approximated three types of disclosure: 1) disclosure asking for identification or listing of a specific item; 2) disclosure asking for an explanation of how the identification or list of the item was determined; and 3) disclosure asking for explanation of internal and external governance over identification of the item.

Once a prototype coding instrument had been constructed, the student research team went through an introductory session and training on the MD process generally, the <IR> MD process specifically, and the coding instrument itself. Members of the student research team coded an initial mini-set of 10 <IR> reports individually, using the coding instrument. The team met to compare coding results to ensure consistent interpretation of coding items and report language, and to refine the coding instrument itself. The coding team then coded the remaining <IR> reports, with results again reviewed to identify possible areas of inconsistent interpretation. Project supervisors utilized spot checks of report coding to ensure consistent application of the coding instrument. The project team repeated the process for the GRI reports. Data from the coding instruments was transferred to Excel for analysis both within each reporting framework and across the two reporting frameworks.

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<sup>93</sup> ROBERT PHILIP WEBER, BASIC CONTENT ANALYSIS 9 (Michael S. Lewis-Beck et al. eds., 2nd ed. 1990); KLAUS KRIPPENDORFF, CONTENT ANALYSIS: AN INTRODUCTION TO ITS METHODOLOGY 18 (Margaret H. Seawell et al., eds., 2nd ed. 2014).

<sup>94</sup> Giacomo Manetti, *The Quality of Stakeholder Engagement in Sustainability Reporting*, 18 CORP. SOC. RESP. & ENVTL. MGMT. 110, 110-12, 115 (2011).

<sup>95</sup> For GRI reports, the coding instrument was drawn from the GRI IMPLEMENTATION MANUAL, *supra* note 40, at 11-12, 32-39. For <IR> reports, we relied on the <IR> FRAMEWORK, *supra* note 38, at 18-19 and <IR> BACKGROUND PAPER, *supra* note 40, at 1-10.

<sup>96</sup> Coding sheet template for each dataset is attached. See *infra* Appendix A.

### III. ISSUE IDENTIFICATION AND ANALYSIS

#### A. Overview

The discussion of sustainability reporting in Section II<sup>97</sup> highlights key distinctions between the GRI and <IR> frameworks. Given these differences, we expected that the study data might reveal significant differences in responses and reporting issues. However, this was not the case. Although specific percentages varied, patterns of performance were generally consistent between the GRI reporting firms and the <IR> reporting firms. We uncovered few significant differences in disclosure attributable to a specific reporting framework.

Our analysis did surface three broad disclosure issues, common to firms under both frameworks. First, adherence to all components of the respective MD Processes was inconsistent, with many companies completing some of the components, but relatively few firms completing the entire Process. Firms also generally struggled to connect their stakeholder engagement activities to the MD Process. Many of the reports had extensive discussion of the firms' engagement processes, but this often lacked any recognition of the role of stakeholder input in the MD Process. Last, disclosure on the issue of internal accountability for the MD Process, raising questions as to the integrity of the reporting process. We turn now to a detailed analysis of issues in these three areas under each of the reporting frameworks.

#### B. Issue #1: Gaps in MD Process Implementation

The MD Process is essentially a tool to help reporting companies identify and report on "material" issues. By definition, determining materiality eliminates some issues from discussion in the report. While this reduction is necessary, it underscores the need for a clearly defined *process* for determining materiality.<sup>98</sup> Both the GRI and <IR> frameworks recognize the role of process in assisting report users to assess the value of information for disclosure purposes.<sup>99</sup> The majority of data collected and analyzed related to firms' implementation of the MD Processes described in Section II above.<sup>100</sup>

##### 1. Coding items

The core of the coding instrument was comprised of the key steps in the framework MD Processes - identify relevant matters, assess relevant matters to identify material matters, prioritize material matters - with sub-factors as set out in

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<sup>97</sup> See *supra* notes 38-83 and accompanying text.

<sup>98</sup> Eccles & Youmans, *supra* note 9, at 5.

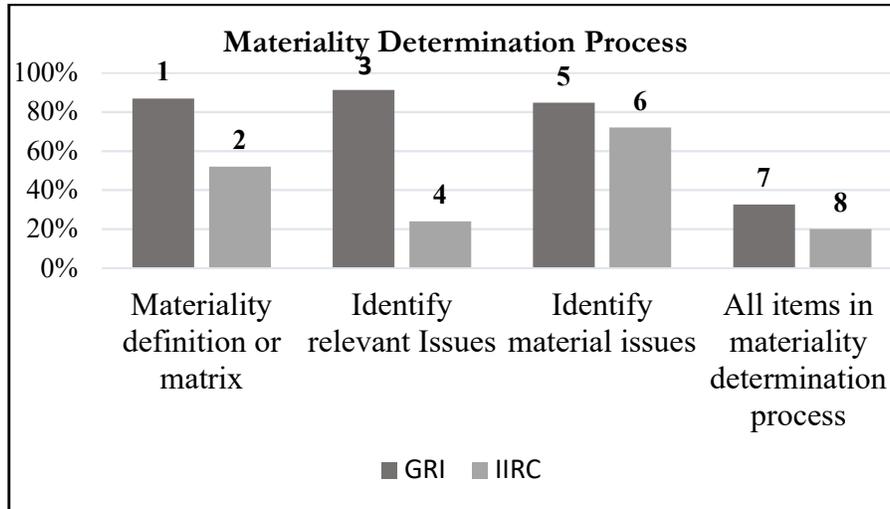
<sup>99</sup> See, e.g., GRI PRINCIPLES, *supra* note 38, ¶ 2.2, at 7-8 (describing the steps in using the GRI guidelines for report preparation); <IR> FRAMEWORK, *supra* note 38, at 18, Guiding Principle 3D - Materiality (describing materiality determination as a process).

<sup>100</sup> See *supra* notes 48-82 and accompanying text.

the framework documents.<sup>101</sup> We also coded for a baseline issue implicit in the MD Processes. We looked for whether the report:

- Contained a definition of materiality or a materiality matrix;
- Included discussion of all steps and factors specifically part of the relevant MD Process.

## 2. Data Analysis and Discussion



**Table 1:** Materiality Determination Process

The MD Process comprised the largest portion of coded items and had the potential to show the greatest complexity and divergence in company responses. In fact, analysis of disclosure on these items displayed several quite clear patterns. The data revealed strong levels of disclosure on a few individual coding items, but also serious gaps in the application of the MD Processes. Most notably, our analysis showed that only a small percentage of firms completed the entire MD Process. This issue also saw some of the most significant differences in disclosure levels between GRI and <IR> reporting firms.

The starting point in considering materiality is definitional: how does the reporting firm define “materiality”? Both the reporting frameworks contain definitions of “materiality,” but it is possible that firms will alter that definition or create their own definition. Investigation of this issue looked for a statement setting out the firm’s definition of materiality or for the presence of a materiality matrix. GRI introduced the concept of the materiality matrix as a visual depiction of the GRI materiality definition for use in its MD Process.<sup>102</sup> Thus, a materiality matrix could be construed as a proxy for a definition of materiality.<sup>103</sup> As Table 1,

<sup>101</sup> See *infra* Appendix A.

<sup>102</sup> See *supra* notes 61-62 and accompanying text.

<sup>103</sup> Overall, use of a materiality matrix was a minority practice for both GRI and <IR> firms: only 36 out of the 96 (37.5%) reports in the combined datasets used a matrix. Although the matrix figures

columns 1 and 2 show, GRI disclosure on this bedrock element was sound, with 87% of firms disclosing either a definition of materiality or a materiality matrix. Disclosure by <IR> firms was substantially lower at 52%. The reason for the disparity between GRI and <IR> reporting on this issue is unclear, but several possibilities exist. At first, it seemed that <IR> reporters perhaps assumed that report users would know that the report incorporated the <IR> definition of materiality (ability to create value) and its focus on providers of financial capital as the audience for the report.<sup>104</sup> However, as we shall find later, most <IR> reports contained discussion of engagement with stakeholders beyond just investors.<sup>105</sup> That discussion seemed to indicate that <IR> reporters, in fact, were not using, or at least not strictly construing, the <IR> materiality definition. It is also possible that <IR> reporters are still struggling to connect their integrated reports to the concept of materiality. Whatever the explanation, the low level of disclosure on this foundational item did not bode well for <IR> reporters' implementation of the MD Process.

Investigation of key elements of the MD Processes also repeated some of this pattern, with higher levels of disclosure on individual items by GRI reporters and generally lower disclosure by <IR> reporters. For example, the first step in both frameworks' MD Process is for the firm to identify "relevant" issues, the pool from which material issues are gleaned.<sup>106</sup> This would seem to be a relatively simple task, especially as it may already be part of existing strategy or risk management processes. We expected robust disclosure on this step and saw it in GRI reporters, 91% of whom disclosed their relevant issues (Table 1, column 3). <IR> disclosure was disappointingly low, with a meager 24% of firms disclosing on this critical step (Table 1, column 4). Low disclosure may indicate that more <IR> firms are skipping this step in the MD Process.<sup>107</sup> This has ramifications for the MD

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prominently in the GRI Implementation Manual's discussion of the MD Process, fewer than half of GRI firms in the sample used a matrix (21 of 46). Among firms that used a matrix, we uncovered a variety of different factors used for matrix axes. Of the 36 reports that included a matrix, only two used the axes given in the GRI Implementation Manual (impact on stakeholders and influence on stakeholder decisions). See CANARY WHARF GROUP, PLC, PRIDE OF PLACE: SUSTAINABILITY REPORT 2014 49 (2014); NIAEP JSC, ANNUAL REPORT 2015 9 (2015). One firm employed a matrix that assessed the "probability" and "severity" of the occurrence of identified issues. See GOLD FIELDS, INTEGRATED ANNUAL REPORT 2015 46 (2015) [hereinafter GOLD FIELDS IAR]. Several natural resource and extractive firms utilized a risk matrix. See CAIRN ENERGY, CORPORATE RESPONSIBILITY GRI REPORT 2015 13 (2015); EXXARO, INTEGRATED REPORT 2014 34-37 (2014). The clear majority of reports – 29 of the total of 36 – used a matrix that measured stakeholder concern/impact along one axis and impact on business along the other axis. See, e.g., CEMEX, CONCRETE SOLUTIONS FOR A SUSTAINABLE FUTURE: SUSTAINABLE DEVELOPMENT REPORT 2015 12 (2015); ACCESS BANK PLC, SUSTAINABILITY REPORT 2014 22 (2014).

<sup>104</sup> See *supra* note 66 and accompanying text and *infra* notes 120-24 and accompanying text.

<sup>105</sup> See *infra* notes 120-24 and accompanying text.

<sup>106</sup> See *supra* notes 56-57, 74-75 and accompanying text.

<sup>107</sup> An additional possible explanation for <IR> reporters' low disclosure on this issue was the <IR> framework's focus on the principle of conciseness and its push for short reports. <IR> FRAMEWORK, *supra* note 38, at 21, ¶ 3E. However, in our sample, <IR> reports were not necessarily shorter than reports prepared under the GRI framework. Rio Tinto's report was 224 pages, while John Keells Holdings produced a hefty 316-page integrated report. See RIO TINTO, ANNUAL REPORT 2011 (2012); JOHN KEELLS HOLDINGS, PROGRESSIVE: ANNUAL REPORT 2012/2013 [hereinafter KEELLS ANNUAL REPORT], [www.examples.integratedreporting.org](http://www.examples.integratedreporting.org). Further, of those firms (both GRI and

Process as it could cause firms to miss important new issues by focusing too early on a small issue set. A second possible explanation is that firms are actually performing this step but are not disclosing their findings. For example, some firms refer to “relevant” issues in their discussion of materiality, but do not identify what their relevant issues are. Leaving out this part of the process has implications for report users in that they do not know the firm’s starting point in the MD Process. Disclosure on this issue aids report users’ understanding of the firm’s thinking as it identifies issues; lack of disclosure leaves report users to wonder whether the firm has seen issues and decided they are not “relevant” to the firm or simply missed issues altogether.

The next step in the MD Process, identifying material issues, underscores the importance of disclosing identified relevant issues. Identifying material issues works from the pool of “relevant” issues to surface the most significant issues for the firm. Identification of material issues is the end-product of working through the MD Process and acts to give report users a clear idea of the firm’s areas of focus for the report. This is also an item more notable where absent: reports prepared without taking this crucial step can lack focus and be overly broad or generic.<sup>108</sup> Such reports may not be clear as to why the firm is addressing the issue. More importantly, skipping this step undercuts the whole point of reporting – i.e., to discuss *material* issues and only material issues. Given the fundamental nature of this step, we expected solid disclosure on this item and it was generally so, with over 84% of GRI firms clearly disclosing their material issues and 72% of <IR> firms doing so (Table 1, columns 5 and 6). Of course, the additional reporting challenge is to move past merely identifying issues to disclose how the firm moved from its relevant issues to its material issues. Itaú Unibanco Holding S.A., a Brazilian financial services company, provided one of the best examples of explaining this critical part of the MD Process. It very clearly designated the steps in its process, starting with its pool of relevant issues. Through narrative and graphics, it described the steps (e.g., internal climate surveys, presentations to investors, engagement with non-profit sustainability organizations) used to narrow its focus to material issues.<sup>109</sup>

The relatively high levels of firm disclosure of material issues led us to hypothesize that many firms were actively using the MD Processes to arrive at their material issue identification. However, analysis of data on disclosure on *all* steps in the MD Processes showed that this was not the case. Columns 7 and 8 of Table

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<IR>) that reported on all MD Process items, several were under 100 pages. *See, e.g.*, DE BEERS, BUILDING FOREVER: REPORT TO SOCIETY 2014 (2014) (a GRI Core report of 52 pages); ITAÚ UNIBANCO HOLDING S.A., INTEGRATED REPORT 2015 (2016) [hereinafter ITAÚ, INTEGRATED REPORT] (an <IR> report of 73 pages). At just 24 pages, Reckitt Benckiser’s GRI report was the shortest report that disclosed all MD Process items. *See* RECKITT BENCKISER, BETTER BUSINESS: SUSTAINABILITY REPORT 2015 (2015). These reports demonstrate that it is possible to disclose implementation of the entire MD Process in a relatively short report and would seem to indicate that report length is not a factor in the low levels of disclosure here.

<sup>108</sup> SustainAbility commented on the disconnect between “how much companies report: and “what information is actually useful,” noting that companies often create reports “whose very length may ... obscure information.” SUSTAINABILITY, *supra* note 5, at 15.

<sup>109</sup> ITAÚ INTEGRATED REPORT, *supra* note 107, at 45; *see also* GOLD FIELDS IAR, *supra* note 103, at 43-44.

1 reveal that implementation of the *entire* MD Process was surprisingly low for both GRI and <IR> firms: only 20% of <IR> firms applied the entire Process and just under one-third of GRI firms did so.

The data points represented in Table 1, columns 5 and 6 and columns 7 and 8 raised intriguing questions on how firms were implementing the MD Process. The issue is one of disconnect between the process and the end-product. The MD Process is just that – a process to be used to determine a firm's material issues. Theoretically, a firm should not be able to generate a list of material issues without having utilized the *entire* MD Process. Yet, a significant number of reports in both the GRI and <IR> datasets contained the end-product of a process that was not implemented in its entirety. The obvious question is, if firms are not employing the whole MD Process, how are they determining their material issues? Are they not using the MD Process or just not disclosing their use of the MD Process?<sup>110</sup>

Equally important for our research was whether there were any patterns in the gaps in implementation of the MD Processes. To determine this, we analyzed data on responses to the individual factors in each step of each framework's MD Process. Tables 2 and 3 below show disclosure levels for each item of the

GRI Reporting Process			
Application of GRI Materiality Determination Process		No. of Reports	Percent
<b>Step 1)</b>	Identification of "relevant" topics		
	Report contains list of relevant topics	42	91%
	Identification of relevant topics reflects GRI definition of 'relevant'	38	83%
	Identification of boundaries for topics	35	76%
<b>Step 2)</b>	Prioritization		
	Report considers extent to which relevant topics reflect economic, environmental, and or social impacts	37	80%
	Report considers extent to which relevant topics substantively influence assessments and decisions of stakeholders	36	78%
<b>Step 3)</b>	Validation		
	Report assesses material topics against principle of stakeholder inclusiveness	32	70%
<b>Step 4)</b>	Review		
	Report discloses organization's process to review report post-publication	28	61%

respective frameworks.

**Table 2:** GRI MD Process

<sup>110</sup> These big picture questions are largely beyond the scope of the present study. However, our data did reveal an interesting possible disconnect between use of the MD Process and disclosure of its use. See *infra* pp. 40-41

<b>IIRC Reporting Process</b>			
<b>Application of IIRC Materiality Determination Process</b>		<b>No. of Reports</b>	<b>Percent</b>
<b>Step 1)</b>	Identification of relevant matters: discussion includes consideration of:		
	Clear identification of material issues	36	72%
	Organizational value drivers	44	88%
	Issues identified in stakeholder analysis/engagement	29	58%
	Other external and internal factors	36	72%
	Organization's performance in reporting cycle	40	80%
	Effect of above factors on business model, strategy, capitals	42	84%
<b>Step 2)</b>	Assessment of importance of relevant matters		
	For matters that are certain to occur: assesses magnitude of effect on org.	39	78%
	For matters not certain to occur: assess magnitude of effect on org.	38	76%
<b>Step 3)</b>	Prioritization of material matters by importance	30	60%

**Table 3:** <IR> MD Process

Review of the data in Tables 2 and 3 reveals moderate levels of disclosure overall, with most companies missing one or more items in the MD Process. For GRI companies, the most frequently omitted item was Step 4 – Review. This item relates to continuous improvement of the firm’s GRI reporting by asking the firm to disclose the processes it uses to leverage the report for future reporting (Table 2).<sup>111</sup> Less than two-thirds of reports identified these internal processes. This could indicate that many firms view reporting as an ad hoc event, not connected to firm strategy. It could also mean that the firm has no reporting strategy and/or inadequate internal governance over reporting. For <IR> reporters, the largest single challenge seems to be prioritizing material matters (Table 3),<sup>112</sup> with less than two-thirds of firms disclosing their prioritization. It is possible that firms simply are not prioritizing their material issues, though this seems unlikely. Prioritization is a basic resource allocation concept, one that firms employ all the time. It is perhaps more likely that firms, in fact, prioritize and, therefore, address issues differently, but do not want to disclose this for fear of alienating stakeholder groups with interest in specific issues.<sup>113</sup>

Tables 2 and 3 also reveal a common issue between GRI and <IR> reporting firms that signals an important challenge for the MD Processes. Both MD

<sup>111</sup> GRI IMPLEMENTATION MANUAL, *supra* note 40, at 33.

<sup>112</sup> Once “material” issues are identified, the <IR> framework instructs that firms prioritize those issues based on their “magnitude.” <IR> FRAMEWORK, *supra* note 38, ¶ 3.28, at 19.

<sup>113</sup> *E.g.* GOLD FIELDS IAR, *supra* note 103, at 44 (good example of description of a prioritization process).

Processes contain an item specifically related to stakeholder engagement, reflecting the important role stakeholders play in determining materiality. For GRI reporters, this is reflected in Step 3 of the process, which asks firms to “validate” their material topics against their stakeholder engagement processes (Table 2, Step 3). The <IR> MD Process specifically ties stakeholder engagement to the identification of relevant issues (Table 3, Step 1 – Issues identified in stakeholder analysis/engagement). Both GRI and <IR> firms alike struggled to disclose how they incorporated stakeholder analysis and engagement into their MD Process, as reflected in the modest levels of disclosure on the respective items (67% of GRI firms, 58% of <IR> firms). The integrated report of Sri Lankan company John Keells Holdings PLC contains a successful discussion of the connection between stakeholder engagement and materiality. The report sections describing the firm’s materiality determination are titled “Stakeholder engagement process” and “Engagement of significant stakeholders,” drawing a clear line between materiality and stakeholders.<sup>114</sup>

Our data indicated that firms are not ordinarily shy about reporting on their stakeholder engagement efforts.<sup>115</sup> Thus, we were somewhat surprised that stakeholder inclusion seemed to create a challenge for reporting companies. This could be because firms do not see a connection between their stakeholder engagement efforts and the identification of material issues. It could also indicate, for some firms, poor quality stakeholder engagement that cannot realistically influence company decisions. For <IR> reporters, it may also indicate uncertainty as to the firm’s relationship with stakeholders, especially as input for reporting, where the report audience is clearly identified as investors, rather than stakeholders more generally.

### 3. MD Process Summary

Materiality determination has been called one of the “most complicated [sustainability]-related decisions for senior management.”<sup>116</sup> Our analysis underscores this sentiment, revealing one consistent theme: inconsistency in utilization of MD Processes. The vast majority of reports we studied showed gaps in the use of relevant MD Processes and spotty use of MD factors. Generally, firms reported well on basic identification items, but demonstrated significant slippage in disclosure as they moved through the steps of the MD Process (e.g., moving from identification of relevant to material issues, or from identifying material issues to their prioritization). In particular, firms struggled with the all-important issue of connecting their stakeholders to the selection of material issues.

The issue of stakeholder analysis and engagement is of such importance to both the GRI and <IR> MD Processes that we collected data on factors not specifically included in the MD Processes, but needed for good-quality stakeholder engagement. This article turns now to an examination of the key issues uncovered with regard to stakeholder engagement.

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<sup>114</sup> KEELLS ANNUAL REPORT, *supra* note 107, at 48, 54-58. Although we accessed this report via the IIRC Examples Database, the report utilizes GRI G3.1 reporting framework. *Id.* at 4.

<sup>115</sup> See *infra* notes 134-36 and accompanying text.

<sup>116</sup> DELOITTE, *supra* note 87, at 2.

### C. Issue #2: Disconnect in Stakeholder Engagement

Stakeholder engagement (SE) is of critical importance for corporate reporting in general and for the MD Process in particular. Sustainability reporting usually focuses on providing non-financial information to a broad range of stakeholder groups.<sup>117</sup> Sometimes overlooked is the importance of stakeholder input into the reporting and disclosure process. The connection between stakeholder input and reporting output is the materiality determination process, through which stakeholder concerns influence the content of a firm's sustainability report.

While both the GRI and <IR> frameworks incorporate stakeholder analysis and engagement, they do so in somewhat different ways. Philosophically, this area is one of the most significant differences between the two frameworks. For GRI, stakeholders are fundamental to the definition of materiality, for purposes of reporting. GRI *defines materiality in terms of* a firm's impact on stakeholders or influence on their decisions.<sup>118</sup> The GRI MD Process, specifically the prioritization step, reflects stakeholders' position as part of GRI's definition of materiality. After identifying all relevant topics, GRI reporters determine "material" topics by looking for topics that have the greatest stakeholder impact and/or greatest influence on stakeholder decisions.<sup>119</sup> Given that stakeholders occupy a primary position in the GRI materiality determination process, we expected to see high levels of response to stakeholder-related disclosure items for firms reporting under the GRI framework.

By contrast, the <IR> Framework displays a less clear relationship between firms and stakeholders. The focus of an integrated report is placed on the group the IIRC identifies as the primary audience for such a report: providers of financial capital.<sup>120</sup> Though focusing primarily on investors, the <IR> Framework does recognize that stakeholders other than investors have ties to the firm, albeit indirect. Stakeholders appear to have only derivative importance in the <IR> world: they are important insofar as they affect the firm's value creation prospects.<sup>121</sup> One <IR> Fundamental Concept, for example, addresses this issue, stating that providers of financial capital are interested in the value an organization creates for external stakeholders "when it affects the ability of the organization to create value for itself..."<sup>122</sup> The <IR> Guiding Principle on stakeholder relationships underscores this sentiment. While it notes that an

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<sup>117</sup> Eccles & Youmans, *supra* note 9, at 4-5; YINING ZHOU, MATERIALITY APPROACH IN SUSTAINABILITY REPORTING: APPLICATIONS, DILEMMAS, AND CHALLENGES, 2-3 (2011), [http://epubs.scu.edu.au/bus\\_pubs/704/](http://epubs.scu.edu.au/bus_pubs/704/); SUSTAINABILITY, *supra* note 5, at 17.

<sup>118</sup> See *supra* note 50 and accompanying text. Sulkowski and Waddock argue that the GRI framework is intended not only for reporting but also as a framework for engaging with external stakeholders. Sulkowski & Waddock, *supra* note 14, at 1064.

<sup>119</sup> See *supra* notes 50, 61-62 and accompanying text.

<sup>120</sup> <IR> FRAMEWORK, *supra* note 38, ¶ 1.7, at 7 (stating that the "primary purpose of an integrated report is to explain to providers of financial capital how an organization creates value over time.").

<sup>121</sup> Mark W. McElroy, *Can There Be Meaningful Integrated Reporting?*, SUSTAINABLE BRANDS (Aug. 11, 2014), [http://www.sustainablebrands.com/news\\_and\\_views/new\\_metrics/mark\\_mcelroy/can\\_there\\_be\\_meaningful\\_integrated-reporting\\_part\\_2\\_2](http://www.sustainablebrands.com/news_and_views/new_metrics/mark_mcelroy/can_there_be_meaningful_integrated-reporting_part_2_2).

<sup>122</sup> <IR> FRAMEWORK, *supra* note 38, ¶ 2.5, at 10.

integrated report should “provide insight” into a firm’s relationships with key stakeholders, it echoes the Fundamental Concept’s focus on stakeholders’ impact on the firm’s value creation.<sup>123</sup> Thus, stakeholders are important to the concept of materiality insofar as they affect the firm’s ability to create value; this reflects the <IR> definition of materiality. Stakeholder input is incorporated into the <IR> MD Process as part of identifying relevant matters, where firms are charged with considering issues identified in stakeholder analysis and engagement as part of their topic identification.<sup>124</sup> The <IR> framework, thus, sets out a somewhat ambiguous relationship between reporting companies and their stakeholders, which may have affected <IR> reporters’ responses to stakeholder-related items.

A final issue related to stakeholders is essentially one of governance over the identification of stakeholders and over the engagement process. Neither the GRI nor the <IR> frameworks provide guidance on developing a coherent process for identifying stakeholders or ensuring that engagement is effective. Use of a third-party standard for stakeholder engagement is important to aid firms in creating engagement practices with credibility.<sup>125</sup> Perhaps the most commonly used standard for stakeholder engagement is AA1000SES Stakeholder Engagement Standard. Created by independent non-profit organization AccountAbility, the standard acts as an “accountability mechanism,” useful for distinguishing between good-quality engagement and poor-quality engagement.<sup>126</sup> AA1000SES also focuses on the incorporation of stakeholder engagement into firm decision-making; it sees engagement as connected to company strategy, including initiatives such as the MD Process.<sup>127</sup> While neither GRI nor <IR> require use of an external standard for stakeholder engagement, we coded for use of a standard (whether AA1000SES or some other standard) as a measure of firms’ commitment to good-quality engagement and its willingness to incorporate external guidance in building its stakeholder processes and practices.

### 1. Coding items

Investigation of firms’ stakeholder engagement disclosure included several items outside of the MD Processes. Specifically, we searched for whether the report contained:

- clear identification of stakeholder groups,
- description of how the firm identified its stakeholder groups,

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<sup>123</sup> “This Guiding Principle reflects the importance of relationships with key stakeholders because...value is...created through relationships with others.” *Id.* ¶¶ 3.10-3.11, at 17. During the public consultation period on the proposed <IR> framework, some respondents expressed concern with the focus on investors as the audience for <IR>, fearing that this automatically ranked investor interests above others. The <IR> framers essentially rejected these concerns in favor of continued focus on investors’ information needs, which they saw as related to value creation. *See* INT’L INTEGRATED REPORTING COUNCIL (IIRC), <IR> BASIS FOR CONCLUSIONS ¶¶ 3.1-3.4, at 5-6 (2013), <http://integratedreporting.org/wp-content/uploads/2013/12/13-12-08-Basis-for-conclusions-IR.pdf>.

<sup>124</sup> *See supra* note 72 and accompanying text.

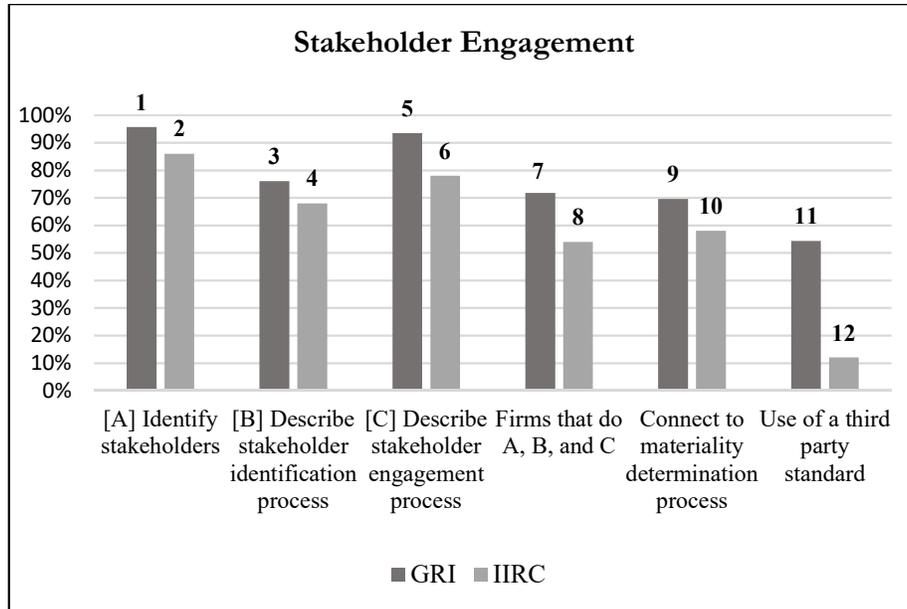
<sup>125</sup> ACCOUNTABILITY, AA1000 STAKEHOLDER ENGAGEMENT STANDARD 6 (2015).

<sup>126</sup> *Id.* at 5 (the standard sets out a framework for “assessing, designing, implementing and communicating an integrated approach” to stakeholder engagement).

<sup>127</sup> *Id.* at 15.

- description of the firm's stakeholder engagement activities, and
- disclosure on whether the firm utilized a third-party standard to construct and implement stakeholder engagement activities.

## 2. Data Analysis and Discussion



**Table 4:** Stakeholder Engagement Processes

Review of data on the SE coding items revealed several interesting points. First, levels of disclosure between GRI and <IR> reporters did not display the marked differences that might have been expected, based on the difference between the two frameworks' general approach to stakeholders. <IR> disclosure lagged somewhat behind GRI disclosure, but overall displayed the same patterns. Second, disclosure here mirrored the pattern shown in the MD data: firms had generally higher levels of disclosure on "identification" items, lower levels on "explain" items, and lower levels on all items combined.

Disclosure on basic identification items was strong for both GRI and <IR> firms. For example, identification of stakeholder groups had some of the highest levels of disclosure on any item in the study, with 95.6% of GRI firms and 86% of <IR> firms<sup>128</sup> providing the information (Table 4, columns 1 and 2).<sup>129</sup> Deeper

<sup>128</sup> A key concern expressed during development of the <IR> Framework was that explicitly identifying investors as the "audience" for <IR> would negatively impact how firms incorporated stakeholder concerns into integrated reports. This was sometimes expressed as a fear of investor capture of the <IR> reporting process. *See, e.g.*, INT'L INTEGRATED REPORTING COUNCIL, <IR>SUMMARY OF

analysis surfaced two possible problems with this seemingly simple item. Most firms identified a host of stakeholder groups – including everyone from customers to investors to government to employees to communities or “society” – but some firms did a better job of providing a rationale for their choices than others. A few firms explicitly described how they identified stakeholders. For example, Royal DSM’s report states that stakeholder groups were identified based on the “influence they have on the company’s operations, as well as whether they are significantly affected by them.”<sup>130</sup> Other companies provided more specific discussion of their relationships with identified stakeholder groups. Sasol created a graphic representation of stakeholder groups that “contribute to our value drivers” with a detailed explanation of how each group does so.<sup>131</sup> Masisa and Gold Fields provided charts naming specific stakeholder groups and explaining why the company engaged with that group, together with a discussion of engagement mechanisms.<sup>132</sup>

More often, firms employed a “list” approach to begin their stakeholder discussion, providing a listing of their stakeholder groups, but without discussion of how they determined their stakeholder groups or why the groups were included.<sup>133</sup> The data in Table 4, columns 3 and 4, which show lower levels of disclosure on the stakeholder identification process, reflect this omission. For these firms, the report user is either assumed to somehow understand the connection between the firm and the stakeholder groups or is left to puzzle out the connection on their own. Additionally, few firms explicitly prioritized their stakeholders, identifying which groups figured most heavily in their decision-making. One might assume that names on the list are set out in order of priority, but this is only an assumption, without any explicit support from the reports themselves.

Both GRI and <IR> firms had similarly high levels of disclosure for the description of their SE process (Table 4, columns 5 and 6), though <IR> disclosure here was slightly lower than for stakeholder identification.<sup>134</sup> In general, firms

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SIGNIFICANT ISSUES 26 (2013), <http://integratedreporting.org/wp-content/uploads/2013/12/13-12-08-Summary-of-significant-issues-IR.pdf>. Our data would seem to mitigate at least some of this concern. All but one of the <IR> firms we studied identified multiple stakeholder groups and none of them specifically prioritized investors as their most important stakeholders. In fact, a review of the listings of stakeholders in the reports revealed that only four firms named investors first. To the extent that the ordinal sequencing of the lists can be taken as a proxy for prioritization, only a small percentage of <IR> reporters – eight percent - appear to put investors ahead of other stakeholder groups.

<sup>129</sup> Although disclosure on this item was quite high, some firms provided no clear identification of their stakeholders. This subset of firms often used the term “stakeholders” in their reports and/or referred to “our stakeholders” but without ever identifying exactly whom they considered as their stakeholders.

<sup>130</sup> Royal DSM, BRIGHT SCIENCE, BETTER LIVING: INTEGRATED ANNUAL REPORT 2015 4 (2015); see also, ITAÚ INTEGRATED REPORT, *supra* note 107, at 45 (Itaú identifies stakeholders via its “Sustainable Performance Spiral”).

<sup>131</sup> SASOL, MAINTAINING MOMENTUM: ANNUAL INTEGRATED REPORT 2015 37 (2015).

<sup>132</sup> GOLD FIELDS IAR, *supra* note 103, at 11; ANNUAL REPORT: INTEGRATED REPORT 2013 48-51 (2013).

<sup>133</sup> One commentator has argued that a focus on inclusiveness might encourage firms to engage in a “superficial and box-ticking” approach to stakeholders, such as our data might suggest. See Chiu, *supra* note 40, at 377.

<sup>134</sup> One possible explanation for the lower <IR> disclosure relates to the <IR> stakeholder approach. It could be that <IR> firms are not clear on the relationship between the firm and its

seemed practiced at including “case study”-type stories and narratives describing interaction with their stakeholders (e.g., recounting their charitable donations or how employee volunteer hours were used, describing the use of focus groups, etc.). However, only a few firms went beyond story-telling to disclose an internal SE strategy/methodology. Votorantim Group, a Brazilian industrial conglomerate, provided the best example of this more sophisticated approach to SE. As part of its discussion of SE in local communities, Votorantim described the internal processes and tools it had developed for use by its internal business units. The company created its own “stakeholder engagement methodology,” constructed a Stakeholder Engagement Guide, and held training workshops for personnel directly involved with SE.<sup>135</sup>

The differences between the “story-telling” firms and those evidencing a more methodological approach to SE is indicative of the overall disclosure pattern, with lower levels of disclosure for “explanation” items and for all items combined than for pure “identification” items. Columns 3 and 4 of Table 4 illustrate this issue, with regard to disclosure on the process for identifying stakeholders falling to 76% for GRI and 68% for <IR>.<sup>136</sup> This drop-off in disclosure levels is repeated if we look at firms that disclose on all three items: fewer than three-quarters of GRI firms disclose on the entire first three coding items and just over half of <IR> firms do so. Unfortunately, high levels of disclosure on individual items gives way to disappointing levels on the complete set of items.

This focus on stakeholders underscores a baseline question: why should reporting firms engage with their stakeholders? Clearly, there are multiple motivations for doing so, one of which can be as input into the firm’s MD Process. Both the GRI and <IR> MD Processes explicitly call on firms to connect their SE to their MD Process, and some firms included this important connection. Eskom’s 2013 Integrated Report led the way in demonstrating how to explain the connection between SE and the MD Process. Its “approach to integrated reporting” contains a section titled “Determining materiality in partnership with Eskom’s stakeholders,” followed by a “Stakeholder materiality matrix.”<sup>137</sup> Unfortunately, not many companies followed Eskom’s example and disclosure on this critical item was generally lackluster. As columns 9 and 10 show, only a modest 69% of GRI reporters and 58% of <IR> reports draw a clear link between their SE and their MD Process.<sup>138</sup> This leaves many reports that may identify and discuss firm’s stakeholder relationships, but do not connect these activities to determination of their material issues.<sup>139</sup> Low disclosure here may reflect the fact that firms engage

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stakeholders under the framework and, therefore, identify stakeholders without quite knowing how to engage them.

<sup>135</sup> VOTORANTIM, INTEGRATED REPORT 2011 111-12 (2011).

<sup>136</sup> This lower disclosure level was true for GRI reporters, despite the fact that GRI contains a specific item requiring disclosure of the basis for the firm’s identification of its stakeholders. See GRI PRINCIPLES, *supra* note 38, at 30 (Specific Standard Disclosure G4-25).

<sup>137</sup> ESKOM, INTEGRATED REPORT 2013 20-21 (2013).

<sup>138</sup> See discussion *supra* 27-28 for discussion of Tables 2 and 3.

<sup>139</sup> See, e.g., ITAU INTEGRATED REPORT, *supra* note 107, at 45 (enumerating the steps in the MD Process and connecting the identification step with finding the “most suitable stakeholders to start the process of determining materiality”); UNICREDIT, 2014 INTEGRATED REPORT 27 (2014), (in a section

with stakeholders for a variety of reasons (including as part of their philanthropic efforts, to build social license to operate, etc.), other than as input for their materiality determination process. Firms may lose sight of the connection between SE and their MD Process and omit to translate SE into input for their materiality determination.<sup>140</sup> Some firms may still be unconvinced that stakeholders should influence identification of material issues. Whatever the reason for the omission, the omission itself reflects a missed opportunity for firms to capitalize on the resources they allocate to SE by connecting it to strategic materiality determination.

A final issue in our research relates to the credibility of firm SE. Are the firm's engagement activities meaningful or are they primarily "photo ops" for the company? Use of a third-party SE standard sets objective criteria for effective SE and we investigated reports for evidence of use of such a standard. Our data revealed a significant difference between GRI and <IR> firms on this issue, with 54% of GRI firms disclosing the use of an SE standard and only 12% of <IR> firms doing so (columns 11 and 12). Given the fundamental importance of stakeholders in the GRI framework, we expected to see investment in the legitimacy of the SE process through use of an external standard. At just over half using such a standard, it seems that there is an opportunity for GRI reporters to bolster the credibility of this important aspect of materiality determination by use of the AA1000SES or some other stakeholder engagement standard. As for <IR> reporters, the extremely low levels of SE standards use may derive from the <IR> framework's focus on investors or may reflect the early challenges <IR> reporting firms are having as they attempt to determine the appropriate role of stakeholders in integrated reporting.

### 3. SE Summary

Based on data collected in this study, firms seem somewhat muddled as to the relationship between stakeholders, company SE processes, and reporting. A first step in clearing some of this confusion is for firms to articulate in detail their relationship to the groups they identify as stakeholders; firms need to explain *why* they consider each group a "stakeholder" of the firm. More importantly, firms should focus on leveraging their SE as input for their MD Process, both to build stronger relationships with their stakeholders and as a check on the credibility of their MD Process. Last, firms can infuse integrity into their SE through use of an external engagement standard.

The issue of governance of and accountability for both the MD Process and reporting generally was the third major issue area surfaced by our data analysis, discussed in the following section.

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entitled "Stakeholder Engagement," the report explains that the materiality analysis allows the firm to "monitor the priority assigned by our stakeholders to different issues").

<sup>140</sup> This oversight may be true as the firm engages with stakeholders or may be related solely reporting, i.e., disclosure of what the firm is doing. One report in this study, for example, contained a statement drawing the connection between stakeholder concerns and their influence on the firm's materiality determination, but did not disclose any of the underlying information on stakeholders, such as who they were, how they were identified, or what exactly constituted the firm's SE process. The firm must have identified and engaged with stakeholders to generate input for their MD process (unless they disclosed untruthfully about it), but simply did not report information on these items.

*D. Issue #3: Hidden Internal Governance/Accountability*

Both GRI and <IR> are voluntary frameworks, with no official oversight over reports prepared using the frameworks.<sup>141</sup> This stands in marked contrast to most financial reporting regimes, where a government regulator has specific authority to monitor adherence to required disclosure frameworks.<sup>142</sup> Neither GRI nor the IIRC police the use of their respective frameworks; since both frameworks are freely available, firms can use some, all, or none of either or both frameworks in preparing their sustainability reports.<sup>143</sup> Lack of institutional oversight of framework implementation leaves report users with the responsibility of policing the integrity of the reporting system for themselves. Where report users cannot double-check the actual information disclosed, they must know as much as possible about the firm's reporting governance – its internal processes for making materiality determinations and for report preparation - to judge the value of the information disclosed in the report, the end-product of the firms' internal processes.

Both the IIRC and GRI recognize the essential vulnerability of report users and the need for disclosure on reporting firms' internal governance mechanisms. Each framework contains governance disclosures specifically related to the MD Process and report preparation. GRI Standard Disclosure G4-48 requires that firms disclose the “highest committee or position that formally reviews and approves the organization's sustainability report and ensures that all material [topics] are covered.”<sup>144</sup> This disclosure is intended to show the extent of the highest governance body's involvement in developing and approving the organization's sustainability disclosures.<sup>145</sup> The <IR> Framework is even more detailed in drawing the connection between these disclosures and report integrity. <IR>

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<sup>141</sup> GRI does offer what it calls an “application check” service, which companies can request to confirm that they have submitted responses to the disclosures required for either a “core” or “comprehensive” report. The service does not pass judgment on the quality of the disclosure or of the firm's performance on sustainability issues. GRI, *GRI to Launch New Check Service for G4 Reports* (Nov. 7, 2013), <https://www.globalreporting.org/information/news-and-press-center/Pages/GRI-to-launch-new-check-service-for-G4-reports.aspx>. The IIRC does not offer review services for <IR> reports. See IIRC, <IR> PRACTICE AID CHECKLIST, [http://integratedreporting.org/wp-content/uploads/2013/08/171\\_HKICPA-IR-in-accordance-with-CHECKLIST.pdf](http://integratedreporting.org/wp-content/uploads/2013/08/171_HKICPA-IR-in-accordance-with-CHECKLIST.pdf) (noting that adherence to the <IR> framework is “self-declared”).

<sup>142</sup> In the U.S., this enforcement authority belongs to the SEC. U.S. SECURITIES AND EXCHANGE COMMISSION, <https://www.sec.gov/Article/whatwedo.html>; see also, David Monsma & John Buckley, *Non-financial Corporate Performance: The Material Edges of Social and Environmental Disclosure*, 11 U. BALT. J. ENV'T'L L. 151, 182 (2004).

<sup>143</sup> The only significant check on firm use of the frameworks is GRI's requirements for claiming to have prepared reports “in accordance with” the GRI framework. GRI PRINCIPLES, *supra* note 38, at 11.

<sup>144</sup> GRI PRINCIPLES, *supra* note 38, at 39. Standard Disclosure G4-48 is required disclosure only for those companies preparing a GRI “Comprehensive” report; it is not required for those preparing “Core” reports. *Id.* at 12, Table 3: Required General Standard Disclosures.

<sup>145</sup> *Id.*; GRI IMPLEMENTATION MANUAL, *supra* note 40, at 56.

reports should contain a statement from those charged with governance that acknowledges their responsibility to ensure the integrity of the report, accompanied by a statement as to whether the report is in accordance with the Framework.<sup>146</sup> Further, the Framework places on those charged with governance of the report the responsibility to ensure effective leadership and oversight of the report and those involved in its preparation, including maintaining sufficient documentation to help senior management in its decisions related to report content.<sup>147</sup> <IR> reporting firms should include description of their implementation of the MD Process<sup>148</sup> and identification of personnel involved in application of the MD Process and with oversight responsibilities for the <IR> reporting process.<sup>149</sup>

An additional governance mechanism is the use of a third-party standard (i.e., a framework or standard other than the primary reporting framework) related to materiality.<sup>150</sup> As we saw with stakeholder engagement standards, external standards inject credibility into voluntary disclosure systems by acting as a check on the reporting firm's unbridled discretion. Need for greater credibility in sustainability reporting has led to the creation and use of third party standards related to a variety of sustainability reporting issues.<sup>151</sup> A commonly used standard for materiality determination is AA1000 Accountability Principles Standard (APS). Created by independent non-profit organization AccountAbility, the standard sets forth basic principles of accountability for sustainability-related reporting<sup>152</sup> and contains a specific principle related to materiality.<sup>153</sup> Neither GRI nor <IR> require the use of an external materiality standard. We coded for a third-party standard on materiality, used in addition to the primary reporting framework, as a measure of

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<sup>146</sup> <IR> FRAMEWORK, *supra* note 38, ¶ 1.20, at 9.

<sup>147</sup> *Id.* ¶¶ 3.41-3.42, at 21.

<sup>148</sup> *Id.* ¶¶ 4.41-4.42, at 29. This description should include disclosure of the process used to identify relevant matters and the process used to narrow down relevant matters to material matters. *Id.* The Background Paper sets out key questions that report preparers could consider in assessing the adequacy of their proposed disclosure on these items. These questions include whether description of the MD Process provides enough information on the process used by the firm for report users to determine which matters the firm considers material and how the firm decided to include or exclude matters, and whether there is sufficient information to make an informed assessment as to the robustness of the firm's use of the MD Process. *Id.*

<sup>149</sup> *Id.*

<sup>150</sup> The use of a third-party standard for materiality must be distinguished from third party assurance of the report. While both have implications for the credibility of the report, the two processes function differently. A third party or external materiality standard is a set of criteria related to materiality, developed by an organization other than the reporting company, which the company uses in preparing its report. Assurance of the report is an audit of the finished report by an organization other than the reporting firm. GLOB. REPORTING INITIATIVE, THE EXTERNAL ASSURANCE OF SUSTAINABILITY REPORTING 6 (2013), <https://www.globalreporting.org/resource/library/GRI-Assurance.pdf>. For a more detailed discussion of assurance in sustainability reporting, see Chiu, *supra* note 40, at 387-400. The focus in this study is on the firm's use of an external materiality standard.

<sup>151</sup> Paolo Perego & Ans Kolk, *Multinationals' Accountability on Sustainability: The Evolution of Third-party Assurance of Sustainability Reports*, 110 J. BUS. ETHICS, 173, 175 (2012).

<sup>152</sup> ACCOUNTABILITY, AA1000 ACCOUNTABILITY PRINCIPLES STANDARD 6 (2008) (the standard defines an "accountable" organization as one that assumes "responsibility for...being transparent about the impacts of [its] policies, decisions, actions, products and associated performance.").

<sup>153</sup> *Id.* at 12-13.

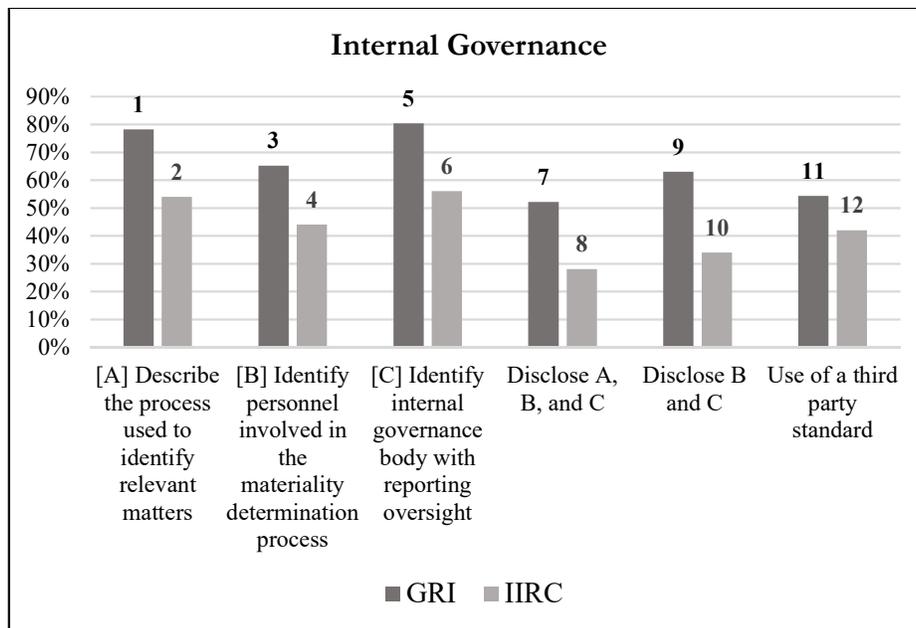
firms' willingness to incorporate external guidance in implementing the MD Process.

### 1. Coding Items

Disclosure on firm materiality and reporting governance can encompass two internal elements – discussion of the MD Process itself and discussion of those involved in and accountable for the MD Process and the report and one external element. Coders looked for the following disclosures related to governance of these areas:

- Description of the application of the MD Process;
- Disclosure of the internal personnel/body with MD Process oversight;
- Disclosure of the internal personnel/body with reporting oversight; and
- Disclosure of whether application of the MD Process included a third-party standard.

### 2. Data Analysis and Discussion



**Table 5:** Internal Governance of MD Process and Reporting

Analysis of the data on internal governance uncovered some of the most significant disclosure challenges for reporting firms. These issues are particularly important to address as they have implications for the basic integrity of the reporting system itself, as well as that of individual reporting firms.

In general, these items showed some of the greatest disparities between GRI and <IR> reporters. This was especially true of disclosure on their MD Process and internal report oversight. For example, GRI disclosure on the first step of the MD Process was 78%, with <IR> disclosure at 54%, a 24-point difference (Table 5, columns 1 and 2). To the extent that this signals <IR> firms' lack of clear lines of accountability for their internal process, it is problematic. It has implications for the reliability of the firm's MD Process itself and calls into question whether the issue of identifying material issues receives attention at appropriate management levels. Both GRI and <IR> see materiality determination as related to corporate strategy.<sup>154</sup> Thus, report users need to know that the MD Process has an effective connection to the top level of firm management. This concern raised a second potential red flag on this issue, with regard to disclosing firms. What internal bodies have oversight over this important process? Was oversight in the hands of the most appropriate internal body for the task? Focused investigation of the disclosing firm reports revealed two primary oversight patterns. Some reporting firms had internal functions dedicated to sustainability (e.g., a sustainability committee or council) and some of these sustainability units reported to executive committees or the board of directors. Ordinarily, firms with a dedicated sustainability unit delegated oversight of the MD Process to that unit. BT Group represented best practice here with its detailed description of its governance mechanisms, including discussion of the "Committee for Sustainable and Responsible Business" and the Committee's responsibility to the Board of Directors for strategy and reporting issues.<sup>155</sup> A second pattern among disclosing firms was to delegate oversight of the MD Process to the firm's audit committee. While this practice has merit as connecting the MD Process to the Board of Directors, it calls into question whether an audit committee possesses the expertise to provide effective oversight of an MD Process. Firms that followed this pattern offered no discussion as to why the audit committee was the appropriate oversight body.

While disclosure levels on individual items in this category seem acceptable (especially for GRI reporters), analysis revealed the same pattern here as seen in Issues #1 and #2: high levels of disclosure on individual items, but decreasing rates of disclosure on *all* items. Table 5, columns 9 and 10 reflect this decrease, showing firms that disclosed oversight of both their MD Process *and* their reporting process, with disclosure rates lower than for the individual component items. Disclosure decreases even more if we look at firms that disclose all of the first three coded items on this issue (disclosure of MD Process, disclosure of oversight of MD Process, and disclosure of oversight of reporting). Reporting rates nosedive to 52% for GRI firms and 28% for <IR> firms (Table 5, columns 7 and 8). As with the issues discussed above, *complete* disclosure of all items required by

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<sup>154</sup> See <IR> FRAMEWORK, *supra* note 38, ¶ 3.3, at 17 (<IR> Guiding Principle 3A is titled "Strategic focus and future orientation" and states that an integrated report should "provide insight into the organization's strategy, and how it relates to the organization's ability to create value....").

<sup>155</sup> BT GROUP, DELIVERING OUR PURPOSE – UPDATE ON OUR PROGRESS IN 2015/16 12 (2016). This is a board-level committee, chaired by the Board chairperson. *Id.*; see, e.g., ATLANTIA, INTEGRATED REPORT 2013 163 (2013) (describing the "Process for the drafting of the report"); NOKIA, PEOPLE & PLANET REPORT 2013 29-31 (2013), ("Managing Sustainability").

the reporting framework remains a challenge for both GRI and <IR> reporting firms. This spotty disclosure chips away at the credibility of the reporting system and undermines the usefulness of the information for report users.

The credibility issue compounds if we look at data on the use of third-party standards related to firm MD Process. Table 5, columns 11 and 12, reveals the relatively low levels overall of disclosure on third-party standard use (54% for GRI reporters, 42% for <IR> firms). This is an area that showed a distinct difference between GRI and <IR> reporting firms as to which standards they used, a difference that may reflect the relative maturity of the GRI framework compared to <IR> reporting.

GRI reporters were overall more likely than <IR> firms to employ standards in addition to the GRI framework, and some firms used multiple additional standards. Only six GRI reporting firms employed the AA1000APS standard, a standard specifically related to the MD Process. The most commonly cited third-party standards were the CDP,<sup>156</sup> the United Nations Global Compact UNGC,<sup>157</sup> and the OECD Guidelines for Multinational Enterprises.<sup>158</sup> Use of these standards raised the issue of whether they are appropriate standards for the purpose. Neither the CDP, the UNGC, nor the OECD Guidelines were designed to aid with materiality determination. Each was created to serve their own individual purposes and can be applied without any linkage to a firm's material issues. For example, a firm could measure and report carbon issues via the CDP framework without ever taking the step of identifying whether carbon issues were "material" for the firm. The purpose of the CDP framework is simply disclosure, not materiality determination. Companies that used these third-party standards did not ordinarily discuss the

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<sup>156</sup> The CDP, formerly known as the Carbon Disclosure Project, is a non-profit organization that has developed carbon and water reporting tools and frameworks. CDP issues invitations to firms to report on a variety of issues related to carbon and water via the CDP's own disclosure questionnaire. Firms may also voluntarily report to CDP or utilize the disclosure framework (which is available on the CDP website) for internal disclosure purposes. CARBON DISCLOSURE PROJECT, GUIDANCE FOR COMPANIES, <https://www.cdp.net/en/guidance/guidance-for-companies..> The CDP Climate Change Information Request is available at [https://b8f65cb373b1b7b15feb-c70d8ead6ced550b4d987d7c03fcdd1d.ssl.cf3.rackcdn.com/cms/guidance\\_docs/pdfs/000/000/227/original/CDP-Climate-Change-Information-Request.pdf?1478623269](https://b8f65cb373b1b7b15feb-c70d8ead6ced550b4d987d7c03fcdd1d.ssl.cf3.rackcdn.com/cms/guidance_docs/pdfs/000/000/227/original/CDP-Climate-Change-Information-Request.pdf?1478623269).

<sup>157</sup> The United Nations Global Compact (UNGC) is an initiative begun in 1999 by then-Secretary General Kofi Annan as a mechanism to foster ethical conduct by business globally and to improve business' reputation. The UNGC's core is a set of 10 Principles related to environmental, labor, human rights, and corruption issues. Signatory companies pledge to act in accordance with the Principles and to report annually on their efforts to do so. *Business Participation*, UNITED NATIONS GLOBAL COMPACT, [http://www.unglobalcompact.org/HowToParticipate/Business\\_Participation/index.html](http://www.unglobalcompact.org/HowToParticipate/Business_Participation/index.html); *Global Compact Policy on Communicating Progress*, UNITED NATIONS GLOBAL COMPACT, [http://www.unglobalcompact.org/COP/communicating\\_progress/cop\\_policy.html](http://www.unglobalcompact.org/COP/communicating_progress/cop_policy.html) (last visited Mar. 20, 2013).

<sup>158</sup> The OECD Guidelines for Multinational Enterprises are recommendations addressed to multinational enterprises operating internationally. They provide non-binding principles and standards for responsible business conduct in a global context consistent with applicable laws and internationally recognized standards. ORGANISATION FOR ECONOMIC COOPERATION AND DEVELOPMENT (OECD), GUIDELINES FOR MULTINATIONAL ENTERPRISES (2011), <http://mneguidelines.oecd.org/guidelines/>.

standard as related to the firm's MD Process.<sup>159</sup> The extent to which firms leveraged these standards as part of their MD Process remains a mystery.

Use of third-party standards by <IR> firms was extremely low, with fewer than half of firms (42%) disclosing their use. Even this percentage is somewhat misleading, given the actual standards that <IR> reporters disclosed. Review of the reports revealed that <IR> firms noted only two standards outside of the <IR> reporting framework: the AA1000APS standard and the GRI reporting framework. Nine of the 21 firms that disclosed use of an external standard used the AA1000APS standards, while 12 firms used GRI. The use of the GRI reporting framework as part of an integrated report is potentially problematic. Recall that the GRI and <IR> definitions of materiality are different, with the <IR> definition focused on value creation and an investor audience and the GRI definition firmly grounded in stakeholder theory.<sup>160</sup> Among <IR> reporting firms that claimed to also use GRI, there was no discussion as to how they reconciled the apparent differences between the frameworks.<sup>161</sup> Had the firm, for example, determined that some stakeholder group affected value creation and, therefore, warranted inclusion in the MD Process? Had the firm simply not wanted to alienate any stakeholder group and so included them as part of the MD Process, whether they impacted value creation or not? <IR> report users are left to wonder exactly how these <IR> reporters identified their material issues.

Despite firms' use of third-party standards, it is not clear that they understand how to connect external standards to the question of materiality or how to use them for determining material issues. Some of this confusion may be because there are multiple reasons to utilize these standards not primarily related to materiality determination. Firms have an opportunity to bolster the integrity of their reporting by employing standards specifically related to materiality and by explicitly integrating other standards into their MD Process.

### 3. Internal Governance Summary

Analysis of the data on firms' internal governance mechanisms for the MD Process and reporting identified several obvious opportunities to improve the integrity of voluntary reporting and build trust with report users. Many firms' reports simply do not disclose who had internal responsibility for either the MD Process or the preparation of the report, leaving report users with no effective way of assessing the credibility of the report or reported information. Firms that have undisclosed internal accountability mechanisms should disclose them. What seems potentially more common is that firms have not created internal accountability for sustainability-related materiality determination and reporting. Some may be

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<sup>159</sup> Nokia came closest of any company to connecting an external standard to materiality. One of Nokia's strategic objectives is to reduce carbon emissions; to this end, the company reports to the CDP. Its "People & Planet" report for 2013 contains several links between discussion of strategic goals and performance as reported to the CDP. NOKIA, *supra* note 155, at 2, 9.

<sup>160</sup> See *supra* notes 118-24 and accompanying text.

<sup>161</sup> The ACCA Factors Study also noted the phenomenon of <IR> reporters using the GRI framework. See ACCA, *supra* note 88, at 12-13, 45-46. The Factors Study offered no assessment of the potential issues created using both frameworks.

attempting to shoehorn oversight into existing accountability channels, such as delegating oversight for the MD Process to an existing audit committee which many lack the expertise needed to effectively oversee the processes. Others may simply not have recognized the need for such accountability. Internal governance of disclosure of non-financial information is equally important to report users as is internal governance financial disclosure, and knowing what those governance mechanisms are is, perhaps, more important to users of non-financial information. Firms should be proactive in building accountability for the MD Process as part of the MD Process, not as an afterthought.

#### CONCLUSION

Concern over the actual impact of reporting led one writer to pose the question is sustainability reporting a “great waste of time.”<sup>162</sup> *The Guardian* article discussed a report by a sustainability consultancy, which argued that sustainability reporting had “stalled” in its effectiveness.<sup>163</sup> The report assessed the current state of reporting as a situation where sustainability reports did not adequately inform stakeholders, nor adequately inform corporate decision-making.<sup>164</sup> Reports had little impact, producing only limited value for companies or stakeholders, compared to the resources invested in their preparation.<sup>165</sup> The report went on to diagnose the problem as the disconnect between “how much companies report externally and what information is actually useful,”<sup>166</sup> i.e., a failure to focus on materiality, for reporting and strategic decision-making.

The sustainability reports analyzed for this study bear out these conclusions. We uncovered key implementation issues—issues that cut across reporting frameworks—that undercut the potential for sustainability reporting to satisfy the information needs of internal and external stakeholders alike. Despite the reporting frameworks’ incorporation of stakeholder analysis, many companies display no more than a rudimentary understanding of stakeholder engagement. Many reports failed to articulate the basis of the firm’s relationship with the stakeholders it identified. More importantly, many reports failed to connect the firm’s SE processes with the selection of material issues.

The failure to connect SE to materiality determination points to the primary pattern we discovered: most firms simply failed to apply the MD Process of their reporting framework fully and completely. A 2013 report by Deloitte called materiality determination one of the most “difficult, underdeveloped, and least systematized aspects of reporting.”<sup>167</sup> The reports we studied support this assessment, with a mere 26% of study reports disclosing application of the entire MD Process. This spotty application of the MD Process makes it impossible to

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<sup>162</sup> Jeff Leinawever, *Is Corporate Sustainability Reporting a Great Waste of Time?*, GUARDIAN (Jan. 6, 2015), <https://www.theguardian.com/sustainable-business/2015/jan/06/corporate-sustainability-reporting-waste-time>.

<sup>163</sup> SUSTAINABILITY, *supra* note 5, at 9.

<sup>164</sup> *Id.* at 7, 15.

<sup>165</sup> *Id.* at 9.

<sup>166</sup> *Id.* at 15.

<sup>167</sup> DELOITTE, *supra* note 87, at 9.

assess the adequacy of those processes themselves. However, it does suggest several steps that reporting companies can take to improve the effectiveness of their reports.

First, firms should recognize that the MD Process will not work if the firms do not work the process. To that end, reporting companies should focus on applying the MD Process with the same rigor they employ in any strategic planning process, with no cutting corners. To accomplish this, firms may need to redirect reporting resources to the MD Process itself, and away from high production value of “glossy” reports. Firms with a history of sustainability reporting may also find they need to let go of their existing model of their report, to the extent that it was not created with materiality in mind. The MD Process should guide report structure, not be superimposed on an existing report structure as an afterthought. Our study of internal governance factors highlights the opportunity for firms to better connect materiality determination with strategic business imperatives of the firm. Reporting companies should construct internal MD Process oversight with accountability to those at the highest levels of strategic planning. As part of the overhaul of their materiality determination, many firms would benefit by revisiting their SE practices, with an eye to improved authenticity and better connection to the firm’s material issues.

Second, our study suggests that firms need to acknowledge the importance of transparency with regard to their internal processes. Since sustainability reporting has no official watchdog, report users must judge the value of the information disclosed for themselves. This they can do only with adequate information on the firm’s internal information gathering and reporting processes. Firms have the opportunity to build credibility in the reporting system and trust with report users by disclosing as much as possible about their internal processes for materiality determination and report preparation.

There is no indication that the demand for sustainability reporting will soon abate. Firms continue to devote significant resources to the task. Reporting companies could, of course, continue on the current reporting trajectory, which for most firms, fails at a fundamental level—it fails to communicate adequately on the firm’s most critical issues. The other option is for firms to recommit to the materiality concept. While not a panacea, this renewed commitment to rigorous application of materiality can keep sustainability reporting from devolving into a “great waste of time.”

## APPENDIX

*A. Coding Sheet for GRI Reports*

<b>Baseline items</b>		
Specific report section on materiality		
Specific report section on stakeholder engagement		
Identification of audience for reporting		
Materiality matrix?		
	Matrix X axis	
	Matrix Y axis	
<b>Mid-level Items</b>		
definition of materiality		
definition of materiality other than copied from GRI, IIRC language		
Identification of stakeholder groups		
Description of stakeholder identification process		
Description of stakeholder engagement process		
<b>Application of GRI Materiality Determination Process</b>		
Step 1:	<u>Identification of "relevant" topics</u>	
	report contains list of relevant topics	
	identification of relevant topics reflects GRI definition of 'relevant'	
	<u>Identification of boundaries for topics</u>	
	report identifies where impacts of topics occur (inside organization, outside organization)	
Step 2:	<u>Prioritization</u>	
	report refers to GRI Materiality Principle* below	
	report considers extent to which relevant topics reflect economic, environmental, and/or social impacts	
	report considers extent to which relevant topics substantively influence assessments and decisions of stakeholders	
Step 3:	<u>Validation</u>	
	report assesses material topics against Principle of stakeholder inclusiveness	
Step 4:	<u>Review</u>	
	report discloses organization's process to review report post-publication to inform Identification step for next report	
<b>High level items</b>		
Disclosure of IIRC materiality determination process:		

	description of process used to identify relevant matters
	ID of internal personnel involved in materiality determination process
	ID of internal governance body with reporting oversight
	does materiality determination process include third party standard?
	is stakeholder engagement process based on third party standard?
	is materiality determination process assured by third party?
	is stakeholder engagement process assured by third party?

*B. Coding Sheet for <IR> Reports*

<b>Baseline items</b>				
Specific report section on materiality				
Specific report section on stakeholder engagement				
Identification of audience for reporting				
Materiality matrix?				
	Matrix X axis			
	Matrix Y axis			
<b>Mid-level Items</b>				
definition of materiality				
definition of materiality other than copied from GRI, IIRC language				
Identification of stakeholder groups				
Description of stakeholder identification process				
Description of stakeholder engagement process				
<b>Application of IIRC materiality determination process:</b>				
1)	<u>Identification of relevant matters: discussion includes consideration of -</u>			
		organizational value drivers		
		issues identified in stakeholder analysis/engagement		
		other external and internal factors		
		organization's performance in reporting cycle		
		effect of above factors on business model, strategy, capitals		
2)	<u>Assessment of importance of relevant matters</u>			
		for matters certain to occur:		
		assesses magnitude of effect on organization		
		for matters not certain to occur:		
		assesses magnitude of effect & likelihood of occurrence		
3)	<u>Prioritization of material matters by importance</u>			
<b>High level items</b>				

Disclosure of IIRC materiality determination process:	
	description of process used to identify relevant matters
	description of process used to narrow relevant matters to material matters
	ID of internal personnel involved in materiality determination process
	ID of internal governance body with reporting oversight
does materiality determination process include third party standard?	
is stakeholder engagement process based on third party standard?	
is materiality determination process assured by third party?	
is stakeholder engagement process assured by third party?	





## INTERNATIONAL IP: HARMONIZING THE PROTECTION OF GRAPHICAL USER INTERFACES

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### *Abstract*

*This article sets forth why sui generis legislation geared towards graphical user interfaces (GUIs), based on both U.S. and international law, is best for framing GUI protection in the U.S. and abroad. The first part of this article focuses on the current protection afforded to computer software programs and GUIs in the U.S. and in certain jurisdictions abroad, and the issues that arise with these protections. An analysis of this type is needed to better understand how protection can be improved. The second part of this article then focuses on reasons why GUIs need uniquely adapted protection. This discussion includes a comparison of GUI design to other subject matter designs that have previously been adopted into or modified by existing intellectual property law. The final part of this article shifts to a discussion advocating for the adoption of a sui generis U.S. law that contains certain aspects of current intellectual property law derived from the U.S. and abroad.*

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## INTRODUCTION

Mobile applications are ubiquitous in today's constantly shifting technological climate. Anyone with a phone, tablet, smart watch, or who just happens to not live under a rock, has used or at least been exposed to a mobile app in one form or another. Indeed, the use of apps has so quickly expanded that they now come in all shapes and sizes. Just as Apple announced several years ago, there appears to be "an app for just about anything."<sup>1</sup> The prevalence of apps has led to significant competition in the marketplace, as software companies and developers attempt to gain a foothold and develop the next best innovation. Greater app usage has caused developers and designers to focus on graphical user interfaces.<sup>2</sup> Graphical user interfaces, or GUIs, are "computer environment[s]" that allow a user to interact with the computer through visual elements such as icons, 'pull-down menus, pointers, pointing devices, buttons, scroll bars, windows, transitional animations, and dialog boxes."<sup>3</sup> GUIs are essential to the development and originality of apps. The innovation behind an app's GUI reflects how users respond to that app, and is key in determining whether that app will be successful within app stores and among users.

Apps are just one example of how GUIs are taking on an increasing importance in the world of intellectual property. Indeed, intellectual property protection for GUIs is a fairly new field that requires greater clarity if developers are better able to understand which elements of their software are protected. Legislatures, courts, and intellectual property scholars across numerous jurisdictions continue to deliberate as to how best to protect GUIs. Current law presents a wide-range of variations and inconsistencies as to how GUIs are protected and how these protections are enforced. In the U.S., for example, GUIs may be protectable as computer software.<sup>4</sup> In contrast, EU law affords protection to GUIs through the Information Society Directive, but only when interaction with the GUI occurs by way of public communication.<sup>5</sup> The

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<sup>1</sup> CommercialsKid, *iPhone 3g Commercial "There's An App For That" 2009*, YOUTUBE (Feb. 4, 2009), <https://www.youtube.com/watch?v=szrsfeyLzyg>.

<sup>2</sup> Thomas Dubuisson, *IP Protection for Graphical User Interfaces in the EU, US and China*, 10 J. INTELL. PROP. L. & PRAC. 767 (2015).

<sup>3</sup> Rachel Stigler, *Ooey GUI: The Messy Protection of Graphical User Interfaces*, 12 NW. J. TECH. & INTELL. PROP. 215, 216 (2014) (quoting *Compact American Dictionary of Computer Words: An A to Z Guide to Hardware, Software, and Cyberspace* (ed. by American Heritage Dictionaries, 1998)).

<sup>4</sup> Copyright in U.S. protects GUIs as a whole, but only against exact copies. *See id.* at 229; *see also* Apple Computer, Inc. v. Microsoft Corp., 35 F.3d 1435, 1442 (9th Cir. 1994); *contra* Directive 91/250, of the European Economic Community of 14 May 1991 on the legal protection of computer programs ("[I]deas and principles which underlie any element of a program, including those which underlie its interfaces, are not protected by copyright under this Directive.").

<sup>5</sup> *See* Case C-393/09, *Bezpečnostní softwarová asociace - Svaz softwarové ochrany v Ministerstvo kultury*, 2010 E.C.R. 609CJ0393 (ruling that television broadcasting of a graphic user interface does not

inconsistent protections currently available for GUIs blurs their scope of protection, and hinders developers and companies from being able to adapt to a world in which connecting with consumers is vital.<sup>6</sup> These inconsistencies also have burdensome financial consequences for those unsure of what currently constitutes protectable material, as there is a substantial amount of money at stake in infringement claims involving GUIs.<sup>7</sup> A uniquely adapted law could provide clarity for the protection of GUIs around the world. Enacting such a law will also assist attorneys in applying intellectual property protections to other disruptive technologies that shift the landscape of protection.

### I. U.S. GUI PROTECTIONS AND ISSUES SURROUNDING THEM

Various forms of intellectual property protection are currently available for computer software programs and GUIs. Within the U.S., the three-prominent means to protect computer software and GUIs are copyright, trade dress, and patents. An initial analysis of how computer software is protected under each scheme is crucial to understanding how GUIs themselves may be protected. In addition, examining how GUIs are protected along with the issues that arise under each scheme is helpful in framing a new type of protection that works better for GUIs.

#### A. Copyright

The United States Copyright Office describes a computer program as “a set of statements or instructions to be used directly or indirectly in a computer to bring about a certain result.”<sup>8</sup> Under the U.S. Copyright Act, a computer software program can be protected as a written or audiovisual work.<sup>9</sup> How a developer wants to protect

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constitute communication to the public of a work protected by copyright within the meaning of Article 3(1) of Directive 2001/29).

<sup>6</sup> See Nicole Bashor, *Touching the Future: Patents on Graphical User Interfaces on the Rise*, INSIDE COUNSEL (Mar. 5, 2014), <http://www.insidecounsel.com/2014/03/05/touching-the-future-patents-on-graphical-user-inte> (“Protection of graphical user interfaces is a must for any company that uses an interface to connect with its audience.”).

<sup>7</sup> SEE SAMSUNG ELECS. CO., LTD. V. APPLE, INC., 137 S. CT. 429 (2016); SEE ALSO NICK WINGFIELD, *JURY AWARDS \$1 BILLION TO APPLE IN SAMSUNG PATENT CASE*, N.Y. TIMES (AUG. 24, 2012), [HTTP://WWW.NYTIMES.COM/2012/08/25/TECHNOLOGY/JURY-REACHES-DECISION-IN-APPLE-SAMSUNG-PATENT-TRIAL.HTML](http://www.nytimes.com/2012/08/25/technology/jury-reaches-decision-in-apple-samsung-patent-trial.html)

(DISCUSSING JURY AWARD TO APPLE OF MORE THAN ONE BILLION DOLLARS IN DAMAGES FOR SAMSUNG’S INFRINGEMENT OF APPLE’S GUI DESIGN PATENT). LATE LAST YEAR, THE U.S. SUPREME COURT LIMITED DAMAGES IN THE *APPLE V. SAMSUNG* CASE, RULING THAT DAMAGES NEED NOT BE CALCULATED BASED ON PROFITS FOR AN ENTIRE DEVICE. SEE INA FRIED, *IN ITS NEW APPLE V. SAMSUNG RULING, THE SUPREME COURT HAS CHANGED HOW PATENT DAMAGES ARE CALCULATED*, RECODE (DEC. 6, 2016), [HTTP://WWW.RECODE.NET/2016/12/6/13854490/SAMSUNG-APPLE-IPHONE-DESIGN-PATENTS](http://www.recode.net/2016/12/6/13854490/samsung-apple-iphone-design-patents) (“[T]OSSING OUT NEARLY \$400 MILLION IN DAMAGES [SAMSUNG] WAS ORDERED TO PAY TO APPLE.”).

<sup>8</sup> U.S. COPYRIGHT OFFICE, CIRCULAR 61: COPYRIGHT REGISTRATION OF COMPUTER PROGRAMS I (2017).

<sup>9</sup> See 17 U.S.C.A. § 102 (2016); see also David Ludwig, *Intellectual Property Protection for Software and Apps*, BETALAW (Mar. 5, 2014), <http://www.betalaw.info/ip-protection-software-and-apps/> (“Software is unquestionably protectable under U.S. Copyright Law, but unless the program is primarily a display of graphics or videos, software is usually registered as a written work.”).

their software may depend on what aspect of the software the developer views as most predominate.<sup>10</sup> If the developer values the source code of the program most, he or she may look to protect it as a literary, or written, work.<sup>11</sup> If the developer recognizes the visual display of the program as most valuable, he or she may wish to protect it as an audiovisual work.<sup>12</sup> Developers are often more interested in protecting user interfaces from copyright infringement because of their commercial value, and the high level of skill and insight that goes into creating those interfaces.<sup>13</sup> Regardless of which subject matter the developer chooses, these protections are only extended to the original expressions embodied in the computer program, not the basic ideas behind the program's creation.<sup>14</sup>

While courts have extended protection to both the source code of a computer program and its user interface,<sup>15</sup> protection for the latter has been limited.<sup>16</sup> This is evident in how GUIs are protected under the copyright scheme. GUI copyright protection is divided in a similar way to computer programs, albeit for different reasons. The individual elements of a GUI are protected as pictorial or graphics works, while GUIs as a whole are protectable as audiovisual works.<sup>17</sup> This dichotomy creates problems for GUIs, in that protection has become limited and difficult to determine. As new interfaces are continuously developed, it may be unclear what individual elements are original enough to be protectable. Similarly, since pictorial and graphical works are only protectable if they are separable from their utilitarian elements, it is difficult to establish protection for an individual

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<sup>10</sup> See U.S. COPYRIGHT OFFICE, *supra* note 8, at 3-4 ("Because computer programs are literary works, registration as a "Literary Work" is usually appropriate. However, if pictorial or graphic authorship pre-dominates, registration as a "Work of the Visual Arts" may be made. Similarly, if motion picture authorship or audiovisual material predominates, registration as a "Motion picture/ audiovisual work" may be made.").

<sup>11</sup> See Gregory J. Wrenn, *Federal Intellectual Property Protection for Computer Software Audiovisual Look and Feel: The Lanham, Copyright, and Patent Acts*, 4 BERKELEY TECH. L.J. 279, 292 (1989) ("Literary works include the written programming instructions of software as stored on the computer.").

<sup>12</sup> See *id.* ("Computer software video displays are considered audiovisual works.").

<sup>13</sup> See Julian Velasco, *The Copyrightability of Nonliteral Elements of Computer Programs* 247-48, (Notre Dame Law Sch., Scholarly Works Paper 392, 1994), [http://scholarship.law.nd.edu/cgi/viewcontent.cgi?article=1449&context=law\\_faculty\\_scholarship](http://scholarship.law.nd.edu/cgi/viewcontent.cgi?article=1449&context=law_faculty_scholarship).

<sup>14</sup> See U.S. COPYRIGHT OFFICE, *supra* note 8, at 1 ("Copyright protection for a computer program extends to all of the copyrightable expression embodied in the program. The copyright law does not protect the functional aspects of a computer program, such as the program's algorithms, formatting, functions, logic, or system design.").

<sup>15</sup> See Stigler, *supra* note 3, at 232 ("Protection extended to 'literal' software elements (specifically, a computer program's underlying code) as well as 'non-literal' elements (the underlying code's structures and their relationships).").

<sup>16</sup> See *id.* at 233 ("Yet, these non-literal elements would only be protected as compilations from exact or near exact copies."). Courts have adopted a test that filters out elements of user interfaces deemed non-protectable, thus making protection for these interfaces thinner; see also VELASCO, *supra* note 13 ("This process entails examining the structural components at each level of abstraction to determine whether their particular inclusion at that level was "idea" or was dictated by considerations of efficiency, so as to be necessarily incidental to that idea; required by factors external to the program itself; or taken from the public domain and hence is nonprotectable expression.") (quoting *Comput. Assocs. Int'l, Inc. v. Altai, Inc.*, 982 F.2d 693 (2d Cir. 1992)).

<sup>17</sup> Stigler, *supra* note 3, at 228; Dubuisson, *supra* note 2, at 769.

element of a GUI.<sup>18</sup> Courts must determine whether particular designs of a GUI are separable from their functional aspects.<sup>19</sup> The Supreme court recently clarified the separability test in *Star Athletica, LLC v. Varsity Brands, Inc.*, holding that “a feature of the design of a useful article is eligible for copyright if, when identified and imagined apart from the useful article, it would qualify as a pictorial, graphic, or sculptural work either on its own or when fixed in some other tangible medium.”<sup>20</sup> Despite this clarification, finding separability can still prove to be a daunting task as courts have yet to apply this approach towards GUI designs.<sup>21</sup> What adds to the difficulty in finding separability for GUIs is the fact that users are increasingly interacting with their devices for utilitarian purposes. The growth of mobile apps is a prime example of this. Another problem arises from the fact that preexisting materials, such as color, frames, and menu styles cannot be protected under copyright unless they are protected as a compilation and “selected, coordinated, or arranged in” an original way.<sup>22</sup> This effectively thins out protection for GUIs, as copyright only protects against exact copies of compilations.<sup>23</sup> If competitors are able to copy even just one part of a GUI, they will be successful in undermining a significant amount of work that a developer will have put into creating that interface. This will deter developers from working to build dynamic and engaging GUIs, and will have an indelible effect on the GUI market as more and more developers create user interfaces for smart phones, tablets, and other contemporary electronic devices.

#### B. Trade Dress

The thinness afforded to copyright protection for user interfaces has led some developers to turn to trade dress rights protected under the Lanham Act, the federal statute that governs trademarks.<sup>24</sup> Trade dress provides protection for the total look and feel of the product’s design or packaging. In order for computer software or a GUI to be protected as trade dress, both must either be inherently distinctive or have acquired secondary meaning.<sup>25</sup> A product is inherently distinctive if its intrinsic

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<sup>18</sup> 17 U.S.C. § 102 (2017) (stating that “the design of a useful article [as defined in this section,] shall be considered a pictorial, graphic, or sculptural work only if, and only to the extent that, such design incorporates pictorial, graphic, or sculptural features that can be identified separately from, and are capable of existing independently of, the utilitarian aspects of the article.”).

<sup>19</sup> For definition and further analysis of separability test, *see infra* notes 127-128 and accompanying text.

<sup>20</sup> *Star Athletica, LLC v. Varsity Brands, Inc.*, 137 S. Ct. 1002, 1012 (2017).

<sup>21</sup> *See infra* note 125 and accompanying text; *see also Star Athletica, LLC*, 137 S. Ct. at 1016 (ruling that designs on cheerleader uniforms were separable from their utilitarian functions, and thus copyright protectable).

<sup>22</sup> Stigler, *supra* note 3, at 229 n.76 (quoting 17 U.S.C. § 101).

<sup>23</sup> *Id.* In one of the first cases involving GUIs, the Ninth Circuit applied a virtual identity standard in analyzing whether Microsoft and HP infringed on an Apple personal computer GUI. The Court concluded that in the case of GUIs “only ‘thin’ protection, against virtually identical copying, [was] appropriate.” *See Apple Comput., Inc. v. Microsoft Corp.*, 35 F.3d 1435, 1442 (9th Cir. 1994).

<sup>24</sup> Stigler, *supra* note 3, at 235-36; *see* 15 U.S.C. § 1125 (2017).

<sup>25</sup> *See Two Pesos, Inc. v. Taco Cabana, Inc.*, 505 U.S. 763 (1992) (ruling that to the extent a trade dress is inherently distinctive, it is not required to have secondary meaning to be protected under the Lanham Act).

nature serves to identify the source of the product.<sup>26</sup> A product has secondary meaning if, from a public perspective, its primary purpose “is to identify the source of the product rather than the product itself.”<sup>27</sup> Thus, in order for a user interface to acquire secondary meaning, it must become so well known that a consumer is able to know who was behind its development just by looking at it. In addition to having acquired distinctiveness, a product must be nonfunctional in nature in order to be afforded trade dress protection. A computer program or GUI feature is considered functional if it is essential to the use or purpose of the product or if it affects the cost or quality of the article,<sup>28</sup> and if exclusive use of such a feature puts competitors at a significant non-reputational related disadvantage.<sup>29</sup> In an action for trade dress infringement, the person asserting protection has the burden of proving a feature is not functional. Lastly, for competitors to be liable under trade dress infringement, their use in commerce of the allegedly infringed feature must have been likely to cause confusion as to its source.<sup>30</sup>

Attaining a sense of distinctiveness for a GUI can be difficult, especially for start-up developers that may just be launching a product.<sup>31</sup> New developers will likely find themselves simply crowded out of the GUI market by larger companies like Apple or Samsung, as they will either be unable to create an inherently distinct interface or will not have the time or resources that are needed to establish secondary meaning. The difficulty in establishing secondary meaning also creates issues for developers who have already entered the market. Since acquiring distinctiveness already tilts in favor of larger companies, these companies can end up using features that are similar to those used by smaller developers. The inability of smaller developers to acquire secondary meaning in their features would effectively allow larger companies to step in and utilize otherwise registrable trade dress without fear of infringing.<sup>32</sup> Furthermore, the requisite likelihood of confusion factor for infringement “exists when customers viewing the mark would probably assume that the product or service it represents is associated with the source of a different product

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<sup>26</sup> *Id.* at 768.

<sup>27</sup> See Wrenn, *supra* note 11, at 286 (quoting *Inwood Laboratories v. Ives Laboratories*, 456 U.S. 844, 851 n.11 (1982)).

<sup>28</sup> *Inwood Laboratories v. Ives Laboratories*, 456 U.S. 844, 850 n.10 (1982).

<sup>29</sup> *Qualitex Co. v. Jacobson Prod. Co., Inc.*, 514 U.S. 159, 165 (1995). If functionality is determined based on the essential to use or purpose requirement, then need not look to whether there is a non-reputational related disadvantage. See *Traffix Devices, Inc. v. Mktg. Displays, Inc.*, 532 U.S. 23, 24 (2001).

<sup>30</sup> 15 U.S.C. § 1125(a)(1) (2017); Circuit courts have offered varying standards of infringement. See *Polaroid Corp. v. Polarad Elecs. Corp.*, 287 F.2d 492 (2d Cir. 1961); *contra* *AMF Inc. v. Sleekcraft Boats*, 599 F.2d 341 (9th Cir. 1979), *abrogated by* *Mattel, Inc. v. Walking Mountain Prods.*, 353 F.3d 792 (9th Cir. 2003).

<sup>31</sup> Stigler, *supra* note 3, ¶ 44 at 237 (“This provides little to no protection for a newly launched design, and therefore favors companies with the resources to fund large scale marketing campaigns before a product’s launch.”).

<sup>32</sup> *E.g.*, *Lang v. Ret. Living Pub. Co., Inc.*, 759 F. Supp. 134, 137 (S.D.N.Y. 1991), *aff’d*, 949 F.2d 576 (2d Cir. 1991) (holding that small time publisher using mark “New Choices Press” failed to show likelihood of confusion in another publisher’s use of phrase “NEW CHOICES FOR THE BEST YEARS”, in part because she had not acquired secondary meaning).

or service identified by a similar mark.”<sup>33</sup> This factor raises the threshold for finding infringement, since it’s likely that confusion exists only when the consumer has been exposed to the mark or icon of a product prior to purchasing it.<sup>34</sup>

Perhaps the biggest obstacle to GUI protection under trade dress is the establishment of non-functionality. As stated previously, features may be functional if they are essential to the consumers’ use of an interface. Drawing the line between functionality and non-functionality can prove challenging. Developers need to not only determine which aspects of the GUIs are needed for competitors to use, but they must also determine whether the look and feel of the GUI affects its “ease of use, efficacy, and salability.”<sup>35</sup> This is referred to as the GUIs aesthetic functionality, which is determined when the protection of the GUI significantly undermines competitors ability to compete in the relevant market.<sup>36</sup> GUIs can almost always be viewed as aesthetically functional, as developers implicitly design interfaces for ease of use and so consumers will be attracted to them. The fact that a GUI is desirable does not necessarily render it unprotectable.<sup>37</sup> Aesthetic functionality is limited to features that serve an aesthetic purpose “independent of any source-identifying function.”<sup>38</sup> The challenge for developers is designing a GUI that serves this source-identifying purpose. In a way, what likely makes a GUIs aesthetically functional is also what arguably makes it distinctive enough to be protectable in the first place. This significantly undermines their protection through trade dress. In addition, useful features of an interface may or may not affect the cost of software, and a part of the interface considered as nonfunctional may become functional at a later point.<sup>39</sup> In the end, while trade dress protection for GUIs appears promising, meeting thresholds for product distinctiveness and exposure make attaining protection difficult. Moreover, courts must perform the unenviable task of reconciling the protection of labor and goodwill that developers put into creating trade dress protected GUIs with the protection with the protection of competition in the GUI marketplace.

### C. Patent

The last scheme under which computer software and GUIs can be protected in the U.S. is patent law. The two forms of patents that can be used to protect computer software are utility patents, which protect functional aspects of a program, and design

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<sup>33</sup> *Fuddrucker, Inc. v. Doc's B.R. Others, Inc.*, 826 F.2d 837, 845 (9th Cir. 1987) (quoting *Lindy Pen Co. v. Bic Pen Corp.*, 725 F. 2d 1240, 1243 (9th Cir. 1984) (Lindy Pen 1) (quoting *Alpha Industries*, 616 F.2d at 443), *cert. denied*, 469 U.S. 1188 (1985)).

<sup>34</sup> *Wrenn*, *supra* note 11, at 287 (“It appears that consumers must be exposed to the look and feel of the relevant software products prior to purchase for the requisite likelihood of confusion to exist.”).

<sup>35</sup> *See id.* at 289.

<sup>36</sup> *Christian Louboutin S.A. v. Yves Saint Laurent Am. Holding, Inc.*, 696 F.3d 206, 221 (2d Cir. 2012).

<sup>37</sup> *Au-Tomotive Gold, Inc. v. Volkswagen of Am., Inc.*, 457 F.3d 1062, 1072 (9th Cir. 2006) (ruling that seller of accessories bearing exact replicas of Volkswagen and Audi logos failed to show marks were aesthetic functional merely by claiming consumers were attracted to marks).

<sup>38</sup> *Id.* at 1073.

<sup>39</sup> *See Wrenn*, *supra* note 11, at 289.

patents, which protect the way a program looks.<sup>40</sup> The duration of patent protection lasts for a much shorter amount of time than for other forms of intellectual property,<sup>41</sup> but what it lacks in length it makes up for in scope. “An owner of a patent may prevent others from making, using, selling, or importing the patented invention in the United States”, and an issued utility patent can prevent others from using the inventive aspect of a software program.<sup>42</sup> Section 101 of the Patent Act of 1952 defines patentable subject matter as “any new and useful process, machine, manufacture, or composition of matter, or any new and useful improvement thereof . . . .”<sup>43</sup> The U.S. Supreme Court has consistently held that a patent including a computer program falls within Section 101 patentable subject matter.<sup>44</sup> Parts of the computer program that are patentable include functional aspects such as source code, as well as the audiovisual look and feel of the program.<sup>45</sup> In order to be eligible for a computer software patent, the software program must utilize additional features or steps that go beyond well-known activities to avoid the possibility that the program will monopolize abstract ideas.<sup>46</sup> This requirement ensures the protection of competition in the marketplace. This also narrows the window in which developers may obtain utility patents, making it harder to do so.<sup>47</sup>

Due to the increasing difficulty in obtaining utility patents, developers have turned to design patents to protect the functional design features of software programs and GUIs. Nowhere is this trend more evident than in the protection of user interfaces. Indeed, just as there has been a shift of utility patent protection for software programs, there has also been a shift in design patent protection for GUIs.<sup>48</sup> To be eligible for a design patent, a software program or GUI must first be considered a “design for an article of manufacture.”<sup>49</sup> Courts construe articles of manufacture broadly, and have defined them as anything “made by the hands of man from raw materials, whether literally by hand or by machinery or by art.”<sup>50</sup> Since computer

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<sup>40</sup> *Id.* at 297.

<sup>41</sup> Michael Risch, *Functionality and Graphical User Interface Design Patents*, 17 STAN. TECH. L. REV. 53, 59 (2013) (comparing patent protection, which lasts 14 years, with copyright protection, which lasts up to 95 years).

<sup>42</sup> Steven Weigler & Sarah Wobken, *Considerations for Advising Software Application Clients*, 45 COLO. LAW. 39, 43 (2016).

<sup>43</sup> 35 U.S.C. § 101 (2017).

<sup>44</sup> Wrenn, *supra* note 11, at 299; *see also* *Diamond v. Diehr*, 450 U.S. 175, 191-93 (1981); *see also* *Alice Corp. Pty. Ltd. v. CLS Bank Int'l*, 134 S. Ct. 2347 (2014).

<sup>45</sup> Wrenn, *supra* note 11, at 300, 304 (“Computer software source code and audiovisual displays play active, essential, *de facto* functional roles in the operation of the computer and any process implemented thereby.”; “[C]omputer implemented processes involving audiovisual look and feel are within the statutory scope of patentable subject matter and are not categorically excluded by the judicial doctrines relating to mathematical algorithms, printed matter, or mental steps.”).

<sup>46</sup> Weigler & Wobken, *supra* note 42, at 43; *see also* *Alice Corp. Pty. Ltd.*, 134 S. Ct. at 2358.

<sup>47</sup> Weigler & Wobken, *supra* note 42, at 43 (“[O]btaining a software patent is increasingly difficult. . . [T]he mere recitation of a generic computer cannot transform a patent-ineligible abstract idea into a patent-eligible invention.”).

<sup>48</sup> Stigler, *supra* note 3, at 238-39 (noting that design patent applications for GUIs has been growing at the fastest rate of any other area).

<sup>49</sup> *Id.* at 239 (“[N]early every type of software graphic can obtain a design patent, so long as it is a ‘design for an article of manufacture.’”); *see also* 35 U.S.C. § 171 (2012).

<sup>50</sup> Wrenn, *supra* note 11, at 305.

programs and GUIs are likely to fall within this broad definition,<sup>51</sup> the next step in determining eligibility is whether the design is novel, nonobvious, and ornamental.<sup>52</sup> The novelty requirement provides that a program design must be “new” and “original,” and that the average observer takes the design for a different, not simply modified, already existing design.<sup>53</sup> To meet the nonobvious requirement, a design must have been “un-anticipated” at the time of its creation in light of earlier designs called “prior art.”<sup>54</sup> To be ornamental, a design cannot be purely functional.<sup>55</sup> If there are no other design options that could achieve the same function as the program design in question, then the design is purely functional and is not within the scope of design patent protection.<sup>56</sup> This protection is similar to trade dress, but offers more leeway in that some functional aspects are allowed and protectable. This also makes it easier for software programs to be protected under design patents than under trade dress, which limits protection of programs to their non-functional aspects.<sup>57</sup>

One could argue that GUIs are afforded much broader protection under design patents than any other form of intellectual property. Unlike the infringement standard for copyright, which requires copying of an exact feature, the standard for design patent infringement is much lower. “A design patent is infringed if, in the eye of a normal observer, the two designs are substantially the same, meaning they are similar enough to deceive the observer and induce him into purchasing one item when he thinks it may be the other.”<sup>58</sup> Another strength of design patent protection is that it can be expanded through continuation patents, which allow patent holders to add slight variations or expand the focus of patent protection.<sup>59</sup> Recent cases such as *Apple, Inc. v. Samsung Electronics, Co., Ltd.* have given greater weight to design patent protection, and have allowed patent holders to more effectively pursue infringers.<sup>60</sup> In addition, design patents are well defined in scope, and their infringement standard is lower than that for copyrights.<sup>61</sup>

Despite their benefits, design patents can be difficult to acquire. Meeting the nonobvious and novel requirements can prove challenging, especially in a field in which there are constant updates to software and user interfaces. Developers are almost always building off of previous designs, so creating something that is truly

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<sup>51</sup> *Id.* (“Computer monitors are made this way as well, and consequently their ornamentation (including audiovisual displays appearing on the monitor) is likely to be included within a broad construction of the term “article of manufacture.””).

<sup>52</sup> Stigler, *supra* note 3, at 239; *see also* 35 U.S.C. §§ 102-103, 171 (2013).

<sup>53</sup> Stigler, *supra* note 3, at 240 (quoting *Thabet Mfg. Co. v. Kool Vent Metal Awning Corp.*, 226 F.2d 207, 212 (6th Cir. 1955)).

<sup>54</sup> *Id.* (quoting 35 U.S.C. §§ 102-103, 171 (2013)).

<sup>55</sup> *Id.*

<sup>56</sup> *Id.*

<sup>57</sup> *See id.*; *see also supra* text accompanying notes 16-18.

<sup>58</sup> *Weigler & Wobken, supra* note 42, at 43 (quoting *Gorham Mfg. Co. v. White*, 81 U.S. 511 (1872)).

<sup>59</sup> Stigler, *supra* note 3, at 242.

<sup>60</sup> *Id.* at 242-43; *see also* *Apple Inc. v. Samsung Elecs. Co., Ltd.*, 678 F.3d 1314 (Fed. Cir. 2012).

<sup>61</sup> Stigler, *supra* note 3, at 244.

novel and nonobvious for a GUI has become increasingly difficult.<sup>62</sup> This was the issue in *Apple v. Samsung*, where Samsung's similar, yet not exact, design was determined to infringe on Apple's. Cases such as this can have monopolistic effects; competitors may be chilled from improving on already invented products, resulting in a lack of variety in the marketplace and increased costs to consumers.<sup>63</sup> Another impediment to obtaining a patent is that they are expensive, costing over two thousand dollars per patent in fees, thus disadvantaging individuals and small companies by making it harder for them to purchase patents.<sup>64</sup> This expense may have an effect similar to trade dress, in which large companies are able to crowd out small competitors to gain protection for their designs. Lastly, even though design patents do not last as long as other forms of intellectual property, their expansion by way of continuation patents may stifle innovation by extending protection well beyond the duration of the original patent.

## II. IP PROTECTION OF GUIs ABROAD

Intellectual property protection for GUIs varies significantly with respect to the forms of protection that are available abroad. In order to provide clear and adequate protection, GUIs must be set apart from the source code and functions that lie behind them and become distinguishable as a separate component.<sup>65</sup> Issues in separating GUIs from their functions and code within EU member states can blur the lines of protection for GUIs between the U.S. and EU. These difficulties are, as mentioned before, a result of the numerous platforms in which GUIs are made available, and the technological changes brought on by mobile apps in particular. This section first offers an analysis of how EU law shapes intellectual property protection for GUIs by looking at the three current forms of protection: copyright, trademark, and industrial design rights.<sup>66</sup> This is followed by a discussion on approaches offered by a few different member states. The discussion continues with approaches offered by Canada and Australia. Finally, this section wraps up with an analysis of the effects of Brexit, on both UK and EU GUI protection.

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<sup>62</sup> This may also be why pendency for GUI design patent applications has been slightly longer in the past than for other design patent applications. See Risch, *supra* note 42, at 60 (stating that pendency for GUI design patents was just under 19 months, compared with 13 months for other applications).

<sup>63</sup> Stigler, *supra* note 3, at 245 ("As previously noted, many believe that incremental improvements to existing software designs are better for technological innovation, and that widely different designs actually hinder software's evolution. As such, this may result in radically different but incompatible products, increased cost to consumers, and a lack of quality and variety of products on the market.")

<sup>64</sup> *Id.*; see also U.S. PATENT AND TRADEMARK OFFICE, USPTO FEE SCHEDULE (effective Jan. 14, 2017) (last updated Sept. 1, 2017), <https://www.uspto.gov/learning-and-resources/fees-and-payment/uspto-fee-schedule>.

<sup>65</sup> Morgan M. Broman, *Legal Uncertainty Under EU Acquis for the Author of Graphical User Interface Design: A New Sui Generis Protection Needed?*, 20 (LUNDS UNIVERSITET 2013).

<sup>66</sup> Rainer Filitz et al., *Digital Design Protection in Europe: Laws, Trends, and Emerging Issues* 3 (2017).

## A. European Union

### 1. Copyright

European law draws a distinct line between GUI and computer program intellectual property protection. EU law currently extends copyright protection of computer programs to programs in any form, including preparatory design work leading up to the development of a program.<sup>67</sup> The European Court of Justice interpreted this language in *BSA v. Czech Ministry of Culture*, and decidedly did not consider GUIs as a form of expression of a computer program within the definitions of EU Directive 91/250/EEC.<sup>68</sup> This led to the conclusion that GUIs are not provided copyright protection under that Directive.<sup>69</sup> The ECJ did state that copyright protection might be available for GUIs under the Information Society Directive 2001/29/EC if the GUI is the author's own intellectual creation, if it meets originality requirements, and if it is communicated to the public.<sup>70</sup> However, the court ultimately decided that since users were unable to interact with the GUI, there was no communication of the GUI to the public.<sup>71</sup> In making this decision, the ECJ defined GUIs as "an interaction interface which enables communication between the computer program and the user."<sup>72</sup>

What is important to note is that the court in *BSA v. Czech Ministry of Culture* decided to refer the scope of IP protection for the GUI back to the member state's national court to decide.<sup>73</sup> As a result, copyright protection for GUIs across all member states has become largely based on what platform the GUI is displayed in, and whether there is sufficient evidence of user interactivity with the interface. This effectively leaves copyright protection of GUIs largely dependent on the originality and interactivity requirements for protection within various member states' legislation.<sup>74</sup> What is also important is that the court never set a standard for determining what level of interaction a GUI must meet. Interaction and the lack thereof is a key component of the court's decision, yet it does not offer a guide as to what level of interaction is enough for a GUI to be deemed protectable under the Information Society Directive. This decision presents an open-ended question of protection, which leads to differing forms of copyright protection among GUI

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<sup>67</sup> Council Directive 2009/24/EC §7 of Apr. 23, 2009, The Legal Protection of Computer Programs (amending Directive 91/250) (EU); *see also* Broman, *supra* note 66, at 19 (noting similarity between this Directive's protection and the U.S. Copyright Act's definition of computer programs).

<sup>68</sup> Broman, *supra* note 65, at 42; *see also* Case C-393/09, *Bezpečnostní softwarová asociace - Svaz softwarové ochrany v. Ministerstvo kultury*, 2010 E.C.R. 609CJ0393.

<sup>69</sup> Broman, *supra* note 65, at 42-43.

<sup>70</sup> *Id.* at 43.

<sup>71</sup> *Ministerstvo Kultury*, 2010 E.C.R. 609CJ0393 (finding that no protection is afforded to a graphic user interface shown via television broadcast since it "is not communicated to the public in such a way that individuals can have access to the essential element characterizing the interface, the interaction with the user, there is no communication to the public of the graphic user interface within the meaning of Article 3(1) of Directive 2001/29.").

<sup>72</sup> *Id.*

<sup>73</sup> Broman, *supra* note 65, at 43.

<sup>74</sup> *See* Filitz et. al., *supra* note 66, at 4.

member states and creates a sense of obscurity as to what GUIs may ever attain copyright protection within the EU.

## 2. Trademark

GUIs may obtain trademark protection under EU law if they are able to serve as source-identifiers of their particular products.<sup>75</sup> Thus, easily identifiable GUI elements, such as the Facebook like-button, the Twitter logo, or various source-identifying colors, may be available for protection under EU trademark laws.<sup>76</sup> Unlike in the U.S., where use is the major requisite for protection, EU trademark rights are usually conferred upon registration of the mark.<sup>77</sup> EU trademark laws are implemented through individual member states' laws, so the requirements for obtaining trademark protection through registration are substantially the same across member states and for the EU as a whole.<sup>78</sup> The challenge with trademark protection is that digital designs, such as GUIs, are devoid of any source-indicating function, meaning that protection is narrowed down to designs that are highly recognizable.<sup>79</sup> This challenge mirrors the difficulty in attaining distinctiveness required for trade dress protection under U.S. law. Even with narrow protection in place, enforcement issues may also arise since the nature of GUIs makes it difficult to prove consumer confusion when infringement occurs in the digital world as opposed to the real world.<sup>80</sup> These issues make trademark protection unreliable, especially with the numerous amounts of mobile app users across the world.

## 3. Industrial Design Rights

Under Article 52 of the European Patent Convention (EPO), computer programs and presentations of information are not regarded as patentable inventions.<sup>81</sup> GUIs may be patentable under EU law when displaying business related information, but only if the interface is of a technical nature that may contribute to the inventive step.<sup>82</sup>

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<sup>75</sup> See Directive (EU) 2015/2436, art. 3, of the European Parliament and of the Council of 16 December 2015 to approximate the laws of the Member States relating to trade marks (stating in part that “[a] trade mark may consist of any signs, in particular words, including personal names, or designs, letters, numerals, colours, the shape of goods or of the packaging of goods, or sounds, provided that such signs are capable of:

- (a) distinguishing the goods or services from those of other undertakings; and
- (b) being represented on the register in a manner which enables the competent authorities and the public to determine the clear and precise subject matter of the protection afforded to its proprietor.”).

<sup>76</sup> Filitz et. al., *supra* note 66, at 4

<sup>77</sup> *Id.*

<sup>78</sup> *Id.* at 5.

<sup>79</sup> *Id.*

<sup>80</sup> *See id.*

<sup>81</sup> Falk Metzler, *Patent Protection of Graphical User Interfaces in Europe*, VISAE PATENTES (Jan. 17, 2011), <http://www.visaepatentes.com/2011/01/patent-protection-of-graphical-user.html>.

<sup>82</sup> *Id.*; *See, e.g.*, Case T-0781/10, Samsung Elecs. Co., Ltd. v. Grootsholten, 2013

Bds. of Appeal of the European Patent Office (ruling that a Samsung device with menu icons displayed on a background image was more than a mere presentation of information, since “the underlying

The difficulty in meeting this inventive step requirement for patentability is the reason why developers have turned to industrial design rights as a more effective form of protection. EU Directive 98/71/EC provides for the legal protection of designs.<sup>83</sup> Protection covers not just the overall look of a design, but may also include individual elements thereof.<sup>84</sup> Furthermore, a provision of the Community Design Regulation explicitly allows for the registration of images, such as GUIs, generated on a computer screen and mobile phone.<sup>85</sup> Unlike patent protection, the standard for attaining industrial design protection is low.<sup>86</sup> This has likely led to the expansion of design right protection for GUIs in the EU. Registered community designs (RCDs) in particular are a form of design rights that have become popular for GUI protection in the EU, just as design patents have become popular in the U.S.<sup>87</sup> Unregistered design protection is also available, but does not offer the broad protection that registration provides.<sup>88</sup> RCDs are protected against similar designs even when an infringing design has been developed in good faith.<sup>89</sup> RCDs can easily apply to certain types of GUIs, provided that their designs are new, have individual character, and constitute the design of an industrial item.<sup>90</sup>

Industrial design protection utilizes various elements of intellectual property schemes in both the U.S. and EU. Protecting GUIs as a whole through design rights is reminiscent of U.S. copyright protection for compilations, while design protection for the individual elements of a GUI parallels with current U.S. protection for GUIs under copyright. In addition, just as design features are excluded from protection if they are solely dictated by the product's technical function,<sup>91</sup> marks are excluded from U.S. trade dress protection if they serve a functional purpose independent of any source-identifying function.<sup>92</sup> Also, similar to EU trademark law, design right

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objective of the problem to be solved [was] to increase user awareness of the currently selected menu hierarchy, and thereby to achieve a more effective man-machine interface.”).

<sup>83</sup> Directive 98/71/EC, of the European Parliament and of the Council on the Legal Protection of Designs, art. 1(a), 1998 (defining ‘designs’ as “the appearance of the whole or a part of a product resulting from the features of, in particular, the lines, contours, colours, shape, texture and/or materials of the product itself and/or its ornamentation.”).

<sup>84</sup> *Id.*; Filitz et. al., *supra* note 66, at 6 (discussing how protection of GUI as digital design could include both the overall look of the electronic screen display, as well as the individual elements thereof).

<sup>85</sup> Dubuisson, *supra* note 2, at 770.

<sup>86</sup> See Filitz et. al., *supra* note 66, at 5-6 (“Any digital design that is new, that is, not identical to prior designs disclosed, and that has an individual character such that an informed user would perceive the design as being different from prior designs may receive protection as an industrial design right.”).

<sup>87</sup> *Id.* at 2.

<sup>88</sup> *Id.* at 6 (“While registered design rights and UCDs share the same requirements and scope of protection, registration provides protection for up to 25 years (subject to payment of renewal fees every five years) and confers the proprietor the exclusive right to use the design, that is, there is no need to prove copying in case of infringement. An important feature of RCDs (and indeed registration with most individual member states) is that the substantive requirements for protection – “novelty” and “individual character” – are not examined prior to registration. Rather, registered designs are assumed to be valid unless and until successfully challenged.”).

<sup>89</sup> *Designs in the European Union, Create Your ‘Design Protection Strategy,’* EUR. UNION INTELLECTUAL PROP. OFFICE, <https://euipo.europa.eu/ohimportal/en/designs-in-the-european-union>.

<sup>90</sup> Dubuisson, *supra* note 2, at 770-71.

<sup>91</sup> Directive 98/71/EC, art. 7(1).

<sup>92</sup> See *supra* notes 25-27, 38 and accompanying text.

protection is harmonized across the EU.<sup>93</sup> Industrial design protection also provides protection for a limited duration of up to 25 years, unlike trademark protection, which is in perpetuity, but not unlike copyright and patent protection. These similarities reflect the sui generis nature of protection afforded to developers through design rights. While protection for a GUI for up to 25 years may not be feasible in today's market,<sup>94</sup> other features of industrial design protection and how they are combined under one scheme may be helpful in adopting a more appropriate and consistent fit for GUIs in the U.S. and EU.

### B. EU Member States

Generally, intellectual property laws are harmonious across the EU. However, member states may differ from each other in their approach to GUI protection. The distinction between computer programs and GUIs remains a focal point in most EU member states' laws regarding protection for GUIs and icons. German law dictates that "computer programs as such can only be protected by copyright law."<sup>95</sup> French law also excludes computer programs from products whose appearance may be protected, meaning GUIs, which are considered as the appearance of software, cannot be protected by design law.<sup>96</sup> According to intellectual property law in the Netherlands, which is based on both national and Benelux legislation, computer programs are not considered as products for purposes of design product protection.<sup>97</sup> While computer programs are not protected under Benelux, GUI protection in the Netherlands is mentioned in the Locarno classification used for industrial designs.<sup>98</sup> This theoretically means that GUIs can be incorporated into design protection if they meet EU requirements noted above.<sup>99</sup>

In terms of patent protection, the German Federal Court of Justice (FCJ) seems to go further than the EPO. The FCJ held in a recent case that the exclusion of presentations of information under EU patent law is overcome when the presentation serves the solution of a technical problem with technical means.<sup>100</sup> The FCJ equated technical effects with an improved perception of the information by the user's mind, and in effect redefined technical effects, which are necessary to establish patentable

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<sup>93</sup> *Id.*

<sup>94</sup> Stigler, *supra* note 3, at 245 (noting that "while [the fourteen year protection for design patents] is more reasonable than copyright's seventy or more years of protection, [it] is much longer than is necessary for the rapidly changing software industry.").

<sup>95</sup> WORLD INTELLECTUAL PROPERTY ORGANIZATION STANDING COMMITTEE ON THE LAW OF TRADEMARKS, INDUSTRIAL DESIGNS AND GEOGRAPHICAL INDICATIONS, COMPILATION OF THE REPLIES TO THE QUESTIONNAIRE ON GRAPHICAL USER INTERFACE (GUI), ICON AND TYPEFACE/TYPE FONT DESIGNS 16 (2016) [hereinafter WIPO STANDING COMMITTEE].

<sup>96</sup> See Ghislain de Trémiolles, *Protection of Graphical User Interfaces in France*, IAM (2016), <http://www.iam-media.com/Intelligence/IAM-Yearbook/2017/Country-by-country/Protection-of-graphical-user-interfaces-in-France?vl=1509713336>; see also Loi 511-1 du 24 avril 2008, C.I.P.

<sup>97</sup> WIPO STANDING COMMITTEE, *supra* note 95, at 4, 12.

<sup>98</sup> *Id.*; WORLD INTEL. PROP. ORG., LOCARNO CLASSIFICATION, <http://www.wipo.int/classifications/locarno/en/>. ("Locarno is an international classification used for the purposes of industrial designs.").

<sup>99</sup> Dubuisson, *supra* note 2.

<sup>100</sup> Bastian Best, *German Software Patents on Graphical Use Interfaces?* (Jan 4, 2016), <https://www.linkedin.com/pulse/german-software-patents-graphical-user-interfaces-bastian-best/>.

subject matter.<sup>101</sup> This approach places an emphasis on the aesthetically functional features a GUI possesses, and allows these features to meet the required functionality threshold for patent protection.

For copyright protection, France takes a similar approach to the ECJ and holds that GUIs are not protected as software accessories under French copyright law.<sup>102</sup> French law may protect the visual or aesthetic appearance of a GUI, so long as the GUI lacks functional elements disallowed under copyright law, and is considered independent of software under design law.<sup>103</sup> Copyright protection for GUIs is possible under Dutch law if the work is creative in character, perceived by the senses, and is not largely determined by technical effect.<sup>104</sup> These laws follow general copyright form in differentiating between the expressive and functional aspects of a GUI. One may argue that allowing individuals member states discretion to interpret GUI protection within the scope of national laws may appear to hinder the cohesiveness that is necessary to establishing a clear sense of what protection actually entails. However, one must keep in mind that the protections afforded are virtually the same from country to country. Member states may look to overarching EU law for certain guidance, and then may fill in the gaps necessary to establish clear protection through their own national laws. In the U.S., enacting *sui generis* law specifically tailored for GUI protection would have a similar effect in filling in gaps of protection, and lead to greater harmonization abroad.

### C. Canada and Australia

As with most other countries, GUIs are protectable under copyright, trademark, and registered designs in Canada, with the most favorable protections likely being through copyright and registered designs. Under Canadian law, computer programs that are original and not trivial may be protected under copyright law.<sup>105</sup> Furthermore, the Canadian Industrial Design Act protects GUIs of a computer program fixed within a screen.<sup>106</sup> The Canadian Intellectual Property Office (CIPO) uses the term GUI in its Manual of Patent Office Practice to refer to “the arrangement of visual elements that will be displayed on a screen, and not to include any of the hardware or software components that may be required to generate the graphical user interface or to make it functional.”<sup>107</sup> The CIPO further stipulates that the visual design that constitutes a GUI is not patentable where the design fails to provide a technological solution to a practical problem.<sup>108</sup> This approach seems to mirror German law regarding patent protection, in that the aesthetic aspects of the GUI must

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<sup>101</sup> *See id.*

<sup>102</sup> *See supra* notes 95-96 and accompanying text.

<sup>103</sup> *See id.*

<sup>104</sup> *Id.*

<sup>105</sup> Hetal Kushwaha, *Protecting Software in Canada – Going Beyond IP Protection*, MARKS & CLERK (Oct. 2, 2013), <https://www.marks-clerk.com/Home/Knowledge-News/Articles/Protecting-software-in-Canada-%E2%80%93-going-beyond-paten.aspx#.WCzP--ErKCR>.

<sup>106</sup> *Id.*

<sup>107</sup> *Computer Implemented Inventions*, 16 CANADIAN INTELLECTUAL PROP. OFFICE, 22 (2010), [https://www.ic.gc.ca/eic/site/cipointernet-internetopic.nsf/eng/wr03157.html#n16\\_09\\_01](https://www.ic.gc.ca/eic/site/cipointernet-internetopic.nsf/eng/wr03157.html#n16_09_01).

<sup>108</sup> *Id.* at 23.

serve some technical purpose.<sup>109</sup> Commentators in Canada have offered discussions of alternative methods of GUI protection, such as through the Integrated Circuit Topography Act.<sup>110</sup> This reflects a potential *sui generis* approach towards software and GUI protection in particular.

Similarly, GUIs are protectable in Australia through copyright, trademark, and registered design. In contrast to many countries, the Australian Design Office holds the position that GUIs should not be protectable by registered designs.<sup>111</sup> Despite this, it is possible in the Australian design system to obtain a registered design for a GUI.<sup>112</sup> The issue with protection lies in the validity and enforcement of that registration, where it is unclear whether the registered design only displays the GUI when in an “on” state, or when it is actually displayed on the screen.<sup>113</sup> As a result of this inconsistency, registered design protection for GUIs are still relatively unclear under Australian law.<sup>114</sup> Issues with protection in Australia mirror those in the U.S. Although protection is available under different intellectual property systems, it is difficult to pinpoint for certain GUI features and to fill the gaps in defining protectability.

#### D. Effects of Brexit

The result of the Brexit referendum last summer presents major obstacles to intellectual property protection abroad, and to the consistency of GUI protection in particular. While it is not yet clear what the exact effects of Brexit will entail for GUI protection,<sup>115</sup> it is more than likely that protections will either be modified or simply cease to apply in the UK.<sup>116</sup> Certain protections will likely still apply in the UK

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<sup>109</sup> See *supra* note 92.

<sup>110</sup> Kushwaha, *supra* note 105 (“Intellectual property protection of software in Canada can go beyond patent protection. Software includes various aspects, and thus a solid IP strategy could consider alternative methods of protection.”); Integrated circuit topographies refer to the three-dimensional configurations of electronic circuits embodied in integrated circuit products or layout designs. *A Guide to Integrated Circuit Topographies*, CANADIAN INTELLECTUAL PROP. OFFICE, [https://www.ic.gc.ca/eic/site/cipointernet-internetopic.nsf/eng/h\\_wr02282.html](https://www.ic.gc.ca/eic/site/cipointernet-internetopic.nsf/eng/h_wr02282.html). (last updated Oct. 02, 2015).

<sup>111</sup> Stuart Irvine, *Protecting GUI Designs in Australia: More Questions than Answers*, FREHILLS PATENT ATTORNEYS (Feb. 5, 2016), <http://www.fapatents.com/resource?id=411> (reasoning that a GUI “cannot adequately distinguish a computer screen as it is not always displayed on the screen, and is not a product itself but rather a use of a product.”).

<sup>112</sup> *Id.* (“Despite the view of the Designs Office, the nature of the Australian designs system is such that it is possible to obtain a registered design for a ‘display screen’ or ‘electronic device’ or the like which is represented as displaying GUI features.”).

<sup>113</sup> EDWARD GENOCCHIO, *DESIGN PROTECTION OF GRAPHICAL USER INTERFACES (GUIs) – AN AUSTRALIAN PERSPECTIVE*, SPRUSON & FERGUSON (OCT. 9, 2014), [HTTP://WWW.SPRUSON.COM/DESIGN-PROTECTION-OF-GRAPHICAL-USER-INTERFACES-GUIS-AUSTRALIAN-PERSPECTIVE/](http://www.spruson.com/design-protection-of-graphical-user-interfaces-guis-australian-perspective/).

<sup>114</sup> See Irvine, *supra* note 111 (“The current position in Australia is not clear.”).

<sup>115</sup> Wouter Pors, *Keeping it Together at the Unified Patent Court*, Kluwer Patent Blog (Oct. 11, 2016), <http://kluwerpatentblog.com/2016/10/11/keeping-it-together-at-the-unified-patent-court/> (stating “Prime Minister Theresa May has now said that the UK will trigger the Article 50 procedure by the end of March 2017, but it is not clear what this exactly means. It is assumed however that it at least means that the UK will be an EU Member State until at least spring 2019.”).

<sup>116</sup> See Sally Shorthose, *Brexit: English Intellectual Property Law Implications*, BIRD & BIRD (Jan. 24, 2017), <https://www.twobirds.com/en/news/articles/2016/uk/brexit-english-intellectual-property-law->

through EU Directives if the UK remains in the European Economic Area, but UK courts would not be precluded from entering decisions that differ from ECJ interpretations.<sup>117</sup> Opening the door for UK judges to differ from their ECJ counterparts on certain areas of protection may create uncertainty as to how GUIs may be protectable within the UK. Of course, UK laws providing protection for GUIs will be unaffected if they do not originate from EU legislation.<sup>118</sup> For other rights that have been extended by EU law, “legislation will be required to either incorporate them into UK law or replace them with alternatives.”<sup>119</sup>

### III. WHY SUI GENERIS PROTECTION?

As this article has shown thus far, a patchwork of protections through various intellectual property systems is what is currently available for GUIs under U.S. and comparative law. What is needed instead is a new, unique approach to GUI protection that will provide clarity and ensure GUIs are protected adequately in an ever-changing digital age. Amendments and modifications to U.S. law offers insight into how uniquely adapted protections have successfully been implemented, and help prove why this approach makes sense for GUIs. This section first analyzes the implementation of architectural works protection under U.S. copyright law, including the similarities and differences between protection for types of architecture and for GUIs. The discussion then focuses on specific examples of sui generis law implemented in the U.S. that pertains to certain designs, and how looking at these examples may help to provide a blueprint for potential sui generis protection for GUIs.

#### A. GUI Parallels to Architectural Works

There is no denying the similarities inherent in GUIs and architectural works. Just as software protection has expanded beyond source code to include user interfaces, so too has blueprint protection expanded to include completed buildings. Analyzing how architectural works are protected under copyright is thus an important piece in determining why it is necessary to enact and implement a sui

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implications (“It is likely that community rights, such as registered and unregistered community designs and EU trade marks (previously community trade marks), will no longer have effect in the UK.”); *see also* Trevor Cook & Anthony Trenton, *The Effect of Brexit on UK Intellectual Property Protection and the Unified Patent Court and Practical Steps to Be Taken Now and in the Future*, WILMER HALE 5 (Jul. 15, 2016)

[https://www.wilmerhale.com/uploadedFiles/Shared\\_Content/Editorial/Publications/WH\\_Publications/Client\\_Alert\\_PDFs/2016-07-15-](https://www.wilmerhale.com/uploadedFiles/Shared_Content/Editorial/Publications/WH_Publications/Client_Alert_PDFs/2016-07-15-)

[The%20Effect%20of%20Brexit%20on%20UK%20Intellectual%20Property%20Protection%20and%20the%20Unif.pdf](#) (“The scope of EU trademarks (formerly known as Community trademarks) is limited to EU Member States. Upon the UK exiting the EU, these unitary rights will no longer cover the UK.”).

<sup>117</sup> *See* Cook & Trenton, *supra* note 116, at 5-6 (noting that patents granted by EPO and directives covering copyright and registered design rights will continue to apply if UK stays in EEA, but that ECJ case law would not be binding).

<sup>118</sup> *See id.* at 6 (“The UK unregistered design right will be unaffected, as it did not originate from EU legislation”).

<sup>119</sup> *Id.* at 3.

generis law for GUI protection. Prior to 1990 in the U.S., finished buildings were not protectable as a form of intellectual property outside of the scope of their functionality. This changed with the Architectural Works Copyright Protection Act (AWCPA) of 1990, which expanded U.S. copyright protection to include architectural works.<sup>120</sup> Congress passed the AWCPA after the U.S. acceded to the Berne Convention,<sup>121</sup> and section 101 of the Copyright Act defines architectural works as:

the design of a building as embodied in any tangible medium of expression, including a building, architectural plans, or drawings. The work includes the overall form as well as the arrangement and composition of spaces and elements in the design, but does not include the individual standard features.<sup>122</sup>

Since then, protection of architectural works has included “habitable structures that are intended to be both permanent and stationary, such as house and office buildings, and other permanent and stationary structures designed for human occupancy, including but not limited to churches, museums, gazebos, and garden pavilions.”<sup>123</sup> The evolution of architectural works copyright protection mirrors that of GUI protection, which has grown from protection of source code as a “literary work” to protection of visual displays as audiovisual works.<sup>124</sup>

With the expansions of protection come increased challenges. Like GUIs, determining protection for architectural works rests on whether or not certain design elements of the architecture are functionally required and, if so, whether the functional design elements are separable from their non-functional counterparts. This can be a difficult line to draw, as both subject matters mesh original, non-functional concepts with those that are functional. In addition, compilation protection is available for both GUIs and architectural works, but offers weak protection against only exact copies.<sup>125</sup> Still, it is easy to see the parallels between GUI and architecture when the focus is on the combination of unoriginal elements to make something creative. Looking at protection through this lens, it may be tempting to write off GUI protection as just another compilation, leaving its functional aspects to design patent protection. However, while compilation protection may be adequate enough for architectural works as a whole, merely applying the same protection to GUIs is not enough. This is because protection differences may arise depending on what subject matter works are copyrighted under. Architectural works may be protectable without

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<sup>120</sup> Raphael Winick, *Copyright Protection for Architecture After the Architectural Works Copyright Protection Act of 1990*, 41 DUKE L. J. 1598, 1598 (1992); see 17 U.S.C. § 102(a)(8) (2016). Prior to the addition of architectural works to protectable subject matter in 1990, architectural plans were protected as graphic works, but finished buildings were not. JULIE COHEN ET AL., *COPYRIGHT IN A GLOBAL INFORMATION ECONOMY* 196 (Wolters Kluwer, 4th ed. 2015).

<sup>121</sup> COHEN ET AL., *supra* note 120, at 197. Article 2 of the Berne convention includes architecture within its definition of literary and artistic works. *Id.*

<sup>122</sup> *Id.* (quoting 17 U.S.C. § 101).

<sup>123</sup> *Id.* at 198 (quoting 37 C.F.R. §202.11(b)(2)).

<sup>124</sup> See *supra* note 92.

<sup>125</sup> See Dubuisson, *supra* note 2 at 768; Stigler, *supra* note 3, at 233.

regard to their physical or conceptual separability.<sup>126</sup> GUIs, being protected as pictorial, graphic, or audiovisual works as opposed to architecture, are not afforded protection outside of a separability scope.<sup>127</sup> This not only makes protection for GUIs distinct from architectural works, but also creates a need for a more adequate form of protection that is uniquely adapted to GUI design.

Another interesting aspect within the realm of “architecture” is the distinction between macroarchitecture and microarchitecture. These are two concepts associated with software architecture, and the distinction between them is fairly simple.<sup>128</sup> Macroarchitecture is concerned with how processors and other components are put together, while microarchitecture deals with how processors and other components can be connected to do useful work.<sup>129</sup> What is interesting about these two concepts is thinking about how they may be protected as intellectual property and, similar to architectural works, how this relates to protection for GUIs. Since macroarchitecture focuses on the overall view in how the pieces of are assembled,<sup>130</sup> its protection under copyright would focus on the complete and creative design that these pieces form when compiled together. This means that macroarchitecture may be protectable as a compilation, as long as its nonfunctional elements can be distinguished from its functional elements. Thus, the same problems for determining separability would arise that also arise with GUIs. On the other hand, microarchitecture may be barred from this type of protection through the merger doctrine.<sup>131</sup> Since microarchitecture focuses much more on individual components and involves making design decisions to “achieve component composability and interoperability,”<sup>132</sup> its protection would move more towards design patent or, in Europe, a registered industrial design. Looking at the different angles that macroarchitecture and microarchitecture may be protected under intellectual property schemes provides insight into how GUIs may

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<sup>126</sup> See COHEN ET AL., *supra* note 120, at 205 (questioning whether *Nelson-Salabes*, an architectural works infringement case, would have been decided differently if the court had applied a conceptual separability approach). Separability doctrine is embodied in 1976 Copyright Act, and is utilized by courts to determine protection available for useful articles. See U.S.C. § 101 (2016); Barton Keyes, *Alive and Well: The (Still) Ongoing Debate Surrounding Conceptual Separability in American Copyright Law*, 69 OHIO ST. L.J. 109, 110 (2008) (“A determination of separability, either physical or conceptual, is a prerequisite to copyright protection for the design of a useful article. In its statutory form, the separability inquiry asks whether the aesthetic features of a useful article can be identified separately from, and can exist independently of, the work’s utilitarian functions.”).

<sup>127</sup> *Supra* note 20, at 1014. (The Supreme Court recently abandoned the distinction between physical and separable separability reasoning that “statutory text indicates that separability [itself] is a conceptual undertaking.”).

<sup>128</sup> See *supra* note 92. (discussing copyright software protection). As software architecture concepts, these two areas would likely be protectable as pictorial and graphic works if the focus of protection was on their design, not architectural works.

<sup>129</sup> EDWARD F. GEHRINGER, ARCHITECTURE OF PARALLEL COMPUTERS 1, <https://people.engr.ncsu.edu/efg/506/s02/lectures/notes/lec1.pdf> (last visited Mar. 22, 2017).

<sup>130</sup> JOSEPH E. HOLLINGSWORTH & BRUCE W. WEIDE, MICRO-ARCHITECTURE VS. MACRO-ARCHITECTURE 1 (1994), <http://citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.55.3904&rep=rep1&type=pdf> (last visited Mar. 22, 2017).

<sup>131</sup> COHEN ET AL., *supra* note 120, at 96 (Merger doctrine bars copyright protection when, [w]here only one or a limited number of ways exist to express an idea, the idea and expression merge...”).

<sup>132</sup> HOLLINGSWORTH & WEIDE, *supra* note 130, at 1.

become protectable through the combination of various intellectual property schemes under a sui generis law.

### B. Current U.S. Sui Generis Law

As has been discussed above, traditional forms of protection may be inadequate to protect new and dynamic forms of intellectual property. When there have been perceived gaps in intellectual property protection, Congress has responded by enacting legislation oriented toward protecting specific types of designs that may have been difficult to protect under traditional forms of intellectual property.<sup>133</sup> The Semiconductor Chip Protection Act (SCPA) is one such example of Congress enacting a sui generis law. Semiconductor chip protection presented issues that GUI protection presents today, as there were concerns that traditional forms of protection were not capable of protecting the labor and capital that went into designing them. Industry players and manufacturers pressured Congress into granting additional intellectual property protection.<sup>134</sup> Thus, the SCPA was enacted to protect mask works fixed in semiconductor chips.<sup>135</sup> The focus of protection was put on mask works, as they bear the circuit designs and describe the entire three-dimensional topography of the finished semiconductor product.<sup>136</sup> This was likely to limit the chances of protection being based on the more utilitarian aspects of the product. The SCPA is codified in the same Title of the U.S. Code as the Copyright Act, but is “separate from and independent of the Copyright Act.”<sup>137</sup> This reflects the point that the act was implemented to “fill the gap between patent and copyright protection,” not just to create a new form of copyright protection.<sup>138</sup>

Another sui generis law applied to a specific design is the Vessel Hull Design Protection Act of 1997 (VHDPA). This law was a response to the case *Bonito Boats, Inc., v. Thunder Craft Boats, Inc.*, in which the Supreme Court struck down a Florida

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<sup>133</sup> See COHEN ET AL., *supra* note 120, at 195 (“To date, Congress has shown a greater willingness to enact sui generis protection for specific subcategories of industrial design perceived to merit special attention than to enact general purpose industrial design legislation.”).

<sup>134</sup> Morton David Goldberg, *Semiconductor Chip Protection as a Case Study* 329 THE NAT’L ACADEMIES PRESS, <https://www.nap.edu/read/2054/chapter/27> (last visited Mar. 19, 2017).

<sup>135</sup> U.S. COPYRIGHT OFF., FEDERAL STATUTORY PROTECTION FOR MASK WORKS, CIRCULAR 100 1 (2012), <https://www.copyright.gov/circs/circ100.pdf>. The SCPA defines mask works as “a series of related images, however fixed or encoded (1) that have or represent the predetermined three-dimensional pattern of metallic, insulating, or semiconductor material present or removed from the layers of a semiconductor chip product; and (2) in which series the relation of the images to one another is that each image has the pattern of the surface of one form of the semiconductor chip product,” and semiconductor chip products as “the final or intermediate form of any product (1) intended to perform electronic circuitry functions and (2) having two or more layers of metallic, insulating, or semiconductor material, deposited or otherwise placed on or etched away or otherwise removed from a piece of semiconductor material in accordance with a predetermined pattern. *Id.*; see also 17 U.S.C. § 901 (2016).

<sup>136</sup> Goldberg, *supra* note 134, at 331.

<sup>137</sup> LEMLEY ET AL., INTELLECTUAL PROPERTY IN THE NEW TECHNOLOGICAL AGE: 2016 IV-47 (Clause 8 Publishing 2016) (quoting H.R. Rep. No. 98-781 (1984)).

<sup>138</sup> *Id.*

law protecting boat hull designs.<sup>139</sup> This is another instance in which interested parties, in this case boat hull designers, appealed to Congress to step in and fill a gap in protection.<sup>140</sup> GUI developers may find the implementation of VHDPAs helpful in that it serves as an example of how pressuring Congress to expand design protection may prove successful if there is enough of an interest.

#### IV. A NEW SUI GENERIS GUI LAW

A sui generis law for GUIs makes sense. GUIs are unique to intellectual property law because they represent the issues in finding a dividing line between functional and non-functional design features in an ever-changing digital age. A law that finds a balance between strict protection that would effectively afford monopolies to GUI developers, and liberal protection that would allow GUIs to be copied easily would best serve courts and practitioners. Looking to both comparative law and existing U.S. legislation that expands the scope of intellectual property protection can provide guidance as to how this new approach can be formulated and implemented.

The focus on forming this new law should be on the adoption of harmonious measures. Many countries outside of the U.S. have increasingly come to rely on registered community designs (RCDs) for GUI protection.<sup>141</sup> RCDs exclude protection for designs if they are solely dictated by the product's technical function.<sup>142</sup> Similarly, U.S. separability doctrine affords protection for designs if they can exist independently of their utilitarian functions.<sup>143</sup> Accordingly, a sui generis GUI law should be based around the requirement that GUI designs must be, to some extent, identified distinctly from their functional purposes. The idea that designs must be separate from their functional purposes to gain protection seems obvious, and observers may question the need for a sui generis law if these measures are already in place to some extent under protections in the U.S. and abroad.<sup>144</sup> However, the issue that remains, and the reason why a sui generis law is integral, is defining how to separate designs in GUIs. GUIs are different from any other area of intellectual property subject matter. They are dynamic, constantly updating, and their designs are much harder to separate from their functional aspects, if they can even be separated at all. Therefore, the requirement that designs must be wholly separate from their functional aspects must be modified under the new law.

Similar to microarchitecture, protection for GUIs should be more on focused on the design decisions made to "achieve component composability and interoperability" in the design.<sup>145</sup> GUIs are by their nature inherently functional; the

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<sup>139</sup> *Id.*; see also *Bonito Boats, Inc. v. Thunder Craft Boats, Inc.*, 489 U.S. 141, 168 (1989) (holding that Florida law was preempted by Patent Act since it offered patent-like protection for ideas deemed unprotected under the federal patent system.)

<sup>140</sup> See LEMLEY, *supra* note 137.

<sup>141</sup> See *supra* notes 86, 97, 105, 111, 116 and accompanying text.

<sup>142</sup> See *supra* note 91 and accompanying text.

<sup>143</sup> See *supra* note 19 and accompanying text.

<sup>144</sup> See discussion *supra* at 5, 8, 17 (discussing U.S. trade dress protection, separability doctrine, and EU RCD protection.)

<sup>145</sup> See HOLLINGSWORTH & WEIDE, *supra* note 130.

purpose behind their development is to make the experience with the interface more enjoyable for the user. Thus, defining their protection should rest on combining aspects of U.S. separability doctrine with those of RCDs around the globe. As stated previously, RCDs already afford protections to GUIs that are similar to U.S. copyright protection.<sup>146</sup> This compatibility would make it easier to reconcile the two regimes under a single law. Designs that are based solely on function could be barred from protection. The law could additionally adopt language from the recent Supreme Court decision regarding separability, and provide for protection if designs can in some way be identified and imagined apart from their functional aspects.<sup>147</sup> Functional aspects of designs may thus be afforded protection, but only if the design itself is not solely based on serving a functional purpose. The law could also expand protection in this respect to include audiovisual works, similar to how RCDs may protect these types of works.<sup>148</sup>

In addition, RCDs provide protection to new designs that have an individual character such that an informed user would perceive the design as being different from prior designs.<sup>149</sup> Protection under a *sui generis* law could thus rest in part on whether users of an interface are able to distinguish a design as unique from designs of other developers. Evidence that informed users can distinguish between two GUIs does not have to be a mandatory requirement in the law, but can simply provide a presumption of validity towards protectability of a design. An analysis of this type makes sense, as the development of GUIs is focused more on the experience of individual users. Whether there are substantial similarities in GUI design among various competitors should also matter less with this new protection, especially since GUIs are more likely to serve a functional purpose. Functionality should not serve as an absolute bar to protection, but should rather defeat a presumption of validity that a design is protectable. The law could provide for a spectrum of functionality. At one end of the spectrum would lie purely functional designs. This would occur when there are no other design options that could achieve the same function as the program design in question, thus making the design purely functional and is not within the scope of protection.<sup>150</sup> At the other end of the spectrum could lie partly functional designs, or designs the functionality of which may serve the purpose of enhancing the user's experience with the GUI but does not otherwise preclude competitors from competing in the market. Developers under the law would then be able to show where along the spectrum their GUI design falls, and whether, despite some degree of functionality, the design taken as a whole constitutes creative and uniquely protectable subject matter.

Legislators framing protection under the new law should consider the delicate balancing act that comes into play within all intellectual property schemes. The balancing act for GUI protection consists of protecting the creative expression within

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<sup>146</sup> See *supra* note 92. For example, Industrial designs are already excluded from protection if their design features are based solely on function. See *id.*

<sup>147</sup> See *supra* note 20 and accompanying text.

<sup>148</sup> See *id.* The current Supreme Court doctrine only applies to pictorial, graphic, and sculptural works.

<sup>149</sup> See Filitz et al., *supra* note 66.

<sup>150</sup> See Stigler, *supra* note 3 and accompanying text.

the developers' designs, while also maintaining an open space where competitors may continue to build upon and expand the functionalities that GUIs provide to users. GUIs are different because how users interact with a certain GUI is an integral part of the creative expression envisioned by developers in coming up with its design. The new law should define GUIs similarly to how the ECJ defined them in *BSA v. Czech Ministry of Culture*, which was as "an interaction interface which enables communication between the computer program and the user."<sup>151</sup> Instead of relying on public communication for protection, as the ECJ did, the new law should recognize protection when users are able to identify the source of the particular GUI based on their interaction with it.<sup>152</sup>

Enforcing developers' exclusive rights in their GUIs must also necessarily entail an examination of how those GUIs are used. Instead of enforcing protection based exclusively on a level of similarity between finished designs, enforcement should focus on the level of similarities behind the development of such designs. Extensive analysis should go into whether potentially infringing developers have "pawned off" other designs by basing the development of their infringing design on how other designs have been used. If, for example, strong enough evidence is presented that, in the eye of a normal observer, the purpose behind the development of design A is substantially the same (meaning they are similar enough to deceive the observer and induce him into thinking the infringing design is another) as design B,<sup>153</sup> then design A is infringing and should thus be enjoined from using that particular design. While this type of enforcement is strict and will likely need extensive evidence such as consumer and developer surveys, it may also help to enhance the development of GUIs as a whole. Developers will be less inclined to create interfaces based on past development, and will be more encouraged to innovate and create something truly unique. Moreover, consumers will not be overly confused and overburdened by the vast amount of similar looking GUI designs that serve the same general purpose. The level of innovation that will proceed in enacting this new law will shape the future of GUIs and ultimately serve the purpose of constitutionally protected intellectual property, which is "to promote the progress and science of *useful arts*."<sup>154</sup>

#### CONCLUSION

Technological changes continue to affect the way individuals think about a variety of issues, whether they involve the economy, sociology, or intellectual property. An argument could be made that one of the main purposes of intellectual property is to respond and adapt to these changes. This article has set out to acknowledge this purpose by framing GUI protection in a new light. Current GUI protection is unclear and not uniform among jurisdictions because developers, legislators, and judges are still grasping how to define adequate protection, while also maintaining the delicate balancing act between the exclusive rights of design

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<sup>151</sup> See Kultury, *supra* note 71 and accompanying text.

<sup>152</sup> See *supra* discussion at 6, 15. This could involve an analysis similar to the source-identifying function behind trade dress protection.

<sup>153</sup> See Weigler & Wobken, *supra* note 42 and accompanying text. This is the same standard of infringement for design patents.

<sup>154</sup> U.S. CONST. art. 1, § 8, cl. 8 (emphasis added).

owners and the rights afforded everyone else in the public domain. The issue these groups face is that they are addressing protection for a relatively new and evolving subject matter within a traditional intellectual property scope. The appropriate way to address GUI protection is through a sui generis law that is more adaptable to the evolving technological landscape. Enacting this type of law will serve the traditional purposes of promoting technology and improving general welfare. This law will also harmonize protections among distinct and, from a protection standpoint, disparate jurisdictions. A law that combines elements from various intellectual property schemes will have a better chance of adoption within international treaties, and be more likely to conform with the basic principles underlying all forms of intellectual property protection.