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THE EUROPEAN LAW FROM GRUNDNORM TOWARDS THE CATHEDRAL:*
CONSTITUTIONAL FEATURES OF A COMPLEX LEGAL SYSTEM

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Abstract: *Many hopes of the adherents of constitutional reform in the EU remained in vain after the enactment of the Lisbon Treaty. Meanwhile the creeping constitutionalisation of the EU law leads to the empowerment of the UE quasi constitutional court- the European Court of Justice (the Court of Justice of the European Union after the enactment of the Lisbon Treaty). This kind of constitutionalism is albeit firmly grounded on judicial cross-border cooperation. The main purpose of this paper is to address the question of whether and how the concept of judicial control based on transactional framework developed in law and economics could effectively supplement if not substitute the notion of constitutional democratic legitimacy. In order to demonstrate that it is logically possible and institutionally feasible to build a system based on circularity, self-referentiality and privatization of legal remedies, the paper contains the analysis of the recent development of the EU law which at least partially takes this direction.*

The aim of the paper is to scrutinize the model of judicial activity within a complex legal system from the perspective of the theory of the so-called *transactional framework*¹. The concept has been proposed by R. Coase and later developed by G. Calabresi and D. Melamed in their pioneering works. Concurring, the paper is composed out of the three parts. The first one concerns the concept of a complex legal system which is to be perceived at the background of the analytical theory of a legal system. This part is heavily dependent on the concept of self-referring rules as proposed by H.L.A. Hart and later developed by J. Raz. The second part concentrates on the theory of the *transactional framework*. Thus the potential results of the study should serve as a benchmark for verification of some theoretical hypothesis offered by the economic analysis of legal remedies. The third part explores the problem of the scope of application of transactional framework in the EU law, especially in the form of liability rules conferring to the party a right to claim damages in case of a breach of the EU law.

I. It could seem that there is hardly anything more abstract than the contemplation of the features and composition of the virtual legal systems *qua* legal systems. Such a commitment to the analytical approach could rightly attract a criticism so charmingly expressed by one of the most famous English judges, namely Lord Denning when he confessed:

„Jurisprudence was too abstract a subject for my liking. All about ideologies, legal norms and basic norms, “ought” and “is”, realism and behaviourism, and goodness knows what else”².

The difference between the complex (Hartian) and the simple (Kelsenian) legal system seems however to play an important role in the description and explanation of the operations of some real legal systems. This especially pertains to the character and existence of the EU law.

A simple legal system is a normative system based on a stable hierarchy of rules in a Kelsenian sense³. As N. Duxbury recently pointed out, the Kelsenian concept of a legal system

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¹ Coase, R.H. (1988). The Problem of Social Cost. In: R.H. Coase (Ed.), *The Firm, The Market and the Law* (pp. 95-156). Chicago: The University of Chicago Press; Calabresi, G., & Melamed, A. D. (1972). Property Rules, Liability Rules, and Inalienability: One View of the Cathedral. *Harvard Law Review*, 85, 1089-1128.

² Lord Denning A., (1983), *The Family Story*, London: Butterworths, p. 38.

³ Hart H.L.A., (1983), "Kelsen's Doctrine of the Unity of Law," in his *Essays in Jurisprudence and Philosophy*, Oxford University Press, pp. 309-42.

validated by the basic norm is affected by some contradictions⁴. According to the assumption accepted by H. Kelsen, every legal norm encapsulates the act of will, expressed by some authority empowered by another norm to create the given legal norm⁵. If this is true however, the basic norm cannot be regarded as a valid legal norm, for the basic norm could not be created by any authority in order to preserve its exceptional status of the pre-supposition of any legal system⁶. As a result Kelsen himself has changed his attitude toward the concept of the basic norm when he observed that it is a fiction in a special sense, as a fiction which not only contradicts reality but is additionally self-contradictory, stating, that:

“(...) a basic norm...not only contradicts reality, since no such norm exists as the meaning of an actual act of will, but also contains contradiction within itself, since it represents the authorization of a supreme moral or legal authority, and hence it issues from an authority lying beyond that authority,”⁷.

Those contradictions has already been revealed by the careful analysis of the Kelsenian concept of a legal system provided by J. Raz, who contended that the Kelsenian basic norm is obsolete and asked the question about the potential substitute for it⁸. Certainly the first possible alternative to the basic norm could possibly be the concept of the rule of recognition as proposed by Hart. Unfortunately the rule of recognition falls short in confrontation with close scrutiny of its merits. As M. Kramer observed, the rule of recognition presupposes either infinite regress or circularity⁹. It could well be right that it is not possible for the rule of recognition to provide with a justification of the origin of a legal order. However the alleged circularity of it could be explained and justified by Hart alone, when he has analyzed the concept of the so-called self-referring rules, finally reaching the conclusion that the phenomenon of the self-referentiality could rightly be deployed as a vehicle apt for the validation of a legal system¹⁰.

⁴ Duxbury N., (2008), “Kelsen’s Endgame”, *Cambridge Law Journal*, 67, p. 55-60.

⁵ *Ibidem*, p. 56.

⁶ Alexy R. (2002), *The Argument from Injustice. A Reply to Legal Positivism*, (trans. B.L. &S.L. Paulson), Oxford 2002, p. 111.

⁷ Kelsen H., (1967), *Pure Theory of Law*, 2-nd ed., M. King trans., Berkley, p. 117.

⁸ Raz, J.(1980), *The Concept of a Legal System: An Introduction to the Theory of Legal System*. 2-nd ed., Oxford University Press, pp. 134-138.

⁹ Kramer M. (1988), “The Rule of Misrecognition in the Hart of Jurisprudence”, *Oxford Journal of Legal Studies* 8 pp. 406-411.

¹⁰ Hart, H.L.A. (1964), “Self-Referring Laws”, *Festschrift Tillägnad Karl Olivecrona*, Stockholm: Kungl. Boktryckeriet, P.A. Norstedt & Söner, pp. 307-16; reprinted in his *Essays in Jurisprudence and Philosophy*, Oxford University Press 1983, pp. 170-178.

A complex legal system is a system whose rules are validated by two apparently different rules of recognition, which means that the practice of judges and officials in a subsystem X is notoriously different from that of subsystem Y. The relationships between the rules of X and the rules of Y may take two forms. Firstly, X and Y could operate as complimentary. This would happen if rules X complemented rules Y. Secondly, X and Y may be regarded as substitutes and thus competing one with others¹¹. Moreover, such a system could also comply with a description of a legal system provided by J. Raz, who analyses the following structure of the self validating system¹². The system possesses the following characteristic: $A \rightarrow B \rightarrow C \rightarrow D \rightarrow A$, which means that the rule A validates the rule B and so on. Such a relationship could rightly be characterized as self-referentiality. The hierarchy of rules is illusive or at least provisional (defeasible). The system is based on the set of self referring rules, as it has rightly been observed by H.L.A Hart¹³. The question arises about the character of the link between D and A. How is it possible for the hierarchically inferior rule D to validate a supposedly superior rule A? The solution given to the problem may be supported by the observation that the rule D could be a specific and concrete rule, such as encapsulated within a verdict of any court¹⁴. The set of such rules create a proper ground for the reconstruction of the existing rule of recognition, underpinning the existence of the legal system¹⁵. If this is so, the rule of recognition is at the same time a sum of practices of the judges and officials and the ultimate source of criteria of validity of the same legal system¹⁶. In other words, the intrinsic characteristic of the rule of recognition places it between points A and D. As a conventional reason for rule following the rule of recognition reveals itself as the rule A, whereas as a set of single operations of the legal institutions the same rule is consisted of the rules of the type D¹⁷. Within a context of the existing legal systems the simpler case could be imagined, namely the case in which there is only one court issuing verdicts comprising the norms of the type D. It is certainly not impossible to immediately associate such a legal institution with

¹¹ Zasu Y. (2007), "Sanctions by Social Norms and the Law: Substitutes or Complements?", *Journal of Legal Studies* 36, pp. 379-396.

¹² Raz, J. (1980) *The Concept of a Legal System: An Introduction to the Theory of Legal System*. Oxford University Press, second edition, pp. 139-140

¹³ Hart, H.L.A. (1964), "Self-Referring Laws", *Festskrift Tillägnad Karl Olivecrona*, Stockholm: Kungl. Boktryckeriet, P.A. Norstedt & Söner, pp. 307-16; reprinted in his *Essays in Jurisprudence and Philosophy*, Oxford University Press 1983, p. 173.

¹⁴ Hart, H.L.A. (1961), *The Concept of Law*. Oxford University Press, pp. 92-97, 106, 142.

¹⁵ *Ibidem*, p. 149-150.

¹⁶ Dickson, J., (2007), "Is the Rule of Recognition Really a Conventional Rule ?", *Oxford Journal of Legal Studies*, 27, p. 373-381.

¹⁷ Marmor, A. (2001), *Positive Law and Objective Values*, Oxford University Press, pp. 2-33.

the Court of Justice of the European Union (CJEU)¹⁸. Certainly such a legal system could remain a simple one since the practice of the CJEU would constitute single and sufficiently coherent Rule of Recognition. The question however remains how the picture would be changed if there were many courts formally independent from the CJEU and at the same time belonging to different judicial structures. Certainly without any instruments it could be impossible for the CJEU to coordinate the operation of the system and consequently some heterodoxical practices of the other courts would possibly create other rules of recognition. Therefore it is crucial to emphasize that the efficacy of the CJEU's coordinating instruments would directly influence the homogeneity of the given complex system, where the CJEU has to coordinate not only its own operations but also the operations of other legal institutions thus mediating between the rule of recognition ultimately characterizing the EU law (and the other components of the EU law) and the rules of recognition shaping the ultimate criteria of validity of Member States.

The relationship between the concept of the simple legal system founded on the single hierarchy of courts and complex legal system composed on different horizontal levels of judicial institutions and imbued with the operation of different, randomly overlapping rules of recognition has been exposed by the CJEU's decision in *Köbler v. Republic of Austria*, (Case C-224/01, [2003] E.C.R. I-10239). The CJEU has endorsed that a Member State may be liable in damages for a national court's serious misapplication of the EU law. The approach presented in *Köbler* has been repeated and reinforced in case C-173/03 *Traghetti del Mediterraneo SpA v. Italy*, [2006] where the CJEU stated that any limitation of State liability on the part of the court has been found as contrary to Community law if such limitations were to lead to exclusion of liability of the Member State concerned in other cases where a manifest infringement of the applicable law was committed¹⁹. The strategy adopted by the CJEU in *Köbler* and *Traghetti* cases in a form adopted by the CJEU induced serious debate in literature²⁰. Many commentators

¹⁸ Formerly the European Court of Justice (ECJ).

¹⁹ The CJEU held that: "Community law precludes national legislation which excludes State liability, in a general manner, for damage caused to individuals by an infringement of Community law attributable to a court adjudicating at last instance by reason of the fact that the infringement in question results from an interpretation of provisions of law or an assessment of facts or evidence carried out by that court. Community law also precludes national legislation which limits such liability solely to cases of intentional fault and serious misconduct on the part of the court, if such a limitation were to lead to exclusion of the liability of the Member State concerned in other cases where a manifest infringement of the applicable law was committed, as set out in (...) the judgment in Case C-224/01 *Köbler* [2003] EUR I-10239."

²⁰ Albors-Llorens, A. (2007). The Principle of State Liability in EU Law and the Supreme Courts of the Member States. *The Cambridge Law Journal*, 66, pp. 270-273; Bertolino, G. (2008). "The Traghetti Case: a New CJEU

emphasize the threat of uncertainty and instability of legal position. Some of them express many doubts concerning potential distortions resulting from those rulings and the application of doctrine of state liability to judicial errors²¹. It is commonly agreed that the EU legal system after *Köbler* might be characterized as being transformed from hierarchical structure into three levels or layers of judiciary composed out of: constitutional courts - first level, highest courts (courts of last instance, ending the procedure, so the structure is fluid, because they vary from case to case) - second level, lower courts - third level²². The fact that the national legal procedure enables parties to ask a first instance court to sit in judgment on a verdict of the court of last instance could weaken and in the long run even thoroughly destroy the traditional linear hierarchy of courts.

Accordingly if traditional, hierarchical structure of national courts within Member States is being weakened by the judicature of the CJEU the question arises about the meaning of such a process and its impact upon the relevant rule of recognition reflecting the actual behaviour of judges in national courts. Imposition of State liability for judicial acts would be likely to lead to the CJEU being called upon to decide whether a national supreme court had acted manifestly wrongly. The lower level national courts may be unwilling to find that superior national courts have acted manifestly wrongly. They might therefore look to the CJEU to make the final judgment. This may lead to the conclusion that the idea of the objectivity of law in Community law cases, whilst not only intellectually attractive, but undoubtedly derived from the concept of the Rule of Law, raises serious practical doubts.

Decision on State Liability for Judicial Acts- National Legislation under Examination". *Civil Justice Quarterly*, 27, pp. 448-453; Breuer, M. (2004). State Liability for Judicial Wrongs and Community Law: the Case of Gerhard Köbler v. Austria. *European Law Review*, 29, pp. 243-254; Ruffert, M. (2007). Case C-173/03 Traghetti del Mediterraneo SpA in Liquidation v. Italian Republic, Judgment of The Court (Great Chamber) of 13 June 2006. *Common Market Law Review*, 44, pp. 479-500.

²¹ Somek, A. (2007). Inexplicable Law. Legality's Adventure in Europe, *University of Iowa Legal Studies Research Papers*, 11; available at SSRN: <http://ssrn.com/abstract=887149>. Accessed 20 February 2009.

²² Breuer, M. (2004). State Liability for Judicial Wrongs and Community Law: the Case of Gerhard Köbler v. Austria. *European Law Review*, 29, pp. 252-254, Chalmers, D, Hadjiemmanuil, C., Monti, G., Tomkins, A. (2006). *European Union Law*. Cambridge: Cambridge University Press, pp. 498-502, Golecki M., Wojciechowski B., (2009), „The Application of Law within a Multicentric Legal System. Economic Analysis of Köbler and Traghetti”, [in:] *Multicentrism as an Emerging Paradigm in Legal Theory*, M. Zirk-Sadowski, M. J. Golecki, B. Wojciechowski (eds.), Peter Lang Publishing Group, Frankfurt am Main, 2009, DIA-LOGOS. Schriften zu Philosophie und Sozialwissenschaften- Studies in Philosophy and Social Sciences, vol. XI, p. 171-174; Golecki M. , Wojciechowski B., (2007), „Cyberspace as a Precondition of Application of Law within a Multicentric Legal Area”, *Masaryk University Journal of Law and Technology*, 1, p. 9-17.

II. Within a hierarchical judicial system the coherence of adjudication is preserved by virtue of appeals and by the same token by the control of cases exerted by higher courts such as court of appeal or Supreme Court. Since each judge tends to avoid overruling, the judicial system usually sustains the cohesion and diminishes the number of judicial errors. Nevertheless, the question arises what would happen if the Supreme Court within some jurisdiction had no virtual possibility to review cases from lower instances alternatively what would happen if instead of one court on the top of the centralized hierarchical structure there would be many different courts and each of them would have the power to review the cases and all of them would be allowed to rely on the preliminary reference set out by the specialized court responsible for the efficacy and coherency of the whole adjudicative practice. Such a situation takes place in the EU law.

The relationship between the CJEU and national courts, especially in regard to the courts of last instance cannot be described as a hierarchical structure. The CJEU does not revise or control verdicts of national courts. Concurringly, the European courts do not have power to overrule judgments given by national courts. This situation is somehow puzzling for many commentators for it requires a completely new approach to standardization and unification of judicial activity. In case of a conflict between the approach adopted by the CJEU and a ruling given by a national court of last instance two strategies are *prima facie* possible.

The first strategy may be called a *public strategy* and it finds its normative ground in the art. 258 of the Treaty on the Functioning of the European Union (TFEU).²³ According to this provision, the Commission has the power to initiate the procedure leading to the application of sanctions against the Member State violating the EU law. The application of relevant sanctions has been regulated according to the art. 260 of the Treaty on the Functioning of the European Union (TFEU)" [ex art 228 of the The European Communities Treaty]²⁴.

²³ Art. 258 TFEU (ex art 226 of the EC Treaty): "If the Commission considers that a Member State has failed to fulfil an obligation under the Treaties, it shall deliver a reasoned opinion on the matter after giving the State concerned the opportunity to submit its observations. If the State concerned does not comply with the opinion within the period laid down by the Commission, the latter may bring the matter before the Court of Justice of the European Union."

²⁴ Art. 260 TFEU (ex art 228 of the EC Treaty): "1. If the Court of Justice of the European Union finds that a Member State has failed to fulfil an obligation under the Treaties, the State shall be required to take the necessary measures to comply with the judgment of the Court. 2. If the Commission considers that the Member State concerned has not taken the necessary measures to comply with the judgment of the Court, it may bring the case before the Court after giving that State the opportunity to submit its observations. It shall specify the amount of the lump sum or penalty payment to be paid by the Member State concerned which it considers appropriate in the circumstances."

It was only in 2005 that the European Commission has issued its *Communication of 13 December*, providing with the precise rules on the application of the sanctions mentioned in art 228. The Communication has been set out in order to “enhance legal certainty and the effective application of Community law”²⁵. According to the Communication the Commission could simultaneously deploy two kinds of sanctions, namely “the penalty by day of delay after the delivery of the judgment under art. 228” and “a lump sum (of money) penalizing the continuation of the infringement between the judgment on non-compliance and the judgment delivered under Art. 228.” Both types of sanctions operate in a way very similar to the criminal or administrative penalty. Additionally the Commission has provided with a new methodology of calculating periodic penalty payments and lump sum fines. The daily penalties are to be calculated according the following formula:

$$D_p = (B_{frap} \times C_s \times C_d) \times n,$$

where: D_p denotes daily penalty payment, B_{frap} denotes basic flat-rate amount “penalty payment” which equals EUR 600, C_s denotes coefficient for seriousness ranging from 1 to 20, C_d denotes coefficient for duration ranging from 1 to 3 and n denotes the capacity to pay of the relevant Member State factor, based on the amount of GDP, the number of voting rights in the Council. Those sanctions are to be regarded as a kind of punishment in form of the fine sentenced by the CJEU. Nevertheless it is not clear to what extent the procedure based on art. 258 and 260 could be applied in case of infringement of the EU law by the highest court within the Member State. Only recently has the CJEU admitted that the well established judicial practice being contradictory with the EU law could be treated as breach of the EU law by the given Member State²⁶. The case *Commission v. Italy* [2003] concerned the problem of the

If the Court finds that the Member State concerned has not complied with its judgment it may impose a lump sum or penalty payment on it. This procedure shall be without prejudice to Article 259. 3. When the Commission brings a case before the Court pursuant to Article 258 on the grounds that the Member State concerned has failed to fulfil its obligation to notify measures transposing a directive adopted under a legislative procedure, it may, when it deems appropriate, specify the amount of the lump sum or penalty payment to be paid by the Member State concerned which it considers appropriate in the circumstances. If the Court finds that there is an infringement it may impose a lump sum or penalty payment on the Member State concerned not exceeding the amount specified by the Commission. The payment obligation shall take effect on the date set by the Court in its judgment.”

²⁵ *Commission Communication of 14.12.2005 on Financial Penalties for Member States who fail to comply with Judgments of the European Court of Justice*, MEMO/05/482, p. 4.

²⁶ Case C-129/00 *Commission v. Italy* [2003] EUR I-14637.

notorious practice of the Italian *Corte di Cassazione* which had been alleged to be contradictory with the EU law. The Italian court in many decisions had relied on its interpretation of the EU law in cases of custom duties. Some commentators) observed that the ruling of the CJEU had been based on vague assumptions according to which the main reason for breach of the EU law stems rather from the bad quality of statutory law having been enacted by the Italian parliament than from direct actions of the Italian court²⁷. The CJEU was not apt to admit openly that the interpretative practice of the Italian Supreme Court led directly to infringement of individual's rights protected by the European law. As a conclusion one may state that the application of the procedure based on art 258 of the TFEU Treaty in case of judicial practice of national courts seems to be if not impractical than at least problematic.

The other strategy which may be called a *privatization strategy*. This could be developed on basis of the preliminary reference procedure under art. 267 of the Treaty on the Functioning of the European Union (TFEU)" [ex art 234 of the The European Communities Treaty].²⁸This strategy is based on the assumption that under art. 267 the TFEU imposes a duty on the court of last instance to make references to the CJEU. This means that „a court or tribunal of a Member State against whose decisions there is no judicial remedy under national law” shall bring also questions of mere interpretation of European law before the CJEU. Thus, there are precise obligations for supreme national courts flowing from primary European law as interpreted by the CJEU. This approach is additionally supported by the recognition of the principle of state liability and might be derived from Joined Cases C-6/90 and C-9/90 *Francovich and Bonifaci v Italy*, where the CJEU held that a Member State was liable to make good the loss and damage caused to individuals as a result of breaches of Community law for which it was

²⁷ Chalmers, D., Hadjiemmanuil, C., Monti, G., Tomkins, A. (2006). *European Union Law*. Cambridge: Cambridge University Press, pp. 359-360.

²⁸ Article 267 (ex Article 234 TEC)

The Court of Justice of the European Union shall have jurisdiction to give preliminary rulings concerning:

(a) the interpretation of the Treaties;

(b) the validity and interpretation of acts of the institutions, bodies, offices or agencies of the Union; Where such a question is raised before any court or tribunal of a Member State, that court or tribunal may, if it considers that a decision on the question is necessary to enable it to give judgment, request the Court to give a ruling thereon. Where any such question is raised in a case pending before a court or tribunal of a Member State against whose decisions there is no judicial remedy under national law, that court or tribunal shall bring the matter before the Court. If such a question is raised in a case pending before a court or tribunal of a Member State with regard to a person in custody, the Court of Justice of the European Union shall act with the minimum of delay.

responsible²⁹. The rulings of the CJEU in *Köbler* and *Traghetti* cases have created the normative framework for the application of the improved *strategy of privatization*, as neatly described by Alexander Somek, who states that:

“(…) there is also a private law response to bad law. It leaves the validity of the act unaffected and imposes instead a liability on the body responsible for its creation. From the perspective of the private law track, the creation of bad law is a tort or, cast in the language of law and economics, its enforcement comes at a certain cost to public authority. It may be sustained, but only at a certain price. The final decision can still be wrong on its merits. The losing party may be harmed by this and deserving of compensation. I should like to refer to the pursuit of this second track as the *strategy of privatisation*.”³⁰

The *privatization strategy* thus relies upon the fact that private individuals may bring suits against their states in case of infringement of the EU law because, according to the assumptions commonly accepted by the adherents of the law and economics movement, adjudication should be treated in an analogous way to production activity³¹. The single effect of this activity is encapsulated within the national court’s decision. The suit should be brought in front of national court which in majority of cases has the obligation to make a preliminary reference. Thus, the activity of national courts throughout the European Union should be standardized, leading to a greater homogeneity of judicial rulings concerning the application of the EU law in different Member States³². But the strategy of privatization does much more than that. As A. Somek once again observes:

²⁹ Golecki M., Wojciechowski B., (2009), „The Application of Law within a Multicentric Legal System. Economic Analysis of *Köbler* and *Traghetti*”, [in:] *Multicentrism as an Emerging Paradigm in Legal Theory*, M. Zirk-Sadowski, M. J. Golecki, B. Wojciechowski (eds.), Peter Lang Publishing Group, Frankfurt am Main, 2009, DIA-LOGOS. Schriften zu Philosophie und Sozialwissenschaften- Studies in Philosophy and Social Sciences, vol. XI, p. 171-174; Golecki M., Wojciechowski B., (2007), „Cyberspace as a Precondition of Application of Law within a Multicentric Legal Area”, *Masaryk University Journal of Law and Technology*, 1, p. 9-17.

³⁰ Somek, A. (2007). *Inexplicable Law. Legality’s Adventure in Europe*, *University of Iowa Legal Studies Research Papers*, 11; available at SSRN: <http://ssrn.com/abstract=887149> p. 12. Accessed 20 February 2009.

³¹ Landes, W.M., & Posner, R.A. (1979). *Adjudication as a Private Good*. *Journal of Legal Studies*, 8, 235-284.

³² Golecki M., Wojciechowski B., (2009), „The Application of Law within a Multicentric Legal System. Economic Analysis of *Köbler* and *Traghetti*”, [in:] *Multicentrism as an Emerging Paradigm in Legal Theory*, M. Zirk-Sadowski, M. J. Golecki, B. Wojciechowski (eds.), Peter Lang Publishing Group, Frankfurt am Main, 2009, DIA-LOGOS. Schriften zu Philosophie und Sozialwissenschaften- Studies in Philosophy and Social Sciences, vol. XI, p. 180-194; Golecki M., Wojciechowski B., (2007), „Cyberspace as a Precondition of Application of Law within a Multicentric Legal Area”, *Masaryk University Journal of Law and Technology*, 1, p. 9-17.

”(…), the *strategy of privatisation* has a different thrust. Its application does not presuppose any inquiry into the concept of law. On the contrary, a legal decision is subjected to the application of another legal norm, that is, some private law rule of liability. No recourse to legal theory is needed here, merely the ordinary principles of tort law, the application of which requires the existence of harm, causality and, where applicable, some standard of fault. The contrast to the public strategy is indeed a stark one.”³³

Thus A. Somek seems to express the view according to which the application of the *privatization strategy* somehow converts the logic of the application of the EU law. The private instruments in form of liability rules will compete with the public instruments such as the sanctions imposed by the CJEU according to art. 238 of the EU Treaty. It at least seems to be suggested by Somek, that the privatization strategy will inevitably lead to some deplorable results, namely it will blur the concept of law and will melt the remnants of traditional approach to the activity of the EU legal institutions. It seems however that the above subtle analysis is at least based on a serious misunderstanding. In fact the application of the privatization strategy will not lead to the deterioration of the Rule of Law in the EU law. The application of this strategy should rather be treated as an evidence of the demise the Kelsenian view of simple legal system, that could be derived from the single *Grundnorm*, so vehemently defended by Somek. Certainly the application of the privatization strategy calls for new descriptive tools and new methodology of legal theory. It is quite obvious that the operation of the complex legal system such as the EU law as applied by courts in Member States can no longer be explained by purely normative analysis of the relationship between different rules within a legal system. Moreover, the need for a new method concerns not only the *privatization strategy* but the *public strategy* as well. This is quite sure as one would take the functional approach of the European Commission into account. The approach which has been presented within *the Communication on Financial Penalties from 14 of December 2005*, where the Commission has presented the methodology thoroughly aligned with the economics of deterrence. Thus the methodological challenge consist not so much in the drawing demarcation line between the privatization and the public strategy, but rather in addressing the question of how to capture and compare both underlying strategies altogether. It

³³ Somek, A. (2007). Inexplicable Law. Legality's Adventure in Europe, *University of Iowa Legal Studies Research Papers*, 11; available at SSRN: <http://ssrn.com/abstract=887149> p. 15. Accessed 20 February 2009.

seems that the economic analysis of remedies could become a potential candidate for such an endeavour. The application of the economic analysis of remedies in order to examine state liability for wrong decisions of domestic courts applying Community law is possible as a result of the acceptance of an additional assumption³⁴. According to R. Coase commodities should be defined as bunches of rights transferred between parties³⁵. These transfers may be either voluntary or involuntary. Voluntary transfers are carried out in the relevant market and under the condition that rights to commodities are well defined and adequately protected. This could be achieved by the application of the property rules which effectively deter the potential trespasser and thus fully protect the entitlements. The scope of the market exchange is however limited by the fact that in many cases transaction costs are prohibitively high. In those cases the exchange could be channeled through the court system, where involuntary exchanges of rights for a given sum of money take the form of compensations awarded by courts. Involuntary transfers play an important role in case of takings and expropriations by Member States as well as in a wider area of tort liability. This model has been extended by Calabresi and Melamed who proposed the concept of *transactional framework*³⁶. This idea dates back to the seminal article of G. Calabresi and A.D. Melamed on *Property Rules, Liability Rules and Inalienability: One View of the Cathedral* where the Authors distinguished three different types of legal rules³⁷. Property rules are protection oriented, for they exclude everybody except the holder from interfering with entitlement. Liability rules are compensation oriented, rewarding the owner with the value of an entitlement, determined by the state. Inalienability rules are intended to deter both potential parties from the transfer of entitlement, regardless of the consent of the holder of entitlement. There is no cost to be determined between parties or damage to be assessed. These three types of rules have evolved creating a characteristic framework for legal institutions across different branches of any legal system³⁸. The detailed shape of this framework is however determined by

³⁴ Golecki M., Wojciechowski B., (2009), „The Application of Law within a Multicentric Legal System. Economic Analysis of Köbler and Traghetti”, [in:] *Multicentrism as an Emerging Paradigm in Legal Theory*, M. Zirk-Sadowski, M. J. Golecki, B. Wojciechowski (eds.), Peter Lang Publishing Group, Frankfurt am Main, 2009, DIA-LOGOS. Schriften zu Philosophie und Sozialwissenschaften- Studies in Philosophy and Social Sciences, vol. XI, p. 178-181.

³⁵ Coase, R.H. (1988). The Problem of Social Cost. In: R.H. Coase (Ed.), *The Firm, The Market and the Law* (pp. 95-156). Chicago: The University of Chicago Press.

³⁶ Calabresi, G., & Melamed, A. D. (1972). Property Rules, Liability Rules, and Inalienability: One View of the Cathedral. *Harvard Law Review*, 85, 1089-1128.

³⁷ *Ibidem*, pp. 1106-1115.

³⁸ *Ibidem*, pp. 1108-1109.

specific national traditions or the peculiarities of civil law and common law systems. It is important that the distinction between different types of legal rules as originally proposed by Calabresi and Melamed rests upon the assumption that property and liability rules are protected by different sanctions³⁹. On the one hand property rules are deterrence oriented. The application of such a rule has to make the infringement of the right protected by a given property rule unprofitable. In a simple formula, costs faced by the potential defendant for the infringement of the protected entitlement should be set at $D > vD$ so that the defendant has no incentive to infringe a given right as the sum he has to pay always exceeds his own valuation of the entitlement. On the other hand liability rules operate by rewarding the owner with some externally determined compensation that is usually set by a court, a legislator, or an administrative agency. In case of the infringement of the EU law the amount of compensation is to be determined by the national court according to the national rules. Under a liability rule, the goal is to compensate the entitlement's holder while allowing a non-consensual taking. The defendant would appropriate the entitlement if its own valuation was higher than the compensation determined by the court, it is if $vD > D$, where vD denotes the defendant's valuation of an entitlement and D denotes amount of damages awarded by the court. Concurringly the goal of liability remedies is quite complex: they compensate the entitled party through the officially determined payment of a compensation usually in form of damages and additionally they somehow allow a non consensual access to the entitlement for the potential defendants who have a valuation of it relatively higher, at least, than the amount of damages. In the context of the EU law if the Member State decides to infringe the individuals' entitlement protected by the EU law, then it has to pay damages. Accordingly damages should equalize individual's (i.e. plaintiffs) valuation according to the equation: $D = Pv$, where D denotes amount of damages awarded by the court and Pv denotes the defendant's valuation of the entitlement.

Given the universal application of the remedies it is striking that among sanctions listed by Calabresi and Melamed the sanction of invalidity or voidness has not been taken into account. It seems that that kind of sanction is all but a provisional one leading to the application of one of virtually two sanctions: compensation or punishment⁴⁰. The alleged deficiency of the Calabresian scheme of remedies does not however play any important role as far as the application of the

³⁹ *Ibidem*, pp. 1123-1125.

⁴⁰ Cooter, R. (1984), „Prices and Sanctions”, 84 *Columbia. Law Rev.*, pp. 1537-1550.

scheme to the EU law is concerned. Since it is impossible for the CJEU or The Court of First Instance to reverse the verdict of the national court, the choice of the remedy concerns the punishment or the compensation exclusively, which means that depending on the strategy deployed in a given case, the wrongful misapplication of the EU law could be sanctioned by property or liability rule.

The first is the case if the procedure of art 258 and 260 TFEU is being implemented by the EU Commission or the Member State. The second holds in case of the individuals claim against the state, according to the rule set out in *Francovich* and precised in *Köbler*. It could accordingly be stated that the *public strategy* based on the art. 250 TFEU implements the property rule, whereas the privatization strategy expressly adopted in *Köbler*, deploys the *liability rule*.

Fig 1 Property rules Liability rules (based on Calabresi & Melamed 1972, p. 1111-1115)

Initial Entitlement	Property Rule	Liability Rule
Individual A	Rule 1	Rule 2
Member State B	Rule 3	Rule 4 (?)

Nevertheless, the possibility of application of liability rules in the EU law goes far beyond that if the recent development of the theory of *transactional framework* is to be taken into account⁴¹. According to the theory of optional law the number of liability rule could be increased. The theory suggests that the liability rule rewarding damages to the potential injured party might be interpreted through the lenses of option theory as a rule granting the injurer the right to acquire an entitlement for a given price equal to the damage assessed by the court. Such a state of affairs resembles a situation in which the injurer (defendant) owns a *call option* over the entitlement. Such an option can be exercised at the price set equal to damage. Concurringly two different liability rules are to be discernible. The rule according to which the holder keeps the entitlement subject to the condition, that the defendant would not exercise the option to acquire the entitlement, and the opposite rule giving the entitlement to the defendant subject to the fact that the plaintiff would not exercise the *call option*. Additionally, property rules may also be incorporated into this optional scheme. One may say that the difference between liability and property rules is quantative instead of qualitative one. In case of property rules the price of the

⁴¹ Ayres, I. (2005), *Optional Law: The Structure of Legal Entitlements*, Chicago, Chicago University Press, pp 16-21.

option is so high that the option is very unlikely to be exercised and this could be regarded as an equivalent of the sanction whose main purpose is deterrence. Under this perspective, property rules could be regarded as a special kind of liability rules with an exuberant price for the option. Additionally the optional theory of remedies has enabled scholars to multiply the framework of remedies. Assuming that liability rule may be stylized as a *call option* (granted to plaintiff or defendant, hence, there are two rules), it is possible to propose an option to sell, namely the *put-option*. The *put option* rule would grant an entitlement to one party and at the same time, it would confer the conditional right to sell the entitlement to the other party, the other party being under obligation to acquire the entitlement at will of the option holder. The extended matrix of the optional law remedies can be illustrated by the following figure:

Fig. 2. Possible combinations of different optional rules (based on I. Ayres 2005, p. 17)

Type of rule	Individuals' options	Member State's options
Rule 1	Asset	0
Rule 2	Asset-Call	Call
Rule 3	0	Asset
Rule 4	Call	Asset-Call
Rule 5	-Put	Asset+Put
Rule 6	Asset+Put	-Put

Thus one can consider the possibility of styling the liability rule set out against the background of the optional theory of law. Referring to the other figure (fig. 1) one should remark that the set of remedies could be much extended as illustrated on the fig. 2. The liability rules of type 1 (pro plaintiff) and 2 (pro defendant) could now be divided in four types; call pro defendant, put pro defendant, call pro plaintiff and put pro plaintiff.

The main normative hypothesis presented by the theory of optional law concerns the choice between property and liability rules. There is no unanimity as far as such a choice between two types of rules is concerned. Additionally, there is no *opinio communis* about the set of factors that should determine the choice of the appropriate type of rule. For G. Calabresi and D. Melamed it seemed to be obvious that property rules were superior in low transaction cost settings while liability rules were more efficient in high transaction cost settings. This initial

position has given way to many contradictory theories and hypothesis. L. Kaplow and S. Shavell, for example, focus on the costs of administering litigation and conclude that liability rules are superior in many circumstances⁴². L. Bebhuk focuses on the incentive to invest *ex-ante* in front of property or liability rules⁴³. He comes to the conclusion that property rules give a stronger *ex ante* incentive to invest and are more efficient in this respect. I. Ayres presents the opposite solution. He claims that liability rules mitigate the risk of strategic behavior and information asymmetry due to their “harnessing effect”⁴⁴. H. Smith occupies a contrary position when he supports the relative efficiency of property rules based on their intelligibility and respect for parties’ “idiosyncratic valuations”⁴⁵.

III. Summarizing one may state that whereas property rules promote voluntary exchanges, liability rules enable involuntary transfers in cases of high transaction costs. Those involuntary transfers play an important role in cases of appropriations and expropriations by Member States as well as in a wider area of tort liability. Empirical surveys show that the average compensation in the EU varies greatly from state to state. If liability rules are superior and privatization strategy expressed in deployment of the liability rules is going to supersede the public strategy based on protection of property rules the couple of questions arise.

Firstly what would be the actual reason for the superiority of the liability rules and what would be the potential result of that? According to the theory of optional law in a form proposed by I. Ayres, the main argument for liability rules and against property rules relays heavily on the concept of harnessing effect and the alleged information asymmetry. The liability regime is virtually more effective because it forces the potential plaintiff to reveal private information about the valuation of the entitlement. The courts may also more accurately divide the costs of application of the EU law, relaying on the doctrine of the manifest infringement. Thus the court in place may still have a choice between the application of the pro liability or pro plaintiff remedies, which would be very difficult in case of property rules and public strategy.

⁴² Kaplow, L., Shavell S. (1996), “Property Rules Versus Liability Rules”, Harvard Law Review 109, p. 713.

⁴³ Bebhuk, L.A. (2001), “Property Rights and Liability Rules: The Ex Ante View of the Cathedral”, *Michigan Law Review*, 100, p. 601.

⁴⁴ Ayres, I. (2005), *Optional Law: The Structure of Legal Entitlements*, Chicago: Chicago University Press, pp. 152-165.

⁴⁵ Smith, H. E. (2002), “Exclusion Versus Governance: Two Strategies for Delineating Property Rights”, *Journal of Legal Studies*, 31, p. 453.

The choice between property and liability rules reveals also some deeper relevant considerations. It is quite obvious that the application of the property rule enhances the protection of the entitlement. The application of the liability rules provides with much a weaker remedy although of a much more flexible and discretionary character. If this is the line of reasoning is a proper one then it seems that the protection of individual's rights bestowed by the EU law is not regarded as a fundamental aim of the CJEU. The much more convincing explanation is that the CJEU tends to strengthen the efficacy of the EU law, applying the concept of the protection of the rights of the individuals as a kind of pretext. If this allegation is correct the future of the EU court system will heavily depend on the level of administrative costs and a coherency of judicial practice in different national courts.

It seems that the application of liability rules could enhance the coherence of the application of the EU law, since the national courts would adjudicate under the shadow of the appropriate liability rule. Nevertheless this result is not obvious and it would be attained only in a case of coherent application of the liability rule as proposed in *Köbler* in different Member States. The result depends heavily on the level of administrative costs, and on accuracy of verdicts of the courts. The accuracy shall predominantly deal with the amount of damages awarded by the national courts thorough the European Union. Empirical surveys show that the average compensation in the EU varies highly from state to state. This issue has been analyzed in two documents prepared by the European Commission: The Green Paper *Damages actions for breach of the EU antitrust rules* COM/2005/0672 and the Commission Staff Working Paper SEU/2005/1732. Both documents emphasize “total underdevelopment” and an “astonishing diversity” in the approaches taken by the Member States as far as the private enforcement through damages claims in Europe is concerned. As a response to those deficiencies the European Commission has adopted White Paper on *Damages Actions for Breach of the EU antitrust rules* COM(2008) 165, having been published on 02.04.2008. The model proposed by the Commission is primarily focused on compensation through single damages for the harm suffered. Additionally the White Paper encapsulates some recommendations concerning collective redress, disclosure of evidence and the effect of final decisions of competition authorities in subsequent damages actions. Those recommendations are intended to balance rights and obligations of the claimant and the defendant. Moreover some safeguards against abuses of litigation are also taken into account. Generally speaking, the Commission proposes to

build stronger procedural framework for litigation and claims for compensation in case of infringement of the EU law. Those means are believed to broaden the access to judicial system. They are however not sufficient as far as the assessment of damages and the principle of equality in different Member States are concerned. The issue is especially relevant under the rule derived from the cases of *Köbler* and *Traghetti* which states that the court in the Member State has the power to assess the amount of compensation in the case of a breach of EU law⁴⁶. Even in the case of the preliminary reference procedure being applied in a given trial the CJEU has no power to decide on the amount of compensation. This means that the harmonization of compensation awarded in the case of judicial error in EU law cannot be attained directly by legal instruments. The harmonization of damages awarded by the courts could however be successful, provided that there is an instrument of the unification of judicial practices in the case of application of EU law. This concerns the level of administrative (or litigation) costs incurred by the court. As Ayres points out: “(...) the costs of determining liability rule damages and securing payment are far from trivial”⁴⁷. Hence, the harmonization of the EU law should minimize the cost of private information about the value of a given entitlement. The problem of the evaluation of entitlement means that the society has to cover the cost of evaluation, being the equivalent of transaction cost in the case of the voluntary transfer of entitlement through the market. As Kaplow and Shavell observe: “the virtue of the liability rules is that they allow the state to harness information that the injurer naturally possesses”⁴⁸.

The problem however arises if the injurer turns out to be the state itself and especially the other court within the same legal system of the Member State. This means that the court which tends to minimize the administrative costs will not spend resources on a thorough investigation concerning the evaluation of entitlement. In the case of rights protected by EU law, such as the right to a retirement bonus in *Köbler* or the right not to be discriminated with respect to state aid for some entrepreneurs as in *Traghetti*, the breach of EU law by Member State, be it administration, administrative or any other court depriving the individual of his or her right, could be interpreted through the lens of *transactional framework* theory, as an attempt at an involuntary taking. In other words the infringement of EU law could be interpreted as if the

⁴⁶ Ruffert, M. (2007), “Case C-173/03 *Traghetti del Mediterraneo SpA in Liquidation v. Italian Republic*, Judgment of The Court (Great Chamber) of 13 June 2006”, *Common Market Law Review*, 44, p. 479.

⁴⁷ Ayres, I. (2005), *Optional Law: The Structure of Legal Entitlements*, Chicago, Chicago University Press, p. 197.

⁴⁸ Kaplow, L., Shavell S. (1996), “Property Rules Versus Liability Rules”, *Harvard Law Review* 109, p. 713.

Member State attempted to carry out an involuntary taking of a given right. The compensation awarded due to the fact, that the illegal action of the Member State constituted an infringement of a right resulting with a loss, might therefore be interpreted as the price of such an entitlement. Hence the question arises how should the court assess this value? Intuitively, the same right established and protected by the EU law throughout all Europe should have at least similar, if not equal value, in all Member States⁴⁹. It is however not the case, since different national courts estimate the amount of damages according to national rules and use different indexes as potential points of reference. This practice stands in sharp opposition to both the EU law and the assumptions of the *transactional framework* as proposed by law and economics scholars.

Conclusion

At this stage a haphazard conclusion could be reached according to which virtually all legal systems are complex. It is not my intention to contemplate that claim which would inevitably lead to the question about the nature of law. I must admit however that I can see nothing *prima facie* wrongful in the allegation that all legal systems are complex in a sense that their legitimacy is based on circularity. I simply follow Joseph Raz and his suggestion that circularity might be the better option if we compare it to the mysterious Kelsenian foundationalism looking for the ultimate source of a legal system outside that system and finding out that the basic norm may provide with such a solid ground. Does such a complexity lead to chaos? The answer is negative if we adopt a different concept of a legal system - ad hoc rule modifies the rule of recognition. Courts act as a kind of interstitial legislator, providing with the necessary and closing the connection between all a relevant rules of a given system (the A-D connection).

In order to prove that this conclusion is sound one could address three fundamental and practical questions, especially taking into account the complexity of the EU law. Why do lawyers engage in a close and careful scrutiny the jurisprudence of relevant courts both in common and civil law countries? Why do we await, with hope or anxiety, the proceeding verdicts of CJEU in Europe? Finally, why the European Commission carefully and sensitively monitors the jurisprudence of national courts, especially supreme courts within Member States? The

⁴⁹ van Gerven, W. (1995) "Bridging the Gap between Community and National Laws: Towards a Principle of Homogeneity in the Field of Legal Remedies", *Common Market Law Review*, 32, p. 679.

importance of the courts' activity seems to be unquestionable. Nonetheless the soundness of the so-called "judicial dialogue and cooperation" should be subdued to the judicial control exerted by the potential victims of the judicial fantasy. These are reasons why the liability of Member States for breach of the Community law does not lead to chaos. Moreover, they operate in the opposite direction as they provide with a necessary remedy, transforming the "lack of democratic control" and the alleged deficit of democracy in the EU into a form of the "judiciocracy". This may be characterized as the control of the courts exerted by the courts on behalf of the citizenry, whose rights have been infringed by misapplication of the EU law.