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Contents

1. Objectives - overview

This study examines all the European Competition Policy regulations of the last 20 years, especially those specific to the maritime sector, their rationale in relation to the structure of and competition in the maritime sector and, mainly, the reasons for the very significant changes in these regulations in the last few years.

In 1986, through the Regulation No 4056/86 (a package of four regulations concerning maritime industry[1]), Maritime transport was essentially exempted from EU competition policy, more specifically from article 81(1) that prohibits agreements between firms. Conference liners were permitted to fix prices - the freight rates - between their members. The rationale was that conference liners generate substantial benefits to shippers too. In 2006 after long deliberations the Commission passed a new regulation that became effective in October 2008, bringing the Maritime transport sector in line as far as the application of article 81(1) of EU Competition Policy is concerned. Conference liners are prohibited as in other sectors; unless the combined market share is less than 30% (this kind of measure is called a "Block Exemption"). This new regulation has been resisted and is still been resisted by shipping companies but shippers associations are all for it. There are also new measures for tramp shipping (the pools) and for cabotage.

Repelling Regulation 4056/86 appears totally justifiable as the conditions for an exemption appear to be no longer fulfilled. There is no conclusive economic evidence that the assumptions on which the block exemption was justified at the time of its adoption in 1986 are, in the present market circumstances and on the basis of the four cumulative conditions of Article 81(3) of the Treaty, still justified.

In addition the Commission came to the conclusion that the exclusion of cabotage and tramp vessel services from the scope of Regulation 1/2003 had no justification and so the Regulation should be amended to include both of these services.

Both liner and tramp shipping operators search for an alternative form of cooperation, to conferences and pools respectively, that won't fall into the scope of Article 81(1).

The effect of the repeal of Regulation 4056/86 is that agreements having an actual or potential effect on trade between EU Member States and having the object or effect of preventing restricting or distorting competition in the EU to an appreciable extent are prohibited in respect of their restrictions.

Pools, as with other looser forms of cooperation involving actual or potential competitors, are by virtue anti-competitive. Following the Commission's reform program, it has become a priority for all operators to examine the extent to which pools might have an impact on EU trade and to analyze them under the EC competition rules.

[1] Journal: Interim Report of The Multimodal Group "Maritime Transport Report"

2. Target Stakeholders

1. Maritime and intermodal transport operators;
2. Law practitioners working in the area of maritime and intermodal transport;
3. Shippers.

3. Glossary terms

Affreightment, contract of - An agreement by an ocean carrier to provide cargo space on a vessel at a specified time and for a specified price to accommodate an exporter or importer.

Cabotage - The carriage of goods or passengers for remuneration taken on at one point and discharged at another point within the territory of the same country.

Conference - An affiliation of ship-owners operating over the same route(s) who agree to charge uniform rates and other terms of carriage. A conference is "closed" if one can enter only by the consent of existing members of the conference. It is "open" if anyone can enter by meeting certain technical and financial standards. Conference members are common carriers.

Consortia - An association of two or more individuals, companies, organizations or governments (or any combination of these entities) with the objective of participating in a common activity or pooling their resources for achieving a common goal.

Shipping pools operate in every sector of the tramp shipping business. A "pool" is a collection of similar vessels, under different ownerships, operating under a single administration. The pool managers market the vessels as a single, cohesive fleet unit, collect their earnings and distribute them under a pre-arranged "weighting" system.

Liner services operate a regular advertised service between ports according to timetables, carrying cargo at fixed prices for each commodity.

4. Competition Policy

4.1 Introduction to Competition Policy

Competition is seen as a process that allows a sufficient number of producers in the same market or industry to independently offer different ways to satisfy consumer demands. Since competition is often equated with rivalry, it pressures firms to become efficient and offer a wider choice of products and services to consumers at lower prices. Firms in competitive markets are forced to compete by raising their productivity, either by means of increased investment, innovation or more efficient business practices. The end result is improved efficiency and improved welfare.

Competition is central to a properly functioning free market economy and vital to promoting economic growth. Efforts to ensure that markets work properly and are free from competition distorting practices are essential to every single industrial country. The shape and form of these efforts may vary from one country to another, but they all have in common their underlying goals and their general principles.

A subset of competition is competition policy, and its subset is competition law. Competition policy has a narrow and a broad definition. In its narrow sense it prohibits anti-competitive action and transactions by enterprises. In its broader sense it safeguards the market competition from distortions caused from government powers.[2]

In the U.S., competition policy is more commonly referred to as anti-trust policy. The 19th century was characterized by a massive American economic expansion. But much of the economic activities in such important areas as oil, steel, railroads and finance were influenced by extensive collusion. In 1890 the federal government passed the Sherman Act, aimed at stopping the anticompetitive behaviour of the cartels and trusts. The Sherman Act prohibits anticompetitive practices and attempts at monopolization. Since the Sherman Act lacked provisions on mergers, the federal government passed the Clayton Act in 1914. Since their inception, these acts have been changed repeatedly, but remain the source of the American Competition policy.

Much of the practical work in the field of competition policy takes place in two places: the courtroom and the academic world, each of course influencing the other.

A development in the academic world, which has come to influence American anti-trust case law substantially, is the emergence of the Chicago School of economics. Its main proponents, such as Robert Bork, believe that government intervention in the field of anti-trust is both unnecessary and potentially harmful and that cooperation and mergers can have substantial gains in terms of efficiency.

The European competition policy has two dimensions: firstly that of the member countries individually and secondly that of the Union as a whole. Although historically important, the national competition policies of the EU member states are now of less importance, since they

[2] Katsoulakos and Bettas N., 2004, p. 209-210

are expected to conform to the EU competition policy. Furthermore, the EU competition policy has supremacy over the national competition policy. The Treaty of Paris, signed in 1951, gave birth to the EU competition policy. Since then, the EU competition policy provisions have been adopted in the Treaty of Rome, signed in 1957. Due to their broad nature, the provisions were left to interpretation by the European Commission, under supervision of the European Court of Justice. This has meant that case law has played a pivotal role in the evolution of the EU competition policy. Aside from the traditional, economic objectives of competition policy, the EU competition policy adds the objective of market integration. Today, the EU competition provisions are found primarily in articles 81 (collusion) and 82 (abuse of dominance) of the Treaty. [3]

The underlying goal of competition policy is to promote efficiency and maximise welfare. The appropriate definition of welfare is the sum of consumers' surplus and producers' surplus. Competition policy should be used to promote competition and encourage efficiency and growth. In addition, if possible, competition policy should also be made consistent with social objectives.

It could be true in some cases that competition policy could not only lead to increased efficiency but contribute to other social objectives as well. However, such a deliberate strategy of trying to achieve multiple objectives using one policy, like competition policy which is mainly suited for efficiency enhancement purposes, may be extremely difficult to manage. Although economic welfare and market efficiency are the basic objectives of competition policy, competition policy generally has been viewed as a way of achieving or preserving a number of other objectives as well such as protection of small business, promoting market integration, fairness and equity, and other socio-political values. The inclusion of multiple objectives, however, increases the risk of conflicts.

A successful competitive economy requires open markets that are open to new ideas and entrepreneurs that will promote innovation. Small businesses can be an important vehicle for these competitive forces. However, protecting small businesses could conflict with economic welfare objectives. The reason is that firms should not be artificially protected when they don’t operate efficiently because then competitors rather than competition may be protected.

[3] Sauter Wolf , 1997, p. 26-38

In addition, such concerns as fairness and equity cannot be quantified easily or even defined acceptably. Attempts to incorporate them could result in inconsistent application and interpretation of competition policy. Clear standards would be unlikely to emerge, thereby leading to uncertainty and distortions in the marketplace and the undermining of the competitive process.[4]

In most cases the conflicts between economic efficiency and other policy objectives either are insignificant or can be balanced.

The goal of promoting market integration was important when the common market was still being established. Where industries were traditionally established within national markets, the challenge was to get them to transcend those boundaries. It was believed that the policy goals of Community competition law were not efficiency or equity, but legality in the service of market integration. Nowadays, the relative importance of the market integration goal has declined.

Most nations have their own competition laws, and there is a general agreement on what is and what is not acceptable behaviour. The degree to which countries enforce their competition policy does vary substantially, with The United States generally regarded as having the most strict competition laws and enforcement.

4.1.1 US Antitrust Law

Antitrust first became effective in the US near the end of the nineteenth century. The antitrust movement started after the consolidation of industry that followed the Civil War. Following the war, large trusts emerged in industries such as railroads, petroleum, sugar, steel, and cotton. The concerns about the growth and abusive conduct of these trusts generated support for legislation that would restrict their power. The first antitrust law in the USA was the Sherman Act, 1890. Section 1 of the Act prohibits: 'Every contract, combination in the form of trust of otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations.'

Section 2 of the Sherman Act states that it is illegal for any person to '…monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any

[4] OECD & World Bank, 1998, p. 4-5

part of the trade or commerce among the several States, or with foreign nations….'. These two sections of the Act contain the two central key principles of modern antitrust policy.

Early in the twentieth century it became apparent that the Sherman Act did not adequately address combinations, such as mergers, that were likely to create unacceptably high levels of market power. In 1914 Congress passed the Clayton Act, which identified specific types of conduct that were believed to threaten competition. The Clayton Act also made illegal conduct whose effect 'may be to substantially lessen competition or tend to create a monopoly in any line of commerce.'

The US is nearly unique among competition law countries in having two enforcement agencies, the Federal Trade Commission (FTC) and the Department of Justice (DOJ). Section 5 of the Federal Trade Commission Act, which enables the FTC to challenge unfair competition, can be applied to consumer protection as well as mergers.

The differences between the two enforcement agencies are that the FTC is responsible for consumer protection issues, whereas criminal violations of Sect.1 of the Sherman Act (e.g., price fixing and market division) are the responsibility of the Antitrust Division.

4.1.2 EU Competition Policy

There are three core substantive norms of EU competition law that are addressed to undertakings: **a.** the prohibition of agreements and concerted practices between firms restricting competition, **b.** the prohibition of abuse of (single firm or joint) dominance, **c.** the prohibition of mergers and acquisitions.[5]

Agreements between two or more firms which restrict competition are prohibited by Article 81 of the Treaty, subject to some limited exceptions. This provision covers a wide variety of behaviours. The most obvious example of illegal conduct infringing Article 81 is a cartel between competitors (which may involve price-fixing or market sharing). Second, firms in a dominant position may abuse that position (Article 82 of the EC Treaty). This is for example the case of predatory pricing aiming at eliminating competitors from the market.

[5] Sauter Wolf , 1997, p. 66

The Commission is empowered by the Treaty to apply these prohibition rules and enjoys a number of investigative powers to that end. It may also impose fines on undertakings that violate EU competition rules.

Article 81 prohibits agreements and concerted practices aimed at lessening competition within the common market and that may cause distortions in the trade between Member States. In particular, it prohibits price fixing, market sharing, output restrictions and tie-in sales. Such agreements and decisions are automatically void. Paragraph 3 defines the situations in which agreements, decisions and concerted practices can be accepted: a) if they improve the production or distribution of a good or promote technical or economic progress; b) if consumers receive a share of the resulting benefits; c) if the restrictions imposed are indispensable to the attainment of these objectives; d) if the firms concerned do not have sufficient market power to restrict competition in the product market.

In the case of agreements concluded to fix prices, restrict output or share markets, the Commission has adopted a criterion that is very similar to per se prohibition.

The Commission has also punished the exchange of information among undertakings as a practice facilitating collusion. For instance, in 1974 26 glass producers made an agreement to exchange data and information about prices and production levels. The Commission forbade the agreement, considering that it allowed to maintain agreed upon prices and to ease the detection of deviations from the agreements.

Article 82 of the EC Treaty prohibits the abuse of a dominant position.

The first problem is the definition of the relevant market, and therefore of the dominant position, before evaluating its possible abuse.

The more restrictive the definition of the market is, the larger the share of the concerned firm will result. The relevant market is defined by two aspects: the product one, i.e. the set of goods belonging to the same market, and the geographical one, i.e. the area within which the firm operates. As for the first aspect, the delineation of the market rests upon the degree of substitutability between products, usually measured by the cross-price elasticity. As for the second one, geographic market delineation usually rests upon the functioning of arbitrage, product prices tending to be uniform within the same market, the only differences being due to transport costs.

The existence of a dominant position is then evaluated on the basis of several structural variables, such as the number of firms, their respective market shares and the nature of entry- and exit-barriers. The abuse of dominance refers to a behaviour that influences market conditions and lessens competition, by adopting methods that differ from the usual competitive ones.

Abuses are commonly divided into exclusionary abuses, those which exclude competitors from the market, and exploitative abuses, those where the dominant company exploits its market power by, for example, charging excessive prices. Where a dominant company is present on a market, competition on that market is already weak. The concern of the competition rules is therefore to prevent conduct by that dominant company which risks weakening competition still further, and harming consumers.

For price based conduct, a conduct which would risk the exclusion of equally efficient competitors should be considered as abusive.[6]

The main legislative texts for merger decisions are the EC Merger Regulation and the Implementing Regulation**.** While companies combining forces can expand markets and bring benefits to the economy, some combinations may reduce competition. Combining the activities of different companies may allow the companies, for example, to develop new products more efficiently or to reduce production or distribution costs. Through their increased efficiency, consumers benefit from higher-quality goods at fairer prices.

However, some mergers, especially when they are horizontal in structure, may reduce competition in a market, usually by creating or strengthening a dominant player. This is likely to harm consumers through higher prices, reduced choice or less innovation. Increased competition within the European single market and globalisation are among the factors which make it attractive for companies to join forces. Such reorganisations are welcome to the extent that they do not impede competition and hence are capable of increasing the competitiveness of European industry. The objective of examining proposed mergers is to prevent harmful effects on competition.

[6] Europa, 2005, IP/05/1626

All proposed mergers notified to the Commission are examined to see if they would significantly impede effective competition in the EU. If they do not, they are approved unconditionally. If they do, and no commitments aimed at removing the impediment are proposed by the merging firms, they must be prohibited to protect businesses and consumers from higher prices or a more limited choice of goods or services. Proposed mergers may be prohibited, for example, if the merging parties are major competitors or if the merger would otherwise significantly weaken effective competition in the market. However, not all mergers which significantly impede competition are prohibited.

4.2 Article 81

Article 81 of the treaty bans agreements between companies that harm consumers by distorting competition and trade between member-states. That ban covers horizontal agreements between firms in the same industry, and vertical agreements between companies along the supply chain.

The notion "agreement" is interpreted broadly under EC competition law. It covers any written or oral agreement between two or more undertakings, whether legally enforceable or not and whether binding or non-binding.

When an agreement is secretive it is called collusion. Collusion takes place within an industry when rival companies cooperate for their mutual benefit. Collusion most often takes place within the market form of oligopoly, where the decision of a few firms to collude can significantly impact the market as a whole. Cartels are a special case of collusion that has institutional form. Collusion which is not overt, on the other hand, is known as tacit collusion. Such collusion does not involve an agreement. When some sort of agreement among the colluding firms is involved the collusion is called explicit.

Many characteristics can affect the sustainability of collusion.[7] The number of competitors on the market is clearly an important factor. Since firms must share the collusive profit, the greater the number of firms the lower the market share they will get. It is thus more difficult to prevent firms from deviating. It should also be clear that collusion is difficult to sustain if there are low barriers to entry. That is because if the already existing firms try to maintain high prices new firms will be willing to enter the market.

[7] Tirole J., 1988

Another characteristic that can affect collusion is the frequency of interaction. There is more scope for collusion when the same firms compete repeatedly. The reason is that firms can react more quickly to a deviation by one of them if they collude. Market transparency is also a factor that facilitates collusion. If prices are not easily observable it is difficult for firms to collude because in other way any deviation could not be recognized. Collusion is more difficult to sustain in declining markets, because the future profits would be small anyway. So market growth is an important factor too.

Innovation gives to a firm a very important advantage over its rivals. It is then obvious that the mentioned rivals would not be willing to collude. Such as innovation product differentiation makes collusive behaviour more difficult. When differentiation aims at segmenting customers and creating customer loyalty it is obvious that those firms have nothing to fear from deviation and thus the other firms avoid collusion. In addition observability issues and information problems may arise which mean that it would be difficult to recognise possible future deviation.

Finally more symmetric market shares facilitate collusion, since the firm with the lowest market share has more to gain from a deviation, and less to lose from retaliation.

Other factors have often been mentioned or looked by competition authorities.

Article 81(1) of the EC Treaty prohibits agreements and other collusive behaviour between undertakings which may affect trade between Member States and which have as their object or effect the restriction, prevention or distortion of competition within the EU. If an agreement falls within this prohibition, it will be automatically void under Article 81(2) unless it can satisfy the provisions for exemption under Article 81(3). That means if it improves production or distribution or promotes technical or economic progress, if it allows consumers a fair share of the benefit, if the restrictions are indispensable to attaining the beneficial objectives and if it does not permit the elimination of competition for a substantial part of the products in question.

4.3 Article 82

The EC Treaty makes clear that its competition rules are designed to establish “a system ensuring that competition in the internal market is not distorted”. In applying Article 82, this means preventing practices of dominant firms that distort the normal functioning of the market.

The “normal functioning” of the market in the presence of dominant firms can have different meanings. It could mean a market that is efficient in the sense that it leads to optimal allocation of resources, provides to economic agents appropriate incentives to pursue innovation, efficiency and quality, and maximizes consumer welfare. Under this interpretation, the rules on abuse of a dominant position are enforced against conduct of dominant undertakings where it is established that the conduct does not enhance efficiency and harms consumers.

The “normal functioning” of the market could also mean a market in which economic agents have access to the market and operate on the market without obstacles created by dominant undertakings. This means that the presence of a number of competitors on the market is of paramount importance and is considered as necessary in order for the market to function so as to achieve the ultimate purpose of competition rules. Under this interpretation, the rules against abuse of dominant position are seen primarily as protecting competitors in order to protect competition. The drawback of this interpretation is that, by focusing on the presence of competitors, it may end up protecting less efficient competitors and prohibiting conduct of dominant undertakings that furthers Article 82’s ultimate purpose of promoting an efficient market. In addition, protecting rivals against competition from the dominant undertaking may reduce their incentive to engage in robust and creative competition that can further efficiency and benefit consumers.[8]

It is not clear as to which interpretation is correct. Various concepts have been used as benchmarks for assessing whether the conduct of a dominant undertaking is abuse. These vague concepts need to be clarified and elaborated so as to reflect the purpose of the rules against abuse of dominance. In its Guidelines on the Application of Article 81 (3), the Commission has done so with respect to the concept of “restriction of competition” and has put forward consumer welfare as the ultimate test.

Harm to consumers, which is expressly referred to in Article 82 (b), is the ultimate test of abuse of dominance, just as it is for Article 81. The ECJ has made clear that the purpose of Article 81 and 82 should be consistent. If harm to consumers is the ultimate test for “restriction of competition” under Article 81, it should be so as well under Article 82.

[8]ICC, 2005, Document n° 225/623

Article 82 is one of the next subjects due for modernisation. The intention is to move from a legalistic and formalistic approach towards enforcement based on economic principles.

4.4 Mergers

A merger is the amalgamation of two or more firms into a single firm. This is typically accomplished by one firm acquiring the assets of the other firm(s). Hence such transactions are referred to as mergers and acquisitions (M&As). There are three types: horizontal mergers involving firms in the same industry, vertical mergers between firms at different stages of the production chain, and conglomerate mergers between firms in unrelated industries. Merger policy typically considers two possible anticompetitive consequences to mergers. On one hand, a merger may induce a unilateral effect on market power. Unilateral effects occur if the merged firm is able to charge higher prices and still increases its profits. On the other hand, a merger may induce a coordinated effect on pricing behaviour. With coordinated effects, the merged firm cannot raise the price on its own but the merger enhances the scope for collusive pricing in the market.

5. The Maritime Market

5.1 Introduction to Maritime Industry

When examining the maritime industry it is immediately realised that this term covers a number of diverse activities which are only linked together by a common characteristic, the carriage of goods and passengers by vessels over the surface of water. The maritime shipping industry is fundamental to international trade because it is the only practicable and cost effective means of transporting large volumes of many essential commodities and finished goods. A criterion for classifying shipping activities concerns the service offered, i.e. whether the ship involved operates in the liner or tramp trades. In the liner trades the ships are operated by companies which provide regular, scheduled, services to shippers or forwarders between specific ports. A key feature in the liner trades is the organisation of shipping companies into conferences hypothetically for the purpose of organising the services. Tramp services on the other hand involve “any transport of cargo in ships which are hired wholly or partly for the carriage of cargoes on the basis of a voyage or time charter or any other form of

contract for non-regularly scheduled or non-advertised sailings where the freight rates are freely negotiated case by case in accordance with the conditions of supply and demand." [9]

Another way of classifying the shipping activities is to use the criterion of the type of good or passenger being transported.

a. The transportation of cargoes in bulk which usually represent raw materials which are used in various manufacturing processes. These cargoes can be subdivided into: (i) liquid bulks (oil, oil products), (ii) dry bulks (iron, grain, coal, etc.)
b. The carriage of general cargo, which mostly consists of finished manufactured products.
c. The transportation of containers.
d. The carriage of passengers.
e. The production of tourist services on board ships, i.e. cruising services.

Bulk cargoes are transported with tramp ships such as tankers, bulk carriers, combined carriers, specialist bulk vessels whilst general cargoes and containers with liner ships such as multipurpose, container and Ro-Ro vessels. Ro-Ro vessels are ships designed to carry wheeled cargo such as automobiles, trucks, etc. As seen in Figure 1 bulk ships hold the lion's share when the process and handle of cargo through EU ports is concerned. Another issue that can be mentioned is the highly containerized liner shipping fleet as almost half of the liner ships that entered EU ports were container ships.

[9] Commission of the European Communities, 2008, p. 4

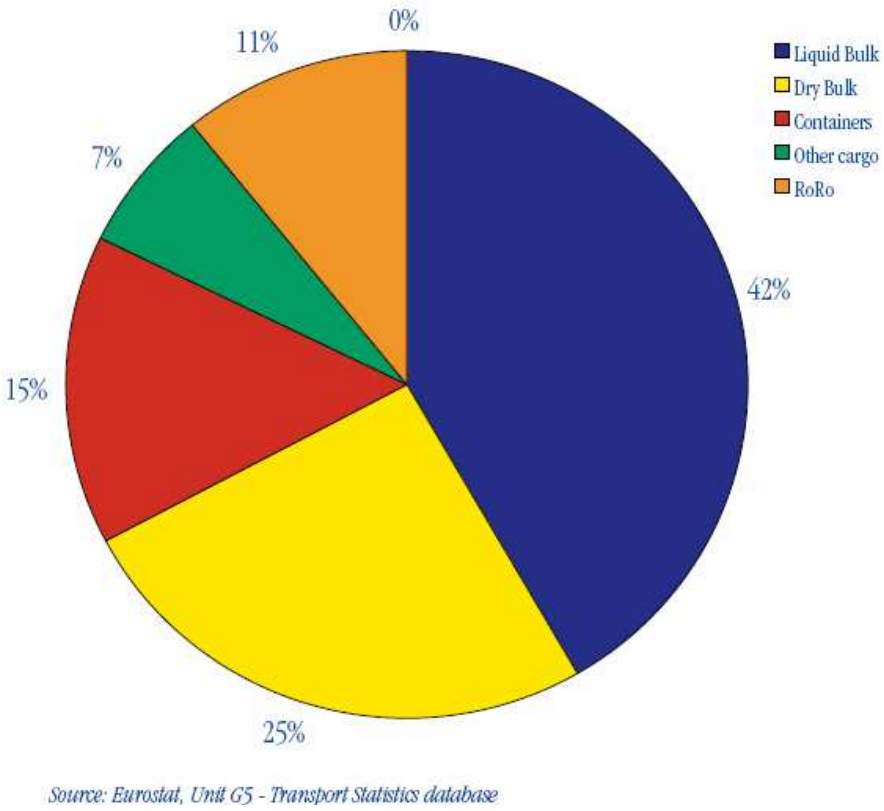

Figure 1 EU Port Throughput by Cargo Type in 2004

5.2 Market Structure in Maritime Sector

The maritime transport sector exists to provide services to other sectors, most notably agricultural, resources and manufacturing.

As such, an efficient and competitive maritime transport sector is essential to the fundamental and sustained competitiveness of these sectors, and the industries and firms within them, whether they are traded or non-traded sectors.

Maritime transport remains the backbone of global trade and transport, eclipsing the main alternate mode, air transport.

Better forecasts see the international maritime transport sector growing by around 8 per cent per annum, on current global economic conditions, with ocean-going vessels (whether tanker, bulk or liner) becoming ever larger and capable of carrying greater loads (for example, container vessel capacity has increased to around 7,000 containers).

Taken as a whole, the international maritime transport sector is regarded as fairly liberal and competitive, especially when compared with other services sectors and transport sub-sectors.

5.2.1 The Issue of Market Definition

The first step when evaluating a competition case is the definition of the relevant product and geographic market. The main purpose of market definition is to identify in a systematic way the competitive constraints faced by an undertaking.

The relevant product market comprises all those products and services which are regarded as interchangeable or substitutable by the consumer, by reason of the products' characteristics, their prices and their intended use.

The relevant geographic market comprises the area in which the undertakings concerned are involved in the supply and demand of products or services, in which the conditions of competition are sufficiently homogeneous and which can be distinguished from neighboring areas because the conditions of competition are appreciably different in those areas.

A carrier cannot have a significant impact on the prevailing conditions of the market if customers are in a position to switch easily to other service providers. [10]

5.2.2 Liner shipping

Containerized liner shipping services have been identified as the relevant product market for liner shipping in several Commission decisions.

Other modes of transport have not been included in the same service market even though in some cases these services may be substitutable.

This was because only an insufficient proportion of the goods carried by containers can easily be switched to other modes of transport, such as air transport services.

It may be appropriate under certain circumstances to define a narrower product market, limited to a particular type of product transported by sea. For example, the transport of perishable goods could be limited to reefer (refrigerated ship) containers or include transport in conventional reefer vessels. While it is possible in exceptional circumstances for some substitution to take place between general cargo and container transport, there appears to be no change over from container towards bulk. For the vast majority of categories of goods and users of containerized goods, general cargo vessels do not offer a reasonable alternative to containerized liner shipping.

Once cargo becomes regularly containerized it is unlikely ever to be transported again as non-containerized cargo.

The relevant geographic market consists of the area where the services are marketed, generally a range of ports at each end of the service.

[10] Lorenzon Filippo & Nazzini Renato, 2007, C215/5

As far as the European end of the service is concerned, to date the geographical market in liner cases has been identified as a range of ports in Northern Europe or in the Mediterranean. As liner shipping services from the Mediterranean are only marginally substitutable for those from Northern European ports, these have been identified as separate markets.

5.2.3 Tramp Shipping

In relation to tramp shipping, the Commission identifies the elements which must be taken into account when defining the market. In general, the substitutability of different vessel sizes must be assessed in order to ascertain whether each vessel size constitutes a separate relevant market.

With regard to the definition of the geographical market, the loading and discharging ports provide the first indicators.

These elements reflect long-established principles of market definition.

Liner Conferences

Perhaps one of the most important characteristic of the liner shipping industry is its high fixed costs. In order to keep its pre-advertised time-schedule, a ship must leave port regardless if it is full or not. Its costs thus become fixed, i.e. independent of the amount of cargo carried. Also, if minutes before the ship sets sail, an unexpected customer arrives at the port with one container to ship and the vessel has unfilled capacity, which is often the case in liner shipping, its operator would be tempted to take on the extra container even at a price as low as merely the marginal cargo-handling costs involved in taking the container onboard. If this were to become common practice among operators, competition among them would push prices down to the level of short-run marginal costs and consequently the liner service would not be sustainable in the long-run, as operators would not be able to cover full costs.

So it has been thought that price competition should be limited and a mechanism should be found to allow operators charge long-run average total costs to the benefit of a sustainable, regular, frequent and reliable service, according to the requirements of demand. This mechanism was found in the face of 'conferences', which are cartel-like coalitions of carriers, having price-setting as their main objective.[11]

In the UNCTAD Code of Conduct for Liner Conferences (UNCTAD, 1975), the term conference or liner conference is defined as '...a group of two or more vessel operating carriers which

[11] Haralambides H.E., 2000

provides international liner services for the carriage of cargo on a particular route or routes within specified geographical limits and which has an agreement or arrangement, whatever its nature, within the framework of which they operate under uniform or common freight rates and any other agreed conditions with respect to the provision of liner services'.

Internal competition, i.e. forces within the conference moving in different directions, and, the endeavour of liners to eliminate fellow carriers within the conference, provide a climate not willing to set monopolistic freight rates. One must bear in mind that the members of a conference once were competitors uniting to avoid extinction, but competition never completely disappear. The members may cover a wide range of nationalities and histories of operation, and the extent of interest each member have in a particular trade and in other lines certainly differ widely.

In order to achieve better returns, individual members will strive for maximum utilisation and efficiency. The desire for greater profits is the strongest inducement for competition among the members.

At times the rules of the agreement aiming at regulating the behaviour of the members are broken as a result of competition amongst members. Breaches of the agreement can be used to attract shippers, by, for example, calculating the freight rate upon weight instead of volume to give the shipper a lower rate and thus the miscalculating member an additional shipper.

One of the most effective ways a conference member has to promote its interests on the expense of competition is loyalty agreements. But even these arrangements cannot tie the shipper to one carrier, and thus internal rivalry thrives. Hopefully internal competition results in better service for shippers.

Conferences compete with each other too of course, offering alternative routes for the transportation of similar products through different gateways. Alternative routes and products can hence limit the monopolistic trends.

Competition between conference liners and independent liners is also of significant importance. When a liner chooses to join the conference or not he will compare two effects. On the one hand, it is attractive to become an independent liner and be able to undercut the conference price (second-mover advantage in price competition). This is based on the realistic presumption that the conference, which dominates the market, is a price leader and

independent liners are the followers. Of course, the conference will anticipate competition by the independent liners and start out with a rather low price. Therefore, on the other hand, reducing the number of independents by joining the conference has the advantage that one can profit from a rather high price, since the conference price will be the higher the lower the number of independent liners. Comparing these effects, each liner will decide to join the conference or not. Depending on the total number of firms, it turns out that either all join in, or that there is also a group of one or more independent liners around it. Generally, the following holds. For any given number of carriers, prices are the lower the larger the number of independent liners is. It's very likely that the price will be somewhere in between the case of full conference membership and the fully competitive case (i.e. without conferences). Moreover, the larger the number of carriers in the market the larger will be the subset of independent liners. Thus, the larger the number of carriers in the market the lower will be the price. In any case, a ban of conferences would always lead to a further price reduction.

6. Competition Policy in Maritime Sector

6.1 Historical Development of Agreements in Maritime Sector

The advent of the steamship around 1850s led to a number of changes in the shipping industry. Before, it had not been possible to offer a service based on a fixed schedule since the sailing times depended on the weather. Additionally, the volume of international trade and the transport capacity increased considerably. The reduced length of the Europe-Asia route resulting from the opening of the Suez Canal in 1862 led to excess capacity, and over-tonnage became one of the central problems. In order to combat the resulting competition, ship owners began to enter into agreements regarding prices and other conditions of transport, called conferences.

The first such conference concerned the United Kingdom – Calcutta, India route and started operation in 1875. The conference system soon spread throughout the world. At first, governments accepted its existence. In England, the Royal Commission on Shipping Rings in 1909 referred to advantages such as rate stability and regularity of service. In the United States, the so-called Alexander Committee investigated the effects of shipping conferences in the light of the Sherman Act of 1890 and concluded that the advantages of the conference

system significantly out-weighed the disadvantages. This led to the adoption of the Shipping Act of 1916 which allowed for conferences under government control.[12]

If the advent of the steamship caused a first revolution in maritime transport, a second revolution occurred with the invention of container shipping, starting in 1966 in the USA. Containerization resulted in an enlargement of transport capacity and a speeding up of travel, due to the modern vessels used. It also created the possibility of door-to-door transport by the way of intermodal or multimodal transport, which is a combination of sea and land transport offered by the same carrier. In line with the extension of the shipping services offered by ship-owners to include the inland segments, conference tariff agreements extended to cover the inland transport of sea-borne containers.[13]

Further, the costs for stevedoring were reduced due to the possibility of mechanical loading and unloading. This was also faster, allowing the vessel to spend more time on sea generating profits. At the same time, containerization made the purchase of new and expensive vessels necessary and carriers had to incur costs for the provision of containers. For the customer, the packaging costs were likely to be reduced; carriers regularly provided the containers free of charge.

Goods transported in a container are also less susceptible to damage and pilferage. Containerization led to structural changes in the maritime transport industry in the form of a new type of alliances, called consortia. Different from conferences, consortia do not focus primarily on price fixing. They are a form of co-operation with the aim of sharing the high costs involved in operating a modern container fleet (no longer affordable to the existing liner companies) while improving the quality of service. [14]

6.2 EC Maritime Legislation

It is well known that for a long time the Common Transport Policy was largely characterized by inactivity on the side of the Community, particularly in the field of maritime transport. One possible reason20 for this is the fact that, before the accession of the United Kingdom, Ireland

[12] Felix Dinger, 2000, p. 6-8

[13] Interim Report of The Multimodal Group, 1994, Sec (94)933, p. 31- 50

[14] Felix Dinger, 2000, p. 6-8

and Denmark in 1973, the Member States were all connected by land. Before 1973, 90% of the intra-Community transport was land-bound. Thereafter, more than 90% of the transport to the new Member States was maritime, with no alternative. More recently, 33 percent of intra-Community trade and 90% of the trade between the Community and third countries is carried by ship.

The Commission report "Progress Towards a Common Maritime Policy: Maritime Transport", published in 1985, constituted the first attempt to develop an EC shipping policy in a systematic way.[15] It contained several specific proposals for Regulations. In 1986 four Regulations were adopted which are now at the centre of EC maritime policy. These Regulations were 4055/86, 4056/86, 4057/86 and 4058/86.

As far as consortia are concerned, the Council asked the Commission already at the time of the adoption of Regulation 4056/86 whether there was a possibility for granting a group exemption. In 1990 the Commission presented a report in which it stated that consortia can help to increase productivity and capacity utilization, produce economies of scale leading to reduced costs, increased reliability and improved quality. The report also contained a first draft for an enabling Regulation.

Regulation 479/92 was adopted on the basis of Art. 83 of the Treaty.

Based on this Regulation, the Commission presented a draft text for a block exemption in 1994 which led to the adoption of Regulation 870/95, later replaced by Regulation 823/2000.

Also an exception of importance for competition law was the early 1990´s adoption of the Council Regulation 3577/92, the cabotage Regulation.

6.2.1 What is a Block Exemption Regulation?

Article 81(1) of the EC Treaty prohibits agreements which affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market. Under Article 81(3) a restrictive agreement may be exempted from the prohibition of Article 81(1) if the positive effects brought about by the agreement outweigh its negative effects and a fair share of these benefits is passed on to consumers.

[15] Tunfors Henrik , 2001

For certain sectors, the Council has empowered the Commission to exempt whole categories of agreements by adopting Regulations, the so called "block exemption" Regulations. The agreements covered by the Regulation are deemed compatible with the competition rules on condition that they respect the rules laid down in the Regulations.

Before granting a block exemption, the Commission needs to be absolutely certain that the agreements covered are compatible with the competition rules.

Moreover, block exemption Regulations are always limited in time so that the Commission can regularly check if market developments have not altered the compatibility conditions.

It is exceptional for a block exemption Regulation to be incorporated in a Council Regulation as is the case of the liner conference block exemption. It is also exceptional for such an exemption to be open-ended in terms of duration as was Regulation 4056/86.[16]

6.2.2 1986 Maritime Package

Agreements between ship-owners which restrict competition were subject to the same principles of Community competition law as all other industries. These principles require, among other things, that restrictive agreements should allow users of the products or services in question a fair share of the improvement in production or distribution or of the technical or economic progress which the restrictive agreement brings about. Therefore if a restrictive agreement brings about no improvement or progress, or if users do not get a fair share of any improvement, the agreement cannot be authorized and of course from an economic viewpoint it should not be authorized.

However in 1986 a broad block exemption from the usual ban on restrictive agreements was given by Regulation No 4056/86. This Regulation was a part of a package of four Regulations concerning maritime industry.[17]

The Maritime Package agreed in 1986 by the EU Ministers forms the basis of the EU common policy on shipping and it is the outcome of a consensus among the EU member countries in a way to pursue a free market oriented approach in liner shipping.

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[16] Europa, 2006, MEMO/06/344

[17] Interim Report of The Multimodal Group, 1994, p. 31- 50, Sec (94)933

This Package includes the Regulations:

i) No. 4055/86 on the principle of freedom to provide maritime transport services between member states and between member states and third countries,

ii) No. 4056/86 on competition rules concerning the application of Articles 85 and 86 of the Treaty of Rome. Article 85 of the Treaty of Rome prohibits agreements between undertakings to fix prices and share markets. Article 86 prohibits the abuse of the dominant position by, for example, fixing unfair prices. Both articles prohibit the applying of dissimilar conditions to equivalent transactions with other trading partners, thereby placing them at a competitive disadvantage,

iii) No. 4057/86 on unfair pricing practices in maritime transport and

iv) No. 4058/86 on coordinated action to safeguard free access to cargoes in ocean trades. [18]

6.2.2.1 Regulation 4055/86

Regulation 4055/86 applies to maritime transport services between Member States and between Member States and third countries which are intended to incorporate the following: a) intra-community shipping services, i.e. the carriage of goods or passengers by sea between any port of a Member State and any port or off-shore installation of another Member State and b) third country traffic, i.e. the carriage of goods or passengers by sea between the ports of a Member State and ports or off-shore installations of a third country.[19]

It also makes reference to the issue of beneficiaries of the Regulation. There are two categories of beneficiaries: a) nationals of Member States, b) nationals of Member States established outside the Community and shipping companies established outside the Community and controlled by nationals of a Member State.[20]

The Regulation confirms the anti-protectionist stance of the Community by requiring the Member States to phase out the unilateral restrictions by which they reserved the carriage of certain goods for vessels flying their own flag, to phase out or adjust the cargo-sharing agreements that they had concluded with third countries before the entry into force of the Regulation on 1 January 1987 and finally not to enter into cargo-sharing arrangements after

[18] Commission of The European Communities, 1990, SEC(90)1594
[19] Jason Chuah, 2003, Journal of International Maritime Law, 9(1), p.83-85
[20] Commission of the European Communities, 1995, COM(95)163

the date of entry into force of the Regulation other than in those exceptional circumstances where Community liner shipping companies would not otherwise have an effective opportunity to ply for trade to and from the third country concerned. In this case, a decision from the Council is required and the rights of the beneficiaries of the Regulation have to be protected.

Broadly speaking, the Community decided that there should generally be no further requirement other than the carrier being seated in a Member State or the relevant ships being registered under the flag of a Member State to confer the right to provide shipping services between the Member States or third countries and the Member States. The rules that gave preferential treatment to ships running under the national flag are no longer permissible.

6.2.2.2 Regulation 4056/86

Liner conferences have existed in Western Europe since 1875, thus during 125 years, 82 years longer than the Community. Their traditional practice of systematic distortion of competition is given authorization through Regulation 4056/86.

The main content of Regulation 4056/86 is the block exemption in favor of specific agreements of liner conferences which is the main objective of adopting the Regulation.

Regulation 4056/86 "shall apply only to international maritime transport services from or to one or more Community ports, other than tramp vessels services".

Thus, neither cabotage nor tramp vessel services are able to be exempt under this Regulation. Liner Conferences are, as defined in Article 1.3(b) of Council Regulation 4056/86, "a group of two or more vessel-operating carriers which provide international liner services for the carriage of cargo on a particular route or routes within specified geographical limits and which has an agreement or arrangement, whatever its nature, within the framework of which they operate under uniform or common freight rates and any other agreed conditions with respect to the provision of liner services".

The reference in the definition to 'a group of two or more vessel-operating carriers', is the first limitation, through which agreements between carriers who do not operate vessels are not qualified for an exemption.

The phrase 'International liner services', excludes both restrictive agreements in non-liner shipping and specialized bulk transport, and cabotage conferences.

The requirement 'on a particular route or routes within specified geographical limits', is not specified in the Regulation, but conference shipping companies are not free to select routes since the monopolistic character of the conferences does not allow that.

The conference members also have to operate 'under uniform or common freight rates and any other agreed conditions with respect to the provision of liner services'. The meaning of uniform or common freight rates is that rates have to be non-discriminatory and unique for each product.

We can therefore conclude liner conferences to be associations which coordinate the operation of regular shipping services for the carriage of general cargo on set routes with fixed schedules and tariffs. These conferences standardize or harmonize the uniform freight rates, sailings etc. of the members of the conference. [21]

Technical Agreements

Article 2.1 of the Regulation provides an exemption under Article 81(3) of the Treaty for certain types of agreements, decisions and concerted practices, if they do not restrict competition and their sole object and effect is to achieve technical improvements or cooperation. These goals can be achieved by:

(a) The introduction of uniform application of standards or types of vessels and other means of transport, equipment, supplies or fixed installation.

(b) The exchange or pooling for the purpose of operation transport services, of vessels, space on vessels or slots or other means of transport, staff, equipment or fixed installations.

(c) The organization and execution of successive maritime transport operations and the establishment and application of inclusive rates and conditions for such operations.

(d) The coordination of transport timetables for connecting routes.

(e) The establishment or application of uniform rules concerning the structure of transport, on condition that such rules do not directly or indirectly fix rates.

[21] Tunfors Henrik , 2001

It must be stressed that the sole object and effect must be to conclude a technical agreement. Any other motive will inactivate the exemption.

The Conference Block Exemption

Article 3 is the principal provision of Council Regulation 4056/86. This provision provided the long awaited legal security as regards the application of the Treaty's competition rules to maritime transport.

It is stated that 'agreements, decisions and concerted practices of all or part of members of one or more liner conferences' are exempted from the application of Article 81(1) of the Treaty. The exemption may be withdrawn under certain circumstances, but is otherwise for an unlimited period of time.

Liner Conferences and agreements are exempted when they have as their objective the fixing of rates and conditions of carriage of goods and one or more of the objectives as stated under Article 3(a)-(e):

(a) The co-ordination of shipping timetables and sailing dates.

(b) The determination of the frequency of sailings.

(c) The co-ordination or allocation of sailings among members of the conference.

(d) The Regulation of the carrying capacity offered by each member.

(e) The allocation of cargo among members.

Thus, the main characteristic of the liner conference block exemption is that the members of liner conferences fix rates.

The Liner Conference Arrangements

Article 4 of the Regulation provides:

"The exemption provided in Articles 3 and 6 shall be granted subject to the condition that the agreement shall not, within the common market, cause detriment to certain ports, transport users or carriers by applying for the carriage of the same goods and in the area covered by the agreement, rates and conditions of carriage which differ according to the country of origin or

destination or port of loading or discharge, unless such rates or conditions can be economically justified. Any agreement or decision or any part of such an agreement or decision not complying with this condition shall be void automatically under Article 81(2) of the Treaty."

This means that the rates must be non-discriminatory for each service.

However, the shipping lines members of a conference are entitled to institute and maintain loyalty arrangements with transport users, the form and terms of which should be matters for consultation between the conference and transport users' organizations. These loyalty arrangements shall provide safeguards making explicit the rights of transport users and conference members. These arrangements shall be based on the contract system or any other system which is also lawful.

Another crucial point is that conference members are able to leave a liner conference and become outsiders offering a competing service. Members should give reasonable notice to the other members but the notice period should not have to exceed six months and should be without penalty.

Obligations Attached to the Exemption

Article 5 of Council Regulation 4056/86 constitute a number of obligations that shall be attached to an exemption:

- consultations between transport users and conferences to seek solutions concerning rates, conditions and quality of liner services,
- conference members shall be able to conclude and maintain loyalty arrangements with transport users,
- transport users shall be entitled to approach undertakings of their free choice in respect of inland transport operations and port services not covered by the freight charge or charges on which the shipping line and the transport user have agreed,
- tariffs, related conditions and Regulations of the conferences shall be made available to transport users.

These five obligations form part of the requirements to maintain an exemption once the ship-owners have fulfilled the conditions for obtaining it.

The last two are common, requiring the conferences to exercise certain activities. The first two imply restrictive practices that are exempted from the prohibition in Article 81(1) of the Treaty.[22]

Article 6 states that agreements between transport users and conferences and agreements between transport users, are also block exempted if they concern rates, conditions and quality of liner services as long as they are the subject of consultations and loyal agreements.

Monitoring of Exempted Agreements

The conference block exemption is subject to monitoring. Monitoring is an exercise where observation of an agreement, and the behavior of the parties, can come in question. This aspect of the liner conference Regulation is found in Article 7 of Council Regulation 4056/86.

Monitoring takes place in the following two cases: breach of an obligation and where the effects of an exemption are incompatible with Article 81.3 of the Treaty. Only the latter is of practical importance.

Article 7 gives the Commission the sole power to monitor an exempted agreement. If the practices are found incompatible with the mentioned Article the Commission can take appropriate measures under Article 7.2(c). The gravity of the measures must be in proportion to the gravity of the situation. Certain special circumstances can trigger monitoring, such as:

- acts of conferences whose outcome is absence of actual or potential competition
- acts of conferences which may prevent technical or economical progress
- acts of third countries which prevent the operation of outsiders in a trade or which impose unfair tariffs on conferences.

If these circumstances result in the absence or elimination of actual or potential competition contrary to article 81.3(b) the Commission shall withdraw the exemption.

Abuse of Dominance

[22] Blanco Luis Ortiz, Van Houtte Ben, 1996, p.120

In Article 8 of Council Regulation 4056/86, it is stated that 'the abuse of a dominant position within the meaning of Article 82 shall be prohibited; no prior decision to that effect is required.' When the Commission, either by its own initiative or following a request by a Member State, finds the conduct of a conference benefiting from a block exemption being incompatible with Article 82 it may withdraw the benefits and take other measures to stop the infringement.

The Commission can in this case withdraw the benefit of an exemption and take appropriate measures to bring to an end the infringements of Article 82, however, before taking a decision the Commission may give the, conference concerned, recommendations for termination of the infringement.[23]

Determination of a dominant position, in the maritime sector, depends on many factors including the level of services and not only upon percentages of the trade shared between the conference and the outsiders. Each given trade must be examined and there is no established answer depending only on the percentage.[24]

In order to solve this issue a traditional analysis of the market must be made.

The next step in the analysis is to assess the existence of a dominant position, a work similar to that of assessing other industries, basically relating to market structure, the structure and operation and their conduct on the market.

In relation to market structure, market share and potential competition is very important. A large share is crucial but not necessarily sufficient to examine whether dominance exist. Potential competition, as indicated by the Commission, is effective only when it imposes a direct and certain threat.

Conflicts of International Law

[23] Power Vincent, 1998, p. 338

[24] Anna Bredima-Savopolou, John Tzoannos, 1990, p. 187

Conflicts of international law are conflicts with the laws of third states. The conferences have members from every continent and are therefore also an object to international law and a variety of national laws.

Article 9 of Council Regulation 4056/86 seeks to establish an internal and international institutional procedure to consult and negotiate with third countries. Paragraph 1 provides that where the application of the Regulation to certain restrictive practices or clauses is liable to create a conflict with the provisions laid down by law, Regulation or administrative action of certain third countries the Commission shall consult the relevant authority of this third country, merging its interest with the Community interests.

Two steps exist: the consultation stage and an optional step of negotiation. This procedure has never been used to its full consequence, but the Commission has had contact with the US Federal Maritime Commission.

3.2.2.3 The Rationale for Regulation 4056/86

The rationale for block exemption was the presumption that the liner shipping industry, in contrast to other industries, operates under unique conditions of 'inherent instability'.

Demand is inelastic, but of great variability, and unbalanced on important trade routes. Because liner shipping carries large numbers of relatively small orders, it is infeasible to precise adjust capacity to match demand. In tramp shipping, by contrast, the presence of large (whole shipload) orders means that it is much easier to match demand and capacity.[25]

Also the supply conditions are characterized by high fixed costs. There are large fixed costs over a substantial range of output, including most capital costs, port charges, crew costs, and fuel. These costs are largely a result of scheduled services, which provide regular service regardless of demand in a particular time interval.

Another issue that can cause instability is that shippers benefit from higher frequency of service and greater availability of space. The actions of one liner operator to increase service or space benefit all shippers, not just its own customers. This generates free riding.

These would imply high risk for some operative decisions and for investments. The result could be a collapse of investments and a breakdown of the market on certain routes. To avoid this,

[25] Achim I. Czerny, Kay Mitusch, 2005

conferences are supposed to be necessary pre-conditions for the provision of reliable schedules to shippers.[26]

Since liner conferences were created in the 19th Century, their supporters have maintained that they offer distinct advantages to shippers as regards freight rates and services. As long as ship-owners are concerned, the Regulation gives scheduled ship-owners security as regards the level of freight rates. This enables ship-owners to address the question of the necessary investments to replace old vessels with new, better vessels without having to worry about fluctuating rates.

It also allows continuity of lines in the same traffic for long periods of time, avoiding the numerous and frequent entries to and departures from the market typical of free competition. In this way, they help to prevent the monopoly of a single large liner company or the oligopoly of a few companies, thus maintaining diversity of lines in the traffic and, in particular, helping small companies to survive.

Finally it promotes, through the rationalization of services, a better utilization of ship owners' naval resources, with a reduction in costs that allows, at the same time, more favorable freight rates to be offered to users.

For countries whose ports are covered by conference members, the Regulation offers wider geographical coverage, a reasonable level of freight rates and, as regards the future, allows the creation and maintenance of commercial opportunities with other countries. Some would argue that the promotion of commerce is the second great advantage of the liner conference system (the first being stability).[27]

Reliability

The eighth recital of Regulation 4056/86 states that "liner conferences have a stabilizing effect, assuring shippers of reliable services".

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[26] Nikhil Gupta, p. 88

[27] Reply to the European Commission's Questionnaire on Council Regulation (EEC) Nº 4056/86", Submitted By Luis Ortiz Blanco

According to the Commission, "reliability in the supply of transport services is the maintenance over time of a scheduled service, providing shippers with the guarantee of a service suited to their needs".

Reliability could also be interpreted as a specific quality of services that would consist in the power of conference members to remain in traffic for long periods of time without constantly being obliged to leave and re-enter. This implies that without conferences the presence of ship-owners on maritime routes would be much less permanent. In other words, liner companies would find themselves having to enter and leave traffic constantly without being able to offer any continuity in services. According to this argument, reliability is a consequence of freight rate stability, which would allow conference members to obtain sufficient income to finance their peaceful continued existence in traffic.

Liner freight rates

A common freight rate is one of the fundamental characteristics of liner conferences. The same rate for the same goods, whether the cargo is offered in large or small quantities disregarded of whether or not the vessel is fully loaded or not.71

All members agree, by reference to the agreement, to charge uniform rates.

In order to implement the agreement effectively the members in many cases follow the same rules and Regulations for the calculation of the freight rates, payment of freight, acceptable packaging for different commodities and uniform rates of commission to agents or brokers. Naturally it is up to the lines of the conference to set the level of freight rates on the various categories of commodities that are shipped. The freight rate is, however, not only set on the basis of distance, as there are many factors that can be taken into account when determining the freight rate. These include:

- The value of the goods
- Weight/measurement
- Nature of the cargo, easiness of handling
- Quantities moving to a particular area
- Competitive factors

Conferences have also made it practice to maintain profits by putting surcharges, often called adjustment factors, on existing rates on various grounds that can include: periods of port congestion, where neither ship-owner nor shipper is responsible where the ship is expensively held at the port, currency movements against the ship-owner or maybe sudden and rapid increases in bunker oil price, emergency surcharges and handling surcharges.

The imposition of surcharges is justified, by ship-owners, on the basis that they are temporary and the events giving rise to them are unexpected and swift.

Surcharges are not a fine, neither a remedy to cure inefficient ports, but a means to limit the initial losses of carriers. [28]

Liner conferences have been praised for making it possible to avoid destructive competition. Without them, it is said, price wars would take place in which carriers would enter into a suicidal downward spiral, offering better rates than the competition until every company went bankrupt or abandoned the traffic before this stage were reached. Price wars would not only cause unpredictable freight rates but also – much more seriously - alterations in traffic, since all carriers would depart for more peaceful waters. Nobody would be prepared to operate on routes where price wars could occur.[29]

Regularity

Regularity in liner shipping means that with full geographical coverage cargo of all qualities, attractive/unattractive, easy or difficult to handle, is accepted. A well-coordinated, time-scheduled liner service is one of the aims of conferences. Thus, an agreed share of sailing is one of the elements of conferences.

Scheduling is a difficult matter, and the more ports a vessel calls at the more likely delays become. One frequent way of solving this dilemma is by entering into conference agreements.

Merits of Liner Conferences

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[28] Tunfors Henrik, 2001

[29] Reply to the European Commission's Questionnaire on Council Regulation (EEC) Nº 4056/86", Submitted By Luis Ortiz Blanco"

The members of the conferences claim that conferences, in general, benefit to both customers (shippers), member lines and the trade of served countries. To the gain of shippers are of course the stability of freight rates, services and schedule.

This means that there is no discrimination between shippers served by a conference, an increase in price can only occur after a notification period of two months and that uniform freight rates are set for a wide range of loading and unloading ports.

A shipper is sure that its competitors cannot by shopping around gain lower rates.

The regular service creates confidence for both ship-owners and shippers that business is secure, and in addition conferences provide broader geographical coverage than individual lines, as well as a variety of ships with flexibility and ability to provide vessels of fitting size and speed capable of meeting the requirements of the trade.

The conferences furthermore claim that the elimination of competition between members lead to service competition, updated equipment of cargo handling and office organization, but also that the conferences, aware that shippers are loyal, dare to make necessary investments.

Moreover, from a competition point of view, weaker lines, which might be eliminated in a free competition regime, survive under the wings of conferences.[30]

6.2.2.4 Regulation 4057/86

The third Regulation (4057/86) contained in the 1986 legislative package, on unfair pricing practices in maritime transport, provides for Member States to impose redressive duties on individual third country ship-owners which, due to non-commercial advantages or incentives granted by their home state, are able to offer very low freight rates in an attempt to win market share. This Regulation was invoked in 1989 when the Council took action against the Korean firm Hyundai Merchant Marine, but has not been used since. The Commission believes that it forms a useful deterrent against anticompetitive behavior. However, it has also identified a number of drawbacks.[31]

Firstly, it can also protect shipping companies which the Community has no interest in protecting. This is because the Regulation defines a Community ship-owner as a company

[30] Tunfors Henrik, 2001

[31] Lyons Paul K., 2000, p. 58-59

established in the EC. It does not, therefore, require any substantial link with economic involvement in Community industry, such as EC employment, investment, or flag. From this, it follows that attempts may be made to circumvent the Regulation by establishing a company in a Member State.

Secondly, in the context of globalization and the increasing sophistication and capital intensity of liner shipping, it is questionable whether a liner shipping operator, even if government-sponsored, would now risk an aggressive entry into one trade by heavy underbidding. The pattern of entry into markets observed in the last few years is one of cooperation through vessel sharing agreements. One could therefore argue that Regulation 4057/86 in its present concept is outdated, at least for the larger liner trades.[32]

6.2.2.5 Regulation 4058/86

This Regulation applies when action by a non-Community country or by its agents restricts free access to the transport of liner cargoes, bulk cargoes or other cargoes by shipping companies of Member States or by ships registered in a Member State, except where such action is taken in conformity with the UN Liner Code.

It provides for coordinated action by the Community following a request made by a Member State to the Commission. Such action might include diplomatic representation to non-Community countries and countermeasures directed at the shipping companies concerned. Similar coordinated action can be taken at the request of another country belonging to the Organization for Economic Cooperation and Development (OECD) with which a reciprocal arrangement has been concluded.[33]

The reason why Regulation 4058/86 was adopted is the observed increase in the number of countries resorting to the protection of their merchant fleets through practices which distorted the application of the principle of fair and free competition in shipping trade with EU Member States.[34]

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[32] Commission of the European Communities, 1996, COM(96)81

[33] European Sea Ports Organisation – ESPO, 2004, p. 61

[34] DG Transport, 1999, p. 181

6.2.2.6 The Exclusion of Maritime Transport of Cabotage

The Regulation is based on the premise that the exclusion from its scope of cabotage traffic and traffic between third countries is of no great practical importance, since such restrictions of competition hardly ever come within the scope of the Community competition rules.

This original reasoning is very similar to that which led to the exclusion of tramp services from the scope of the Regulation, and only half disguises what is, effectively, a political imposition by certain Member States who are reluctant to allow the Commission to meddle in their "internal affairs".

In any event, the presumption seems to have little foundation as regards cabotage since there are cases in which trade between Member States may be affected. In certain circumstances, restrictions on competition in cabotage services for the transshipment of goods destined for another country, Member State or otherwise, and ferry services within the same country, but which are a compulsory stage on a longer voyage within the Community, could affect intra-Community trade.[35]

6.2.2.7 The Exclusion of Tramp Services

Regulation 4056/86, according to its Article 1(2), applies to all kinds of maritime transport services, including passenger services, with the exception of tramp vessel services, which are strictly defined in Article 1(3)(a) as follows: the transport of goods in bulk in a vessel chartered wholly or partly to one or more shippers on the basis of a voyage or time charter or any other form of contract for non-regularly scheduled or non-advertised sailings where the freight rates are freely negotiated case by case in accordance with the conditions of supply and demand.

The first draft Regulation referred to, and excluded, "bulk transportation" or "bulk transports" (in Article 1(2)). It did not refer to "tramp vessel services"; this term was introduced in the second amended draft. Finally "tramp vessel services" were defined as a wider concept than "bulk transport".

General cargo transport undertaken by tramp vessels is excluded from the Regulation, whereas bulk transport, if carried out by liner vessels, is included.

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[35] Reply to the European Commission's Questionnaire on Council Regulation (EEC) Nº 4056/86", Submitted By Luis Ortiz Blanco

The reasons, for excluding tramping from the Regulation's scope, are that it is unnecessary for the Community to apply competition laws given the competitive nature of that sector of the maritime industry. The reasons for the exclusion are political rather than technical and legal: if the exclusion of cabotage was imposed by the southern States as a whole, the exclusion of tramping was probably due to pressure from Greece, which specialized in bulk tramp services, and at that time was the leading Community merchant fleet in terms of tonnage and the only Member State which from the outset supported the Commission in the negotiations which led to the adoption of Regulation 4056/86 by the Council.

From the standpoint of competition policy, there is no reason to leave tramping outside the scope of sufficiently effective procedural rules. [36]

6.2.3 Regulation 3577/92

In the maritime sector, provisions which would allow the market to function were initially included in the first drafts of Council Regulation 4055/86 on the freedom to provide (international) maritime services. In 1986, the Council adopted this Regulation. However, at the final moment, maritime cabotage services were removed from the directive because of economical and political issues. The reason for the difficulties arose from the differences in the cultures regarding cabotage in each of the Member States. The UK and Denmark and, to an extent, Germany, Belgium and the Netherlands had totally open cabotage regimes, with all vessels under all flags having access. This was in contrast to the position of the Mediterranean Member States.

Prior to the adoption of Regulation 4055/86, it was clear that Member States were polarized into two opposing camps. One side wanted a totally open policy, the other wanted full control with internal maritime transports in national waters. In particular the inter-island services in the territories of Spain, Portugal, France, Italy and Greece were regarded as sensitive both from a strategic and social point of view.

Whilst cabotage provisions were excluded from Regulation 4055/86, the Council asked the Commission to produce a proposal for a separate Regulation concerning the liberalization of maritime transport in EU.

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[36] Reply to the European Commission's Questionnaire on Council Regulation (EEC) Nº 4056/86", Submitted By Luis Ortiz Blanco

In general, liberalization involves the exposure of the transport market to laissez-faire, or free market, achieved through the removal of most regulatory controls over pricing, while permitting carriers to enter and leave the markets at will.

Council Regulation 3577/92, of 7th December 1992, applied the principle of freedom to provide services to maritime transport within Members States (maritime cabotage). The Regulation grants freedom to provide maritime transport services within a Member State for Community ship-owners operating ships registered in a Member State and flying the flag of a Member State.

Article 1 of the Regulation stipulates who the beneficiaries are of the freedom to provide maritime cabotage services. They are Community ship-owners who have their ships registered in a Member State and flying the flag of that Member State, provided that they comply with the conditions for carrying out cabotage in that Member State.

Article 2(2) of the Regulation distinguishes three types of Community shipowner.
"(a) nationals of a Member State established in a Member State in accordance with the legislation of that Member State and pursuing shipping activities
(b) shipping companies established in accordance with the legislation of a Member State and whose principal place of business is situated, and effective control exercised, in a Member State or
(c) nationals of a Member State established outside the Community or shipping companies established outside the Community and controlled by nationals of a Member State, if their ships are registered in and fly the flag of a Member State in accordance with its legislation."
A substantial article of the Regulation deals with the right that Member States have to provide transport services subject to public service obligations (PSO) in the interest of maintaining adequate cabotage services between the mainland and its islands and between the islands themselves. Under European Commission guidelines, a PSO in ferry services may only be declared to provide services needed to address problems of insularity or economic disadvantage that would not normally be addressed without public intervention. The definition of a PSO is set out as: “any obligation imposed upon a carrier to ensure the provision of a

service satisfying fixed standards of continuity, regularity, capacity and pricing, which standards the carrier would not assume if it were solely considering its economic interest".[37]

Safeguard measures may be taken by the Commission where the internal market would seriously be disrupted by the liberalization of cabotage or where countries whose domestic island ferry cabotage rules and contracting procedures are in violation of Council Regulation 3577/92. In the case of France, Italy, Greece, Portugal and Spain mainland cabotage was gradually liberalized according to a specific timetable for each type of transport service. Mainland-island and inter-island cabotage for these countries was liberalized in 1996.

Article 7 of the Regulation, prohibits Member States from introducing restrictions on the freedom to provide services which did not exist before the Regulation entered into force.

6.2.4 Regulation 823/2000

Consortia, a different type of organization of liner firms from the traditional liner conferences was not clear following the passage of the 1986 Maritime Package. After six years of consideration, the EU Council approved a Regulation relating to consortia on February 25, 1992 (Regulation 479/92). As seen above, the conferences are exempted from the competition rules (Regulation No. 4056/86), but consortia were in a sense at risk because they were different from conferences. The 1992 Regulation gives to consortia in the European liner trades a group exemption from EU competition law also.

The Council set a period of validity of 5 years for the block exemption. After this period, the block exemption could be, if appropriate, renewed.

In 1995 the Commission made use of these powers by adopting Commission Regulation No 870/95 of 20 April 19956 and subsequently decided to renew the block exemption for a further period of five years through the adoption of Regulation No 823/2000.

Commission Regulation No 823/2000 provides a block exemption in relation to consortium agreements in maritime transport. A consortium is defined as a joint service provided by two or more shipping lines. Its main features are sharing of space and the determination of port calls and schedules.

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[37] C. I. Chlomoudis, P. L. Pallis, S. Papadimitriou, E. S. Tzannatos, 2007

The objective of a consortium agreement between two or more vessel operating companies is to enter into operational and technical co-operation so as to provide a joint liner service.

Consortium agreements generally help to improve the productivity and quality of available liner shipping services of member lines through the economies of scale they allow in the operation of vessels and utilization of port facilities. Users of the shipping services provided by consortia generally obtain a fair share of the benefits resulting from the improvements in productivity and service quality which they bring about, if there is sufficient competition in the trades in which the consortia operate.

Liner conferences do not involve any operational co-operation between shipping lines. The only co-operation concerns price fixing. Today, shipping lines co-operate operationally through consortia agreements. To ensure that supply meets demand, co-operation is only required with regard to the supply of vessels. Slot charter and space sharing agreements minimize the investment risks of ship owners.

As indicated above, Regulation 823/2000 does not exempt joint price fixing amongst consortium members. This is explicitly stated in recital 9 and in Article 2 (1) of Regulation 823/2000.

In addition the Regulation applies to international liner shipping services for the carriage of cargo, mainly by container (Article 2(1)). As set out in Article 1 of Regulation 823/2000, this includes services to and from a port in the European Union but excludes services within the same Member State, i.e. maritime cabotage.

The requirement that the service involves the carriage of cargo chiefly by container, as set out in the aforementioned Article, excludes the application of Regulation 823/2000 to passenger and to tramp vessel services.

With regard to the geographic scope, the definition in Article 2(1) refers to a consortium operating on one or more trades. A consortium can therefore operate a joint service on a single or several different trades (e.g. a global alliance).

Article 4 of Regulation 823/2000 prohibits consortium members to carry out or include provisions in their agreements relating to the non-utilization of existing capacity, notably by refraining from using a certain percentage of the capacity of vessels operated within the

consortium. The prohibition refers to a restriction for the purpose of raising prices, a serious violation of competition rules sanctioned by Article 81 of the Treaty.

As long as the market share thresholds are concerned Article 6 of Regulation 823/2000 currently defines two market share thresholds for the application of the block exemption: a market share threshold of 35% for consortia operating outside a liner conference and 30% for those operating within a conference.

However, even if a consortium is above the 30% market share threshold, that does not automatically mean that such consortium is illegal, but that the member of the consortium need to self assess if their cooperation restricts competition and if so, satisfies the conditions of Article 81 (3) of the Treaty.

Regulation 823/2000 is of particular significance from a trade perspective as containerized liner shipping accounts for approximately 20% of EU external trade in value terms. Due to the very high level of investment and the fixed schedules required to set up a service – it takes on average 6 similar sized container ships to set up a liner shipping service – a significant part of the liner container services is offered by groups of shipping lines organized in consortia.

Consortia have become the preferred operating structure for carriers who operate on a global level, providing many commercial advantages (service coverage and frequency) and financial advantages (scale of economies) to carriers. Now, little more than half the capacity of the top 20 lines is operated by alliance members.

7. Modernization of Maritime Competition Policy

7.1 Need for a Change

Maritime transport services are the key to the development of the EU economy. It is paramount that the rules applying to the sector reflect today's market conditions. So the existing impediments for EU business to compete, innovate and grow should be removed. Legislation needs to be simplified and to be cost effective.

The Commission is presently consulting widely on a new comprehensive maritime policy aimed at developing a thriving maritime economy.

7.2 Regulation 1/2003

Regulation 4056/86 was the implementing Regulation for Articles 81 and 82 of the EC Treaty ('Articles 81 and 82') in relation to maritime transport. In other words, it lays down the detailed rules for the application of those articles to maritime transport, in respect of which Council Regulation 17/62 did not apply. For the Commission, the effect of this lacuna was that it had very limited enforcement powers in those areas.[38]

The new implementing Regulation for Articles 81 and 82 was Council Regulation 1/2003, which entered into force on 1 May 2004. With that, the implementing measures in Regulation 17/62 as well as Regulation 4056/86 were repealed and maritime transport was brought under the common competition enforcement rules.

Regulation No. 17 was based on direct effect of the prohibition rule of Article 81(1) and Article 82. Article 1 of Regulation No. 17 therefore stipulated that agreements, decisions and concerted practices of the kind described in Article 81(1) EC-Treaty and the abuse of a dominant position in the market, within the meaning of Article 82 EC-Treaty, shall be prohibited. Also, Regulation No. 17 rested on prior notification to the Commission of restrictive agreements and practices for exemption under Article 81(3) EC-Treaty.[39]

The reform eliminated the notification and exemption system and replaced it by a system of direct application of the law, which can be enforced not only by the Commission but also by the national competition authorities and by national courts. This means that an agreement which fulfils the conditions of the exemption rule contained in the Treaty is legal from the outset.

Article 81(3) of the Treaty can be invoked as a defense in all proceedings, including before national courts and national competition authorities without the need for an administrative intervention by the Commission. It is no longer necessary or indeed possible to obtain an individual exemption under Community law either from the Commission or from Member States.

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[38] Niels C. Ersbøll, 2005, The European Antitrust Review 2005, p. 95-98

[39] Felix Müller, German Law Journal, vol. 5, No. 6, p. 721-740

Conversely, just as was the case before the entry into application of Regulation 1/2003, a restrictive agreement which does not fulfill the conditions of the exemption rule under Article 81(3) of the Treaty will be void and unenforceable from the beginning. Undertakings are now in the obligation to self-assess their business practices to determine whether they comply with competition law.

Block exemptions Regulations were also maintained as a means to provide greater legal certainty. Regulation 1/2003 did not introduce any substantive changes to Regulation 4056/86 containing the liner conference block exemption. As a result, tramp vessel services and cabotage services continued to be specifically excluded from the scope of application of the rules implementing Articles 81 and 82 EC Treaty. Regulation 1/2003 replaced Regulation 17/62 as well as the provisions on procedures and sanctions contained in Regulation 4056/86. This means that for the first time in the EU the same procedural rules apply to all causes, whether transport-related or not.

Under the new Regulation, businesses will no longer need to incur the cost of notification to benefit from an exemption. This will be highly beneficial for those agreements that are clearly lawful, but greater care will be needed in self-assessment by businesses, the closer their agreements come to the scope of the prohibition in Article 81(1). In some such cases the costs of legal advice may reach the level of notification costs. However, in particularly difficult cases businesses will be able to avoid excessive legal costs by being able to request a written opinion from the Commission to clarify the status of their agreement.

Also the fact that a common competition standard for business co-operation across Europe was adopted encourages further market integration, enhancing the ability of businesses to enter new markets and encouraging investments.

Finally, the new Council Regulation establishes a new mechanism of cooperation between the Commission and the competition authorities of the Member States.

However, the specific substantive competition provisions relating to the maritime sector continue to fall within the scope of Regulation No 4056/86.

7.3 Regulation 463/2004

Consortia agreements, as a form of cooperation, are already open to providers of international liner services under the consortia block exemption Regulation (Regulation 823/2000). In 12 March 2004 Regulation 823/2000 was amended by Regulation 462/2004.

The changes made to Regulation 823/2000 in 2004 were mainly procedural. They were adopted to bring Regulation 823/2000 into line with last year's general reform of EC competition law that sought to decentralize a significant amount of competition law enforcement from the Commission level to the Member States.[40]

For example, as of 1 May 2004 (Regulation 1/2003), competition authorities in Member States were accorded the same powers as the Commission with regard to withdrawal of the benefit of the block exemption in individual cases where an agreement, although exempted through Regulation 823/2000 from the Article 81(1) EC prohibition, nevertheless has effects incompatible with Article 81(3) EC in the territory of the Member State.

The system of notifications of consortia to the Commission for clearance was also abolished. The new system requires the companies concerned to assess for themselves whether a consortium agreement falls within the scope of Regulation 823/2000. Notwithstanding the amendments made in 2004, in 2005, the Commission introduced some further minor amendments in order to make Regulation 823/2000 more suitable for its purpose, following concerns that, in some respects, the provisions of Regulation 823/3000 were not sufficiently attuned to current practice in the industry.

Regardless of the procedural amendments, Regulation 823/2000 remains largely intact as the Commission remains of the view that the benefits of consortia are still valid. Consortia generally help to improve the productivity and quality of available liner shipping services because of the rationalization they bring to the activities of member companies and through the economies of scale they allow in the operation of vessels and utilization of port facilities.

Also the Consortia help to promote technical and economic progress by facilitating and encouraging greater utilization of containers and by using vessel capacity more efficiently. Consequently, consortia will remain a safe haven for liner shippers for the foreseeable future,

[40] Watson, Farley & Williams, 2007, p. 26-29

provided they meet the criteria as set out in the Regulation. Customers (i.e. transport users) also generally view the consortia block exemption positively.

Consortia is considered as the most acceptable and preferable form of cooperation between ship-owners, emphasizing that industries have increased efficiency and improved quality of services to their customers through certain forms of cooperation, which do not include price fixing. Users of the shipping services offered by consortia can obtain a share of the benefits resulting from the improvements in productivity and service, by means of cost reduction derived from high levels of capacity utilization and better service quality, stemming from improved vessels and equipment.

7.4 New Era in Maritime Competition Policy – Regulation 1419/2006

The liner shipping market has changed considerably since Regulation 4056/86 was adopted. The continuing trend towards containerization has led to an increase in the number and size of fully-cellular container vessels and to an emphasis on global route networks.[41] This has contributed to the popularity of consortia and alliances as a means of sharing costs. The growth in importance of these operational arrangements has been accompanied by a decline in the significance of conferences.

Transport users, who seek customer-focused relationships with carriers, have systematically questioned the conference system which they consider does not deliver adequate, efficient and reliable services suited to their needs. So they call for the abolition of conferences.
Other jurisdictions and international organisations have also questioned the benefits of maintaining the conference system.
Defenders of liner conferences have always claimed that the liner market is unique and thus required special treatment under competition law. An examination of the market shows this is no longer so today: in the twenty years that the Regulation has been in force the liner shipping market has changed considerably**.**

The liner shipping industry is not unique in the sense that its cost structure does not differ substantially from that of other transport industries and shipping lines do not suffer from exceptionally low returns on investment when compared to other scheduled transport

[41] Ministry of Competitiveness and Communications , 2007, COM(2006)869

providers. There is therefore no evidence that the industry needs to be protected from competition by anti-trust immunity for price-fixing and rate discussions.

The continuing trend towards containerization has led to an increase in the number and size of container vessels and to an emphasis on speed, frequency of service and global route networks. This has contributed to the popularity of consortia and alliances as a means of sharing the cost of the investments required to provide a competitive liner shipping service. The growth in importance of these operational arrangements, which do not involve price-fixing, has been accompanied by a decline in the significance of conferences

These developments raised the question of whether reliable scheduled maritime transport services can be achieved by less restrictive means than horizontal price-fixing and capacity limitation. This in itself would be sufficient to justify a review of the EU liner conference block exemption.

Against this background the Commission launched a review of Regulation 4056/86.

This review concluded in the adoption of a new Council Regulation, 1419/2006 which was published on 25 September 2006 and came into force on 18 October 2006. However it had a two year transitional period which means that the repeal did not become effective until October 2008.

The two key changes introduced by the Regulation are:[42]

- Regulation 4056/86 is repealed in its entirety, including the liner conference block exemption and
- Regulation 1/2003 is amended to bring cabotage and tramp vessel services under the scope of the common competition implementing rules.

7.4.1 Repeal of Regulation 4056/86

Exemptions from competition rules are normally reviewed by the Commission every few years to ensure that they continue to fulfill the four cumulative conditions of Article 81.3 EC. Regulation 4056/86 had never been revisited. This until March 2003, when the Commission initiated an extensive review of Regulation 4056/86 to ascertain whether the block exemption

[42] Watson, Farley & Williams, 2007, p. 10-12

delivered the benefits for which it was first established and to determine the best way to apply competition rules to liner transport services in today's market conditions.

7.4.1.1 Review of Regulation 4056/86

Recital 8 of Regulation 4056/86 refers to the assumption that liner conferences have a stabilizing effect assuring shippers of reliable services and that such results cannot be obtained without joint price fixing and capacity regulation.

To fulfill the first condition of Article 81(3) of the Treaty, it must be established that economic benefits flow from the price fixing and capacity regulation by conferences.

Price stability has been defined as "the maintenance of freight rates at a more or less constant level by liner conferences". It is questionable however if price stability as such would be regarded as sufficient for the fulfillment of the first condition of Article 81(3). Price stability only becomes relevant if it is read in conjunction with the concept of "reliable services" meaning "the maintenance over time of a scheduled service, providing shippers with the guarantee of a service suited to their needs".

Data put forward during the review process did not show that actual freight rates have been stable or that conferences have contributed to rate stability, i.e. with or without conferences there is price volatility. It was found that with conferences the source of price volatility comes from the structural instability of market participation and conference membership. This can be a fundamental problem, since market entry and exit can be associated with transaction and investment costs. In contrast, without conferences price volatility will continue.

Carriers consider the reliability of service as the main benefit that derives from conferences.

However, in today's market, conferences are not able to enforce the conference tariff and do not manage the capacity that is made available on the market. The majority of cargo is carried under confidential individual agreements between carriers and transport users ("contract cargo") rather than under the conference tariff. The proportion of contract cargo is very high ranging from 90% and above in the transatlantic trade to 75% in the Europe to Australian trade. The same occurs in the Europe to Far East trades. Regarding capacity regulation, this is a decision that is taken by individual lines or by consortia. Thus, it is difficult to claim that the provision of reliable services results directly from conference price fixing and capacity regulation. Therefore the first condition of Article 81 (3) is not satisfied.

The second condition of Article 81(3) of the Treaty requires that, if liner conferences were to achieve economic benefits, a fair share of these benefits should be passed on to consumers. In the case of a hard-core restriction of competition such as horizontal price fixing the negative effects are very serious and the benefits have to be very clear cut. However, no clear positive effects have been identified in the review process. Transport users have systematically opposed the conference system which they consider that it does not deliver adequate, efficient and reliable services suited to their needs. They call for the abolition of conferences and consider the existing consortia block exemption to provide an adequate framework for co-operation among liner shipping carriers. It should be noted that although the conference tariff is no longer enforced it may act as a benchmark for the setting of individual contracts. This results in a reduction of shippers' negotiating power.

The second condition is therefore not fulfilled.

Under the third condition of Article 81(3) of the Treaty, the test is basically whether there are less restrictive alternatives than conference price fixing which would assure reliable liner services to the benefit of consumers. Today, scheduled liner services are provided in several ways. Independent carriers operate outside conferences on all main trades to and from Europe. Co-operation arrangements between liner shipping lines not involving price fixing, such as consortia and alliances, have increased and have important shares of the market in all major trades. Under certain conditions, consortia are block exempted from the prohibition set out in Article 81(1) of the Treaty by Commission Regulation (EC) No 823/200 on account of the rationalization they bring to the activities of member companies and the economies of scale they allow in the operation of vessels and port facilities.

Moreover, confidential individual service contracts between individual carriers and individual shippers account for the majority of cargo transported. Finally it should be noted that in some trades, conferences do not exist and this has not affected the regularity of the services. The restrictions permitted under Regulation 4056/86 (price fixing and capacity regulation) are therefore not indispensable for the provision of reliable shipping services. The third condition is therefore also not fulfilled.

Finally, the fourth condition of Article 81(3) of the Treaty requires that competition should not be eliminated on a substantial part of the market. Conferences operate alongside consortia, alliances and independent operators. It would appear therefore that the fourth condition of

Article 81(3) of the Treaty may be fulfilled. However, since the four conditions of Article 81(3) of the Treaty are cumulative and the first three conditions are not fulfilled for the reasons explained above, the question whether or not the fourth condition is fulfilled could be left open.

This said, carriers are likely to be members of a conference on a trade and outsiders in another. They may also be members of conferences and of consortia or alliances on the same market thus cumulating the benefits of the two block exemptions. In all cases, they exchange commercially sensitive information with their competitors that may allow them to adapt their conduct on the market.

In addition for charges and surcharges there is clearly no price competition between conference and non-conference carriers.

In conclusion, the four cumulative conditions of Article 81(3) of the Treaty that would justify an exemption are not fulfilled by conferences in present day market circumstances.

Also the review brought in light that experience from other recently liberalized transport sectors shows that service quality and innovation are likely to be improved. Since four out of the top five world-wide liner shipping carriers are European, a more competitive environment should allow EU liner shipping carriers to compete, even more successfully, and grow.

Liberalization gives smaller EU carriers the opportunity to grow fast if they follow an innovative business model. The success of small carriers depends on their ability to adapt to a competitive environment and not on their actual size.[43]

It should be noted that conference members come from all over the world. Liner conferences serving EU trades contain EU liner shipping carriers as well as carriers from third countries. EU carriers are also conference members on non-EU trades. As stated above EU carriers have a strong position on all world trades not only on EU trades. Therefore the competitiveness of EU carriers relative to non-EU carriers would not, in principle, be altered by the removal of the exemption.

[43] Statement by Fabrizia Benini, 2006

7.4.1.2 Rationale of the Repeal

One of the principal risks associated with conferences is that competition between them is limited simply to the quality of services. Companies that operate on a given route therefore become involved in a race to operate ever bigger vessels with ever greater capacity.

In economic theory, it is a well-known fact that through price fixing agreements conferences can create useless overcapacity among competitors and lead to waste.

Stability

Supporters of the stabilizing nature of conferences remain silent about one of the principle reasons for instability in freight rates in scheduled liner transport: discrimination between goods established by conferences.

Principally through agreements on freight rates, the liner conference system tries to avoid a type of instability that is normal in other forms of liner transport. In doing so, liner conferences not only establish common or uniform freight rates, but also (because they need not do so to achieve stability) rates that are discriminatory as regards the type of goods. Although at first sight it appears unnecessary to guarantee freight rate stability, discrimination in tariffs has become a fundamental part of liner conferences' strategy. Liner conferences try hard to eradicate the normal fluctuations of the market but at the same time they favor another new form of instability with their tariff structure.

If the aim is to promote stability, it appears obvious that tariffs that do not discriminate between different types of cargo would achieve this aim much better, since neither the independents nor the ship-owner conference members would fight to obtain the most valuable cargo.

Since stability is the only advantage recognized by Regulation 4056/86, if stability in freight rates is lost conferences will stop producing the main advantage that justifies their existence, according to the interpretation of Article 81(3) of the Treaty contained in the Regulation. Thus, if liner conferences do not exercise their much praised stabilizing function the justification for their privileged position disappears.

In conclusion, it appears that stability is not as advantageous as the supporters of liner conferences argue, and in any event liner conferences do not provide the stability that they

claim to. Shippers do not enjoy either fixed prices or predictable costs. Therefore, the block exemption should be withdrawn.

Fixing of Freight Rates

The principal restriction caused by conferences is the fixing in common of freight rates that are uniformly applicable to different types of cargo. However, this restriction does not appear to be indispensable. There are two main reasons for this. First, the behavior of conference members themselves shows that they can do without this restriction on competition without any apparent negative effect on stability: on the one hand, ship-owners sometimes operate in traffic as conference members and at other times as independents and on the other, it is very common for conference members not to respect freight rates negotiated with other members. Secondly, less restrictive alternatives exist (including some put into practice by conferences themselves) for the attainment of the same objectives that conferences claim to pursue, in particular freight rate stability.

Price Wars

As it has been mentioned in the absence of conferences price wars would take place.

However, price wars can be seen from another angle, either as the natural consequence of the existence of conferences or as instruments at the service of the monopolizing tendencies of these cartels.

The liner conference system is, in fact, the perfect breeding ground for price wars.

Independents have absolutely no interest in triggering a price war, which they are much more likely to lose than the unified conference members, who they confront individually (regardless of whether there are one or more independents in the traffic). Logically, they prefer to continue operating comfortably under the protective umbrella of the conference tariff (the higher the umbrella the better).

There are two reasons for liner conferences starting a price war.

First, the independent may abandon the traffic after a period of time, unable to cope with the conference's price cuts.

Secondly, the independent may become associated with the conference (either as a full member or as a tolerated outsider) on reasonable terms. This means lower market shares but higher profits, due to the general increase in tariffs to levels equal to or higher than those existing prior to the price war. In conclusion, liner conferences may effectively exist to prevent what they themselves cause.

Reliability

Reliability was appeared to be a great benefit that ship-owners obtain from conferences. However from an economic standpoint, and from the shippers' point of view, the reliability of a given ship-owner is not the important question. The crucial factor is the permanent existence of a sufficient number of viable and competitive transport options in any given traffic, independently of how long individual ship-owners survive. As long as there are ship-owners prepared to substitute those that leave the market - and it appears that there will never be a shortage of those willing to join the market, even without liner conferences - the fact that the "names" change (even those that have always existed) should not worry anyone apart from those that disappear.

Quality of Service

As regards the quality of service there is no evidence at all that conferences aid the establishment or improvement of scheduled maritime transport services. Similarly, there is no evidence that the market share-out within a conference allows its members to offer their services at an optimum level or to rationalize their own sailing programs. Economic losses caused by such a situation will always be passed on in the form of higher freight rates.

The number of ports used by a conference tends to be less than the number that individual conference members would use if the conference did not exist. This is particularly true following containerization, which has led ship-owners to serve increasingly fewer ports directly and to use feeder[44] services as a means of serving ports outside the principal route. Independently of whether this practice makes sense in economic turns, the truth is that containerization has limited and concentrated the supply of direct services. It is impossible to

[44] Feeder ship: a term for small to medium container ships which provide the collecting and distribution of containers from/to smaller ports to/from the big hub-ports connected to the worldwide container lines.

know precisely what would have occurred if containerization had not been added to the phenomenon of conferences, or vice versa.

Had more rigorous competition existed perhaps liner companies would have competed by offering more numerous direct services and the number of "principal" ports would be much greater than it is today. In the European Union, for example, there are peripheral areas where direct services, which always benefit users in terms of the lack of surcharges and lower transit time, have disappeared.

If conferences had not existed, it is probable that a large number of direct services would have been maintained and perhaps vessels would not have become as large as they are today.

Another issue that is raised concerning the quality of services is that conferences are market leaders. Their policies on tariffs, surcharges and services are imitated (with or without concerted practices) by independents. As a result, where independents exist, the alternatives that they offer differ little from those offered by conferences, which in practice means that there are fewer alternatives on the market for shippers.

Economic Efficiency

There is no evidence that the supposed reduction in costs is greater than the increase in costs caused by (for shippers, but also for liner companies) the existence of conferences.

The feeling of security that conferences give their members in fact causes an increase in costs, the opposite effect to that suggested by conferences.

Conference members only compete amongst themselves as regards the quality of the service, in order to win market shares, principally from other conference members. Given the lack of freight rate competition, this type of competition can cause members to spend excessively on improving service quality, at a much higher level than is needed by shippers. As a result the costs incurred by conference members in competing in this way inevitably result in higher freight rates.

- the maintenance of all conference ship-owners in traffic, regardless of their competitiveness and their individual economic viability on a competitive market, results first in an excess of tonnage in traffic that must be paid by shippers and secondly as a consequence an effect regarding freight rates. This is because rates must be fixed at a level that covers the costs of

the most inefficient conference member, without which this member would cease to exist. This is precisely what conferences aim to avoid, so the conclusion must be that the most inefficient conference members effectively dictate the level of freight rates.

In general, conferences have weakened rather than strengthened liner companies, since they have become less competitive. Instead of trying to expand their business, ship-owners have been content either to maintain their quotas within conferences or to buy competing ship-owners thus taking over their share of the market. Proof of this is that conferences have maintained almost the same members, (although with different brand names or labels) for long periods of time, with very few changes to the way they were originally established.

Technical Efficiency

The idea that liner conferences promote technical efficiency also requires closer analysis. It is believed that the liner conference system prevents the most efficient conference members from increasing their market share by taking business away from inefficient members.[45] If this were possible, efficient members would be able to reduce their costs and increase efficiency even more.

Further, if conferences are successful in achieving the type of insulation from competition that they seek this inevitably leads to inefficiency. In stating that efficient operation requires control of capacity or control of entrants and that the exclusion is necessary for efficient operation, supporters of liner conferences forget that such insulation may simply lead to inefficient results.

The incapacity to innovate and reduce costs may be a consequence of a lifeless liner conference market that is dominated by liner conferences.

Liner Market Structure

In general, the degree of concentration on liner markets is always very high. First, very few shipowners control the vast majority of transport capacity through containers in the world: approximately twenty of them control more than 72% of the total, and the five largest hold 34%. As if this were not enough, on all of the routes there is always, naturally, a limited

[45] Rochdale Report, 1970

number of operators, higher or lower according to the length of the route, the maximum economic size that is viable for vessels used in service and, logically, the intensity of trade between the countries connected by the ports at either end.

The existence of conferences on a market where the number of operators is limited has two effects. First, as with any price cartel, it creates an artificial tariff umbrella that protects less efficient operators, and avoids them having to abandon the market (which would produce an even greater concentration). Secondly, and even more importantly, it would cause "follow-the leader" policies, due to the oligopolistic nature of the market being cartelized. This is precisely what explains historically the success of conferences: the fewer the number of operators that remain outside a cartel, the more stable the cartel.

The attempts to cartelize the markets where tramp vessels operated failed, precisely because of the excessive number of carriers offering such services.

Whatever the exact structure of the market is, conferences, by themselves (given their own market share) or with the help of the .structural approach of the independents, hold the necessary power to control the market. If they did not have the market power needed to be price leaders (that is, if they were not capable of making the independents follow their pricing decisions), they would disappear, since instead of being useful, they would become a problem for their members.

As a result, in one way or another, conferences systematically establish a collective dominant position.

Entry Barriers

At first sight, the clearest indicator that barriers to entry exist on the scheduled liner market is that liner conferences are able to raise their freight rates above the competitive level and discriminate against certain types of cargo. In this way, they obtain the highest possible level of income from each shipper.

If this barrier did not exist, the easy and rapid entry of competitors would bring to an end supra-competitive rates and discrimination against certain goods. When rates go up and remain above the competitive level, without any new entries onto the market taking place, it must be concluded that the barriers to entry onto the market are substantial and prevent effective potential competition.

Other barriers that discourage entry are the systematic existence of excess capacity on shipping lines, the capacity of conferences to unleash price wars, the use of predatory practices to deal with the entry of a significant independent competitor, and the legal possibility that conferences carry out practices directed at ensuring the loyalty of clients. In reality, the existence of conferences represents a barrier to entry.

As regards exit barriers, it is generally recognized that these are even higher than entry barriers. The Commission has also pointed out the difficulties of abandoning a given route without suffering enormous losses, not only in financial terms but also as regards commercial reputation.

In conclusion, liner conferences do not appear to produce sufficient improvements or advantages to compensate for the much greater damage that they do as regards competition, nor do they benefit more than they prejudice scheduled maritime transport users.[46]

7.4.1.3 Impact of the Repeal

Lower prices

Evidence available from other liberalized markets suggests that prices will decline. The introduction of competition for both international telephone calls and European economy airfares caused average prices to fall by more than half within the decade as national monopolies or dominant firms became subject to greater competition.

The removal of the block exemption could increase the efficiency of carriers and this will result in lower prices for shippers. This is a view backed by the European Shipping Council (ESC), which represents European shippers.

In addition, it is believed that the buyer power of large shipping line customers mean that shipping companies will compete on price in large sections of the market. This suggests smaller customers may enjoy a greater share of the benefits of this deregulation.

Lower price volatility

In 2005 ICF consulting[47] were asked to look at the liner industry by the European Commission. ICF examined the effect on price volatility in other liberalized markets and concluded that in

[46] Reply to the European Commission's Questionnaire on Council Regulation (EEC) Nº 4056/86", Submitted By Luis Ortiz Blanco

the long term prices will be less volatile than at present. There may, however, be some increase in price volatility in the short term as a new market equilibrium is reached. There is little evidence to support an argument that conferences have moderated the volatility of freight rates. Removal of the block exemption may increase price stability.

However, there is a risk that price volatility may get worse on the smaller trade routes, particularly in the short term.

The airline industry has similar characteristics to liner shipping with high fixed costs, trade imbalances and seasonal fluctuations in demand. The ICF study examined the price fluctuation in air travel and found that rates had been relatively stable over the past decade. The study also examined US rail freight rates as this industry is also characterized by high fixed costs and found that prices had been stable over the past decade. Past experience from these industries suggests that price volatility in the liner industry will be reduced if the market gets more competitive.

Increased Efficiency and Innovation

Conference rates are influenced by the members' operating costs, these carriers may, however, not be the most efficient carriers in the market. As already mentioned inefficient carriers stay in the market at the detriment of shippers.

However if rates are set competitively this will ensure that the most cost efficient carriers stay in operation and inefficient carriers either improve their efficiency or leave the market.

As regards innovation competitive markets encourage firms to innovate to compete for customers on quality of product and price. Other evidence from liberalized markets, such as the airline industry, suggests that innovation would increase if the liner industry were made more competitive.

Innovation and increased efficiency associated with fuel savings would also bring benefits for the environment as a result of reduced emissions.

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[47] ICF Consulting, 2005, Economic Assistance Study on Liner Shipping

However, the expected price decreases may lead to higher demand and therefore more ships on the seas, so the overall effect on shipping emissions is ambiguous.[48]

Impact on Small Firms

The liner shipping industry requires firms to invest in considerable fixed costs. The Global Insight report concludes that liberalization may be beneficial for small carriers if they follow an innovative business model. The impact on firms will not be directly related to size. Instead a firm's ability to operate in a competitive environment will be a more important factor. Small carriers can reduce their operating costs and increase operational efficiency by joining alliances.

A report produced by ICF concluded that there is no common view amongst stakeholders that removal of the block exemption will affect small shippers. Although, theoretical arguments can be made that larger shippers could use predatory pricing strategies to drive small firms out of the market.

Small firms may find it harder to adjust rapidly to the block exemption removal and may be at a disadvantage compared to larger firms. However, it should be noted that a small European carrier has managed to carry on trading on the Europe East Coast South America route despite the removal of conferences on this route in 2004.

7.4.2 Amendment of Regulation 1/2003

Prior to the introduction of the new Council Regulation 1419/2006, cabotage and tramp services were the only remaining sectors to be excluded from the Community competition implementing rules.

The Commission acknowledged that the lack of effective enforcement powers for those sectors was an anomaly from a regulatory point of view. No convincing reason was given to maintain the exclusion for tramp vessel services. Similarly, although cabotage services often have no effect on intra-Community trade, this does not mean that they should be excluded from the scope of Regulation 1/2003 from the outset.

[48] Explanatory Memorandum to The Merchant Shipping (Liner Conferences) ACT 1982 (Repeal) Regulations 2008

As the mechanisms of Regulation 1/2003 are appropriate for applying the competition rules to all sectors, it was clearly appropriate that the scope of that Regulation be amended so as to include cabotage and tramp vessel services. [49]

7.4.2.1 Tramp Shipping Today

The new law assimilates tramp shipping to all other sectors of the economy and gives the Commission power to apply the competition rules concurrently with national competition authorities, using the powers it acquired under Council Regulation 1/2003 (the Modernisation Regulation) in May 2004. The transitional period, provided for liner conferences, does not cover the tramp shipping sector, meaning that the new rules have technically applied since 18 October 2006.

There is nevertheless a risk it could exercise its powers of information gathering to obtain copies of agreements and other market information, and if it found examples of hardcore cartels involving territorial or customer sharing between ostensibly independent operators it might not hesitate to commence proceedings. It has already sent out some informal requests for information to a number of pool managers and/or members.

The main impact of the rules will be felt in relation to pools and other forms of co-operation between competitors and potential competitors which involves direct or indirect rate coordination, limitations on output, sharing out of markets or customers, non-competition contracts, information exchanges or any other potentially anti-competitive provisions.

They should not have any specific impact on agreements that are usually termed "vertical", i.e. between parties operating at different levels of the supply chain, such as contracts of affreightment (CoAs)[50], requirements contracts, time or voyage charters, management agreements, agency agreements unless these have particular features

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[49] Watson, Farley & Williams, 2007, p. 11

[50] Contract of Affreightment: an expression usually employed to describe the contract between a ship-owner and a charterer, by which the ship-owner agrees to carry goods of the charterer in his ship, or to give to the charterer the use of the whole or part of the cargo-carrying space of the ship for the carriage of his goods on a specified voyage or voyages or for a specified time.

that tend to restrict competition: (such as exclusivity of supply or purchase, non-compete, tying of additional services in a package, long-term commitment obligations), or if two or more competitors agree jointly to provide such services on common or preferential terms.

Pools raise specific competition law issues because, in a typical pool, the pool manager will usually have day-to-day powers to negotiate contracts and rates with customers on behalf of all members of the pool for the ships in the pool, as well as taking sole responsibility for fleet scheduling, fixing of voyage and time charters and CoAs (up to agreed limits), and a number of commercial and operational matters. This constitutes an agreement directly or indirectly to fix prices, limit output and/or divide markets or customers between the members which are generally considered being hardcore offences under the competition rules.

There is currently no automatic block exemption for pooling agreements. The Commission's notice on de minimis agreements, that generally excludes agreements between actual or potential competitors provided their combined market share is below 10%, does not apply if there is any price fixing, output limitation or sharing of markets or customers. The block exemption for specialisation agreements[51] covers joint production between parties with no more than a 20% market share, and also covers agreements for the joint provision of services, other than purely the joint distribution or marketing of services. This might apply in certain cases to pools. We have already noted that the block exemption for liner consortia only covers the pooling of container vessels.

Pool agreements also often contain clauses that have the potential to restrict competition, such as restrictions on operating vessels outside the pool during and/or after the period of membership, information sharing arrangements and long notice periods required to withdraw vessels from the pool or leave the pool altogether.

To the extent that any provisions are deemed to be hardcore restrictions of competition they automatically fall within the terms of Article 81(1). There may be

[51] Commission Regulation 2658/2000

scope for arguing that they are covered by an individual exemption, but this requires careful self-assessment by the parties to the pool, requiring both legal and economic analysis. Individual exemption applies only where an agreement leads to economic efficiencies in the market (not just for the owners who pool their vessels), and every restriction including price restrictions must be justified as indispensable to achieve these efficiencies. At the same time the position of the parties in the market must not reduce competition in the market as a whole by, for instance, foreclosing new entry or making it more difficult for competitors to operate.

The consequences of non-compliance can be extremely serious. In particular the competition authorities have powers to carry out dawn raids on business to detect anti-competitive behaviour, impose fines of up to 10% of the worldwide group annual turnover of any party found liable.

Given the novelty of the rules in this part of the shipping industry (in contrast to the liner industry which has experienced competition law for many years) the European Commission is not expected to put the full weight of its enforcement powers to work immediately. Fines would only be imposed for obvious cartel-like behaviour, and not genuine pooling agreements, in this interim period.

Furthermore, self-assessment will remain a difficult exercise until the Commission has issued clarification of the existing law and possibly even introduced new block exemptions geared to the specific problems of the tramp sector. The exercise is likely to take until well into 2008.

That said, anyone involved in any way with a shipping pool or contemplating entering into one should not be complacent. It is certainly not too early for pool members to start the process of ensuring compliance with the competition rules, beginning with a legal analysis of their agreements in the light of the existing competition rules, analysing the economic background in which the agreements operate with a view to identifying what the relevant market is, and beginning the process of identifying express restrictions or other potentially restrictive effects that could possibly be reduced or eliminated to avoid major problems under competition law.

Until the European Commission's guidelines emerge, however, pool members face some difficult choices: they can either wait and see (which, as indicated, may not be the best

course), or start the legal and economic analysis now so as to identify the options. Those options are likely to include full self-assessment (which may be worth considering for pools that are not reckoned to control a high market share), some preliminary adjustment of the contract terms to reduce the risks of fines later, or possible termination.

Another option for pool members is to reconstitute their pools as full-function joint ventures, which are treated as concentrations under the EC Merger Regulation.[52] These require a separate and independent corporate and management structure to be established to carry on the business of the pool, which must be established as a long-term autonomous "undertaking" operating self-sufficiently on the market in which the members do not interfere with commercial decisions over and above what shareholders normally do.

The creation of a full-function joint venture falls outside the ordinary EU competition rules, but is in principle subject to merger control at either European Community or national level. The EC Merger Regulation applies exclusively to all concentrations with a Community dimension, meaning those where the parties to the transaction meet certain minimum turnover thresholds. These must compulsorily be notified to the European Commission and cleared before completion.

There are cases where a full-function joint venture provides an attractive alternative to pools, but it does considerably change the nature of the pool and its relationship with its members. For that reason many may not wish to rush into this solution without waiting to see what transpires from the European Commission guidelines.

7.4.2.2 Cabotage

Non-international (cabotage) transport services benefited from a unique status in that they were in principle subject to the competition rules but those rules could only be enforced by the national cartel authorities in each EU Member State, who in fact never had any reason to do so.

However, since 18 October 2006 any agreement between cabotage operators that affect trade between Member States will have to be compatible with article 81(1) of the Treaty. An exception is made when an agreement meets the four conditions of Article 81(3), i.e. when the agreement increases efficiency, enables consumers to receive a fair share of the resulting benefits, doesn't contain any restriction which is not indispensable and doesn't distort competition.

[52] Council Regulation 139/2004

There are no guidelines published concerning the application of the new Regulation for cabotage services. The guidelines though which address liner and tramp shipping are relevant because cabotage services are provided either as liner or tramp shipping services.

The burden is now on undertakings and their advisers to assess correctly the compatibility of their business arrangements with Articles 81 and 82 as the notification system is abolished.

Another issue for the cabotage service providers is that they may be considered to be in a dominant position if they have concluded in a contract for public service on a particular route and they are the only operators on this route.

8. Conclusions

It is obvious that Regulation 4056/86 ought to be repealed because the conditions for an exemption appear to be no longer fulfilled. There is no conclusive economic evidence that the assumptions on which the block exemption was justified at the time of its adoption in 1986 are, in the present market circumstances and on the basis of the four cumulative conditions of Article 81(3) of the Treaty, still justified.

In addition the Commission came to the conclusion that the exclusion of cabotage and tramp vessel services from the scope of Regulation 1/2003 had no justification and so the Regulation should be amended to include both of these services.

Both liner and tramp shipping operators search for an alternative form of cooperation, to conferences and pools respectively, that won't fall into the scope of Article 81(1).

8.1 Liner Shipping

The effect of the repeal of Regulation 4056/86 is that agreements having an actual or potential effect on trade between EU Member States and having the object or effect of preventing restricting or distorting competition in the EU to an appreciable extent are prohibited in respect of their restrictions.

With the imminent abolition of the exemption for liner conferences, the liner sector faces an immediate problem as undoubtedly such conferences do constitute price fixing. The EU regime applies only to conferences operating to and from the European Union. Participants may still take part in price-fixing and capacity regulation in

conferences operating on non-EU routes, so far as allowed under other competition law systems.

The Commission has been involved in extensive debate and discussion with both sides of the liner industry (both owners and shippers) on what should replace the block exemption. The guidelines on the application of competition rules to maritime transport sector makes it clear that liner conferences are unlikely ever to be individually exempted under Article 81(3) as the threshold for exemption is set too high.

Suggestions that some form of information exchanging to allow publication of benchmark rates could be declared permissible have in large part been rejected by the European Commission. On 29 September 2006 the Commission already published an "issues paper" setting out its preliminary assessment of information exchanges in the liner market. These leave room only for very limited forms of information exchanging and fall well short of what liners had been requesting.

What seems to be the best alternative are Consortia agreements. The European Shippers' Council is also in favor of consortia, as to what should replace the block exemption.

Consortia differ from conferences in containing no pricing element at all, with partner lines sharing ships, swapping slots or co-operating in some other way, in order to cut costs and improve efficiencies, while still competing for cargo.

The Commission and cargo owners, as well as lines, have always acknowledged the benefits of operating alliances that's why block exemption for liner consortia has existed since 1992 and this continues to benefit joint scheduling arrangements and other forms of vessel sharing (subject to a market share cap of 30-35%).[53]

That, however, specifically excludes agreements that involve price fixing. Moreover, since it specifically refers to consortium agreements involving maritime services provided "chiefly by container", it can virtually never apply in the tramp sector.

The European Commission has redrafted the text of the consortia block exemption that is due for renewal in 2010.

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[53] Commission Regulation 823/2000

However container lines are alarmed at some of the proposed changes that, they claim, would force a number of important co-operations to be disbanded.

What have alarmed the liners are two clauses in a draft of a block exemption for consortia that would come into force in 2010 when the present Regulation expires.

These state that "the market shares of carriers that provide services both individually and within a consortium on the same relevant market have to be aggregated", and that "market shares of consortia operating in the same relevant market and interlinked by common membership have to be aggregated".[54]

A proposed market share threshold has also been set at 30%, lower than the level now permitted for non-conference lines. Yet the industry has forged many links between alliances, or between individual consortium members and other lines, in an effort made to cut costs, which would breach that ceiling when combined.

The text has provoked an outcry in liner shipping circles. Container line bosses are furious that the commission wants to aggregate market shares in situations where there are inter-linking arrangements between consortia, or where a line provides a service both individually and through an alliance on the same trade route.

Addressing the European Maritime Law Organization's 14th annual conference in Copenhagen, Mr. Guersent expressed the Commission's point of view: "The purpose of a block exemption was to provide legal certainty for some forms of agreement between container lines that are not regarded as anti-competitive.

Such legal certainty can only be provided in situations where it is safe to assume that no competition problem will arise. But some inter-linking arrangements are known to have market shares of up to 80%.

The commission is precisely not ready to give its permission in such situations. I am not saying that there is for sure a competition problem in such a case. I am simply saying that it is not impossible that there is a competition problem."

Mr. Guersent also stated that the industry "is better treated than many other industries", and is the last transport industry to benefit from a block exemption.

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[54] Janet Porter, 2008

The European Shippers' Council on the other hand proposed to the European Commission that a renewal of the consortia block exemption in 2010 should not take place.

Although shippers are broadly in favor of alliances because of the benefits they deliver in terms of operating efficiencies, the ESC has told the commission it does not believe a block exemption is necessary. Consortia should ensure they do not infringe EU competition rules through self-assessment.

However, the commission is committed to renewing the current Regulation for another five years, although there is no guarantee that it will be extended beyond 2015.

The Commissions aim is to achieve greater convergence between the consortia block exemption and the allowances for other industries where market share thresholds are mostly set at 20%.[55]

With a ceiling of 30%, the maritime industry will still benefit from a preferential sectoral treatment.

Furthermore, even a consortium that has a market share of more than 30% will not automatically be illegal. Member lines will have to self-assess to determine whether competition is restricted.

What liner consortia cannot expect is legal certainty in every case, since a block exemption Regulation can only give immunity to clear-cut situations.

8.2 Tramp Shipping

Pools, as with other looser forms of cooperation involving actual or potential competitors, are by virtue anti-competitive. Following the Commission's reform program, it has become a priority for all operators to examine the extent to which pools might have an impact on EU trade and to analyze them under the EC competition rules.

Generally, the administrator or manager of the pool will negotiate all of the rates for the vessels under its control and all rebates, discounts etc., in which case price competition between the ship owners is eliminated. As a flexible form of cooperation, pools are similar to alliances. As such, they may appeal in particular to sectors of the industry where the need for cooperation can vary significantly, depending on market trends.

[55] Janet Porter, 2008

The best alternative to shipping pools and the one that matches better to the structure of the tramp shipping industry, considering that the block exemption for consortia agreements does not refer to tramp ships, is a joint venture.

Replacing a tramp shipping pool with a JV would not necessarily change much of what some shipping pools already do today and how they are structured.

Certain JVs, if structured correctly, can be notified and cleared as concentrations. Cooperation between the JV parties will thus be “immune” to the Commission’s investigation.

These JVs are referred to as full-function joint ventures (FFJV) and are defined as JVs that “perform all the functions of an autonomous economic entity on a lasting basis”. In the context of the EC competition rules, the Commission applies the term JV to an undertaking that is “jointly controlled” by at least two parents. Combining these two definitions, an FFJV is therefore an undertaking that is jointly controlled by at least two parents and that performs all the functions of an autonomous business on a lasting basis.

Joint ventures can therefore provide the tramp shipping industry the economies of scale that are necessary without the fear of being unlawful.

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