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The EU Reform Treaty & the Competition Protocol: Undermining EC Competition Law

Alan Riley

1. Introduction

Agreement was reached by the EU member states in June 2007 to remove the competition phrase contained in Article 3(1)(g) of the EC Treaty¹ from the new Reform Treaty (hereafter referred to as the competition principle) and create a 'competition protocol'² that includes the words from Article 3(1)(g). This paper argues such treatment of the matter is inadequate to protect the current competition *acquis* and ensure the healthy future development of Community competition law.

¹ The provision of "a system ensuring that competition in the internal market is not distorted".

² In the Presidency Conclusions the text of the protocol is set out as "The High Contracting Parties considering that the internal market as set out in Article 3 of the Treaty on European Union includes a system ensuring that competition is not distorted". The protocol then goes on to provide that "The Union shall, if necessary, take action under the provisions of the Treaties, including under Article 308 of the Treaty of the Functioning of the Union". Article 308 currently provides "If action by the Community should prove necessary to attain, in the course of the operation of the common market, one of the objectives of the Community, and this Treaty has not provided the necessary powers, the Council shall, acting unanimously on a proposal from the Commission and after consulting the European Parliament, take the appropriate measures". It is understood that no substantive changes are planned for Article 308 in the Reform Treaty. It should also be noted that the protocol is likely to be subject to some amendment. See the latest version from the draft Council Treaty negotiating document, which suggests the following text: "THE HIGH CONTRACTING PARTIES, CONSIDERING that the internal market as set out in Article [I-3] of the Treaty on European Union includes a system ensuring that competition is not distorted, HAVE AGREED UPON the following provision, which shall be annexed to the Treaty on European Union and to the Treaty on the Functioning of the Union: [Sole Article] For the purposes of the first recital, the Union shall, if necessary, take action under the provisions of the Treaties, including under Article [308] of the Treaty on the Functioning of the Union". See <http://www.consilium.europa.eu/uedocs/cmsUpload/cg00002.en07.pdf>

Far from being a minor technical adjustment, this paper argues that the excision of the competition principle from the front of the Treaty is likely to have a number of damaging consequences for EC competition law. There is a real danger that in future EC competition law will be cribbed, crabbed and confined. While price-fixers may still be fined and dominant firms such as Microsoft put under the investigatory microscope, the power of the State to distort competition through subsidy and regulation will increase. There are also serious concerns as to the extent to which the excision of the competition principle will be deployed to assist industrial policy arguments in merger control cases and frustrate the liberalisation of hitherto protected industrial sectors.³

The paper is divided into four parts. Section 2 considers whether a protocol is sufficient to protect the current competition *acquis*; section 3 considers the likely consequences if Article 3(1)(g) is not restored and the final section offers a conclusion.

2. Is a protocol enough to protect competition?

In a letter of 27 June 2007 to the Financial Times, Mr Michel Petite, the Director General of the European Commission's Legal Service, rejected the arguments of FT columnist Wolfgang Munchau that the removal of the competition principle from the Reform Treaty threatened the status of competition in the single market. (Petite's letter is worth quoting in full – see box on next page.)

³ See Jonathan Galloway, "The Pursuit of National Champions: The Intersection of Competition Law and Industrial Policy", *European Law Review*, Vol. 28, No. 3, 2007, pp. 172-186.

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Petite argued firstly that the competition principle enunciated in Article 3(1)(g) has never been an objective in Community Law. The competition principle had only ever appeared as an objective in the failed EU Constitution. Since it has never been an objective in the EC Treaty, its non-appearance as an objective in the Reform Treaty does not impact the status of competition in the Community legal order. He then goes on to argue that as a protocol is legally binding in Community law, the ‘competition protocol’ has the effect of protecting the status of competition law.

Text of letter to the editor of the FT from Michel Petite

Sir, Wolfgang Munchau ("The madness of Europe's drift to mercantilism", June 25) seems to be worried by the removal of an explicit reference to free and undistorted competition from the provision in the future 'Reform Treaty' listing the policy objectives of the European Union and has doubts as to the legal implications of the protocol that the European Council has proposed in its place. As a matter of fact, competition is not currently one of the objectives of the European Community set out in Article 2 of the EC Treaty: the reference to "undistorted competition" appears only in Article 3 on the Community activities to be implemented to attain those objectives. Clearly, an objective that does not exist cannot be lost! The fact that competition is a means and not an objective of the Community has not – over the past 50 years or so – prevented the European institutions, and in particular the European Commission and the European Court of Justice, from taking effective action against any restriction or distortion of competition within the internal market, whether resulting from initiatives taken by undertakings or by member states' public authorities. The text of the 'Constitutional Treaty' provided for a substantial reworking of the above provisions, with an explicit reference to "free and undistorted competition" linked to the 'internal market' objective. The principal effect of dropping those words from the future 'Reform Treaty' is to bring us back to the present situation. To avoid any risk of uncertainty as to settled law and to make fully clear that competition will continue to be one of the main policies aiming at the good functioning of the internal market, the European Council decided to provide for the protocol referred to by Mr Munchau, which paraphrases the current EC Treaty provisions. It is also worth recalling that, from a legal point of view, a protocol forms an integral part of the Treaty to which it is annexed and has the same legal value as Treaty provisions. That is why I do not share Mr Munchau's legal concerns on this issue.

Source: *Financial Times*, 27 June 2007.

This letter is disingenuous in the extreme. What it seeks to glide over is the fact that the EC Treaty Article 3(1)(g) listed competition as an activity of the Community and that no similar provision will exist in the preamble or first few articles of the Treaty under the new Treaty regime.

Petite argued that this is not important because of the legally binding nature of a protocol in Community law. Accordingly, the status of competition law would be maintained in the Reform Treaty. While it is correct to say that a protocol is legally binding, his argument does not take account of the way the European Court of Justice looks to the objective and purposes of the Treaty from the preamble and the first few articles to interpret substantive Treaty provisions.

What is overlooked in Petite's analysis is that the preamble and the first few 'principle' articles are always going to have a tremendously important impact on the Court. First, the ECJ is going to take account of Articles 31(1)⁴ and 33(4)⁵ of the Vienna Convention on the Law of Treaties which emphasise the importance of the objective and purpose of the Treaties as a guide to interpretation. Second, as a result of the existence of 19 technically equally authentic language versions of the Treaties the Court has little alternative but to take an object and purpose approach. The third factor is the development of a strong Community law sui generis purposive interpretation tradition. This tradition seeks to deal with major questions of scope and conflicts of values by consideration of the objectives and purposes of the Treaties as set out in the preamble and the first few articles of the Treaties. In the EC Treaty this means the preamble, Articles 2 and 3 and certain other articles of principle such as Articles 10 on co-operation and Article 13 on discrimination.

No mere protocol can achieve the same interpretative status as the preamble and the first few articles. Any close examination of the case law demonstrates the fundamental nature of Article 3(1)(g) in making competition an objective of the Community legal order, most notably in *Continental Can*⁶ where the Court ruled that 'If Article 3(f) [now Article 3(1)(g)]⁷ provides for the institution of a system ensuring that competition in the Common Market is not distorted, then it requires a fortiori that competition must not be eliminated. *This requirement is so essential that without it numerous provisions of the Treaty would be pointless.*[authors italics]'⁸

⁴ "A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose."

⁵ "When a comparison of the authentic texts discloses a difference of meaning which the application of articles 31 and 32 does not remove, the meaning which best reconciles the texts, having regard to the objects and purpose of the treaty, shall be adopted."

⁶ Case 6/72 [1973] ECR 215.

⁷ The provision moved from Article 3(f) at Maastricht becoming Article 3(g). At Amsterdam it became Article 3(1)(g).

⁸ Op. cit., para 24.

This view has been echoed in more recent cases, for example, in *Courage Limited v. Crehan*⁹ the Court was clear as to the effect Article 3(1)(g) had on Article 81 (then Article 85):

According to Article 3(g) of the EC Treaty (now, after amendment, Article 3(1)(g) EC), Article 85 of the Treaty constitutes a fundamental provision which is essential for the accomplishment of the tasks entrusted to the Community and, in particular, for the functioning of the internal market.¹⁰

At the very least it is open to question how easy it is going to be for a protocol tacked on to the back of the Treaty to maintain the status of Article 81 (and Article 82) as a ‘fundamental provision’. The *Crehan* case concerned a challenge to the English rule that a party to a contract which it alleged to be unlawful was barred from subsequently bringing an action for damages based upon that same contract. The Court took the view that the absolute bar to action was unjustified and such factors as the relative bargaining power of the parties and their conduct should be taken into account in permitting an action for damages to proceed.¹¹ Without Article 3(1)(g) setting out the interpretative object and making Article 81 a ‘fundamental provision’ will the Court be able to take such a broad approach to the application of the competition rules based on a protocol in the future?

Perhaps even more disturbing is the discussion of the conflict of objectives in *Albany International*.¹² *Albany* concerned the status of a state measure imposing compulsory charges to a pension fund. The key issue in that case was the way the Court recognised that two conflicting Community objectives were in play.

.....It is important to bear in mind that, under Article 3(g) and (i) of the EC Treaty (now, after amendment, Article 3(1)(g) and (j) EC), the activities of the Community are to include not only a ‘system ensuring that competition in the internal market is not distorted’ but also ‘a policy in the social sphere’. Article 2 of the EC Treaty (now, after amendment, Article 2 EC) provides that a particular task of the Community is ‘to promote throughout the Community a harmonious and balanced development of economic activities’ and ‘a high level of employment and of social protection’.¹³

What happens when competition is no longer an objective in one of the key first few interpretative articles of the Treaty and the competition objective has

to be balanced against social objectives that are in one of the key interpretative articles? How likely is it that the Court will balance the competition protocol with the same weight as one of the social objectives set out at the front of the Treaty?

The broad influence of Article 3(1)(g) can also be seen in the debate on the development of Article 82 in *British Airways v. Commission*.¹⁴

The starting-point here must be the protective purpose of Article 82 EC. The provision forms part of a system designed to protect competition within the internal market from distortions (Article 3(1)(g) EC). Accordingly, Article 82 EC, like the other competition rules of the Treaty, is not designed only or primarily to protect the immediate interests of individual competitors or consumers, but to protect the *structure of the market* and thus *competition as such (as an institution)*, which has already been weakened by the presence of the dominant undertaking on the market. In this way, consumers are also indirectly protected. Because where competition as such is damaged, disadvantages for consumers are also to be feared.¹⁵

It is possible that here however the French government and its Commission supporters may find that excising Article 3(1)(g) from the front of the Treaty has a significant downside. If Article 3(1)(g) is excised then it would make it easier for the proponents of a more economically liberal approach to Article 82 to argue that there is less need to protect the structure of the market and permit instead a greater focus on harm to consumers and consumer welfare.

Article 3(1)(g) was also one of the major planks in the development of the State Measures cases from *Inno v. ATAB*¹⁶ in 1978 to the recent *CIF* case¹⁷ which seek to restrict the power of the Member States to circumvent the competition rules. For example, if a Member State seeks to hide an illegal price-fixing cartel under the umbrella of state legislation, the ECJ has permitted the Commission to challenge such legislation using Article 3(1)(g) read with Article 10.¹⁸ Does the excision of Article 3(1)(g) mean that it will be more difficult for

⁹ Case C-453/99 [2001] ECR I-6297.

¹⁰ *Ibid.*, para 20.

¹¹ *Op. cit.*, para 22.

¹² C-67/96 [1999] ECR I-5751.

¹³ *Ibid.*, para 54.

¹⁴ Case C-95/04 P, 15 March 2007, not yet reported.

¹⁵ *Ibid.*, para 68.

¹⁶ Case 13/77 [1977] E.C.R. 2115.

¹⁷ Case C-198/01 [2003] ECR I-8055

¹⁸ See, for example, the *Belgian Travel Agents Case 311/85 ASBL Vereniging van Vlaamse Reisbureaus v. ASBL Sociale Dienst van de Plaatselijke en Gewestelijke Overheidsdiensten* [1987] ECR 3801.

the Commission to challenge such state inspired circumvention of the competition rules in the future.¹⁹

It is also clear that Article 3(1)(g) has been deployed to buttress the state aid rules. For example, take the approach of the Court of First Instance in *Air France v. Commission*:²⁰

Article 92(1) of the Treaty ...refers to 'aid granted by the States or through State resources `in any form whatsoever'. Consequently, those provisions must be interpreted not on the basis of formal criteria but rather by reference to their purpose, which, according to Article 3(g) of the Treaty, is to ensure that competition is not distorted. It follows that all subsidies from the public sector threatening the play of competition are caught by the abovementioned provisions, it being unnecessary for those subsidies to be granted by the government or by a central administrative authority of a Member State (see, to that effect, Case C-305/89 *Italy v Commission* [1991] ECR I-1603, paragraph 13, and *Sloman Neptun*, cited above, paragraph 19).²¹

It could however be argued that as long as the words of the competition principle are found somewhere in the Treaty, even in a legally binding protocol, they would still have the same interpretative effect.²² The difficulty with this view is that it could only ever sustain credibility if one were to argue that the preamble and the first few articles of the Treaty did not have any special interpretative effect compared with

¹⁹ See for instance Barry Rodger (ed.), *Article 234 and Competition Law: An Analysis*, Kluwer, 2007. In particular, note in chapter 3 where Rodger points out that state-related case law constitutes the majority of competition rulings handed down by the ECJ.

²⁰ Case T-358/94 [1996] ECR II-2109.

²¹ Op. cit., para 55

²² One additional argument that could be made is that the reference in the proposed protocol to Article 308 EC which does refer to the Community objectives could be deployed by the ECJ to deem competition law an objective. For this view to prosper, unfortunately, a heroic effort at interpretation would be required by the ECJ. Article 308 is in essence the 'any other business' provision of the Treaty. It is difficult to see how the Court can derive such an interpretation from Article 308. Furthermore, the text of the sentence, while specifically referring to Article 308 makes it clear that the Union can take action under "the provisions of the Treaties" more generally, which suggests that what the authors of the protocol had in mind was to preserve the legal base for legislation on competition matters beyond Articles 81 and 82, for instance in respect of merger control. In fact, this second sentence reinforces the view that the excision of Article 3(1)(g) from the front of the Treaty has undermined the status of competition law. Why otherwise would the framers of the protocol have felt it necessary to include the second sentence of the protocol to preserve the legal base for competition legislation?

other provisions of the Treaty. It is however clear from the text and structure of the preamble and the first few articles as well as the case law discussed above that they clearly do have significance that is not accorded to other Treaty provisions and protocols.

It is difficult therefore to sustain the argument that the excision of Article 3(1)(g) from the front of the Treaty will not have a significant negative effect on Community competition law. At the very least there has to be concern that the power of the Member States to distort competition law has been facilitated by the removal of Article 3(1)(g). For example, will the CFI and the ECJ consider that they can safely uphold the existing state measures case law which expressly relies upon Article 3(1)(g) to restrict state inspired circumvention measures to distort the competition rules? Both courts will probably find it difficult to maintain the legal position set out in existing case law when the competition principle upon which a large part of it rests has been removed from the interpretative provisions of the Treaty? Clearly the competition protocol will be given some weight, but it is very difficult to see how it can be given the same weight as the interpretative provisions at the front of the Treaty. The conclusion therefore is that the competition *acquis* will be weakened by the excision of Article 3(1)(g).

One person who has little doubt as to the impact of the excision of Article 3(1)(g) from the front of the Treaty is President Sarkozy. At the June press conference, he took the following view of the excision of Article 3(1)(g):

We have obtained a major reorientation on the objectives of the Union. Competition is no longer an objective of the Union or an end in itself, but a means to serve the internal market...

Perhaps even more illuminating is this snapshot taken from the Q&A:

Question: To return to the objectives of the EU, on competition and the protection of citizens: What do these changes mean exactly in the daily life of the French and or the Europeans?

Answer. This perhaps gives a little more humanity to Europe. Because as an ideology, as dogma, what did competition give to Europe? It has given less and less to the people who vote at the European elections, and less and less to the people who believe in Europe. There was perhaps a need to reflect. I believe in competition, I believe in markets, but I believe in competition as a means and not an end in itself. This may also give a different legal direction to the Commission. That of a competition that is there to support the emergence of European champions, to carry out a true industrial policy. It was not a

question of making an economic Treaty or a liberal Treaty and explain it to the citizen. It was a question of turning our backs to ideology, dogma and naivety.²³

3. Consequences for competition if the proposed reform treaty is not amended

It is difficult in advance of a finalised Treaty text – never mind any case law on the issue – to give a comprehensive overview of the impact of the relegation of the undistorted competition phrase to a protocol. However, it is not unreasonable to suppose that some member states will be looking to use the Reform Treaty to weaken the crucial impact of competition law. Three particular lines of attack are relatively easy to identify.

First, to expand the scope for lawful state aid: As the *Air France* case indicates above, Article 3(1)(g) was available to reinforce the obligations in respect of state aid, to limit any legal formalism and minimise justifications for aid. The ECJ could look again at cases like *Air France* restricting the scope of the notion of the sources of aid.

Second, to permit merger clearance on broader industrial policy grounds: The scope of EC merger control has always been contentious. However, over the last decade it has slowly evolved to a much stronger consumer welfare standard focusing on direct harm to consumers. This development is potentially at risk. With the removal of Article 3(1)(g) and the existence of social and economic development objectives in the new Article 3, there is scope to make an argument for a broader industrial policy standard in merger clearance.²⁴ The broadening of the assessment standard could also make it easier for member states to justify clearance on the basis that the deal would create a national or European champion. The development of a stronger industrial policy approach to merger clearance and support for industrial champions as indicated above clearly seems to be one of the aims of Sarkozy's excision of Article 3(1)(g).

²³ I am thankful to Dr Giorgio Monti at the LSE who extracted these quotes, translated them and put them on his blog. The quotes can be found at his blogsite (see <http://competitionlawboard.blogspot.com/2007/06/more-on-politics-of-brussels-summit.html>).

²⁴ There is an apparent conflict here between the prospect of weakening the structural approach to Article 82 and a stronger industrial policy approach to merger control. However, it is submitted that this conflict is more apparent than real. Once the objective of Article 3(1)(g) is excised from the front of the Treaty, there is a greater danger of fragmentation. Hence Article 82 may lose the structural aspect of its case law whereas the merger control case law may take on a stronger industrial policy character.

Third, to weaken the pressure for market liberalisation, particularly in respect of ownership unbundling in the energy sector: One major concern here is that the Commission's powers under Article 86(3) of the EC Treaty and Article 7 of Regulation 1/2003 to order the break up of monopolistic infrastructure could be circumscribed by the excision of the competition principle. At the very least the removal of the competition principle is likely to raise concerns in DG Competition as to the scope of its powers in Article 86(3) and Article 7 of Regulation 1/2003 to take measures such as ordering ownership unbundling and/or such parallel measures requiring gas release schemes under the Merger Regulation.

4. Choking competition law

Many practitioners may take the view that they need not be bothered by this development. Leniency applications will still be made, merger filings will still take place and Article 82 may inadvertently be given a more economically radical edge. However, outside these core areas, if the competition principle is not restored to its position as one of the key interpretative articles of the Treaty, the development of competition law and the competitiveness of the European Union will suffer. The fundamental development of competition law into hitherto protected sectors and its ability to limit the impact of state interference on the competitive process will be compromised. Given the size of the state in most member states, this is no small matter for European competitiveness and the long-term prospects for growth and the economic future of all Europeans

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