



Views on Commission Regulation (EC) No 906/2009

June 2013

The World Shipping Council (WSC), the European Community Shipowners' Associations (ECSA), and the International Chamber of Shipping (ICS) respectfully submit these preliminary views on the Commission's review of Commission Regulation (EC) No 906/2009 on the application of Article 81(3) [101(3)] of the Treaty to certain categories of agreements, decisions, and concerted practices between liner shipping companies (consortia). The World Shipping Council is a non-profit trade association, with offices in Brussels and Washington, D.C., that represents the interests of the international liner shipping industry in public policy and regulatory matters. WSC's twenty-nine member companies account for more than ninety percent of the world's liner shipping capacity. ECSA is a non-profit trade association whose membership comprises the national shipowner associations of the European Union and Norway. ECSA's aim is to promote the interests of European shipping so that the industry can best serve European and international trade and commerce in a competitive free enterprise environment to the benefit of shippers and consumers. ICS is the global trade association for shipowners with a membership comprising national shipowners' associations in 36 countries, representing all sectors and trades and over 80% of the world merchant fleet.¹

The purpose of this initial informal submission is to present the view of the liner shipping industry with respect to the need for continuation of the Consortia Block Exemption Regulation (BER), with the aim of assisting the Commission as it continues its review of the

¹ The World Shipping Council is registered with the Registry of Interest Representatives. Additional information about WSC and the liner shipping industry is available at www.worldshipping.org. The European Community Shipowners' Associations is registered with the Registry of Interest Representatives. Additional information about ECSA and its member associations is available at <http://www.ecsa.eu>. The International Chamber of Shipping is registered with the Registry of Interest Representatives. Additional information about ICS is available at www.ics-shipping.org.

Consortia BER. WSC, ECSA, and ICS respectfully urge the Commission to continue the current successful policy authorized by Article 103 of the Treaty and by Council Regulation (EC) No 246/2009 by extending the Consortia BER for at least another five years.

Executive Summary

In Section 1 below, we provide a brief review of the Council and Commission findings with respect to the Consortia BER to date.

Section 2 discusses developments in the liner shipping market since the Commission's last review of the consortia BER. That section emphasizes the trends of sharply higher fuel prices, flat freight rates, and the trend towards using larger vessels in the trades that will support them as a way to reduce carrier costs and provide the most efficient services possible. These developments demonstrate that the factual predicate that the Commission has recognized for years with respect to the benefits of consortia continues and is in fact reinforced by economic developments since the last review of the BER.

Section 3 directly addresses the question of why the Consortia BER is a more appropriate tool than the Horizontal Guidelines for applying competition law to liner shipping consortia. The Consortia BER has been shaped through nearly 20 years of practical experience to reflect both the Commission's compliance objectives and also the industry's need for clear guidance stated in terms that are specific to the activities that are common to virtually all consortia.

Although one could argue that the Consortia BER is consistent with the general guidance provided by the Horizontal Guidelines, the converse argument could not seriously be made. That is, if the Consortia BER were repealed, it would be entirely implausible to suggest that the level of specificity and certainty provided by the Consortia BER could be derived from the very general principles of the Horizontal Guidelines. But it is that very specificity and certainty that have, for almost 20 years, made the Consortia BER such an effective compliance tool for both carriers and the Commission. The fact that most consortia share many common elements makes this form of cooperation especially well-suited for guidance through the block exemption mechanism.²

² The Commission recognized over twenty years ago that the common features of consortia and the frequency with which changes were made to consortium agreements make this type of cooperation well-suited to regulation through the block exemption mechanism:

"Consortia in liner shipping are a specialised and complex type of joint venture. Unlike most commercial and industrial joint ventures the scope, parties, activities and terms of consortia agreements are frequently altered. A block exemption for consortia should therefore concentrate on clarifying the requirements under which consortia can be

If the Consortia BER were repealed, ten expert competition law attorneys could make ten different lists of what could and could not lawfully be done within a liner consortium under the Horizontal Guidelines, and all ten would have an equal chance of being correct. Allowing all parties to know exactly what they can and cannot do within the safe harbor of the consortia BER allows carriers to focus resources on operational improvements as opposed to devoting those resources to overcoming compliance uncertainties. In addition to providing carriers with a clear, common understanding of the rules, the BER has given shippers comfort that the consortia that provide them with welcome efficiencies and improved service will enhance rather than diminish competition. WSC, ECSA, and ICS query what public policy would be furthered by replacing the certainty that exists today with the ambiguity and confusion that would result from repeal of the Consortia BER.

Section 4 discusses the adverse economic and operational implications of failing to renew the Consortia BER. Although it would be an exaggeration to suggest that liner consortia would cease to exist in the European trades in the absence of the BER, it would also be incorrect to assume that repeal of the BER would have no adverse consequences. The legal certainty provided by the BER allows carriers to consider the formation, amendment, dissolution, or replacement of consortia solely on the basis of the operational benefits that might be generated. By providing carriers the confidence that their consortia can be operated lawfully, the Consortia BER facilitates the large-scale investments that are necessary to deploy and operate the efficient services that consortia provide. Where, as here, the underlying economic activity (use of consortia) has been found to be beneficial for trade, and the existing means of legal guidance (the BER) is well-suited to the task and is accepted by carriers and shippers, there is a great deal more to be lost than there is to be gained by allowing the Consortia BER to lapse.

1. History and Rationale of the Consortia BER

Beginning with Commission Regulation (EC) No 870/95, which was adopted by the Commission pursuant to the power granted to it by Council Regulation (EEC) No 479/92, the Commission has adopted a series of consortia block exemption regulations, each effective for a period of five years. The current regulation, No 906/2009, adopted under authority of Council Regulation (EC) No 246/2009, expires in April of 2015.

exempted from the prohibition of cartels pursuant Article 85(3) of the Treaty, rather than differentiating between consortia."

Commission Report on the possibility of a group exemption for consortia agreements in liner shipping, COM (90) 260 final of 18.6.1990.

Throughout the history of the Council and Commission regulations concerning liner shipping consortia, the Parliament, the Council, and the Commission have consistently found that consortia falling within the scope of the published regulations “help to improve the productivity and quality of available liner shipping services by reason of the rationalisation they bring to the activities of member companies and through the economies of scale they allow in the operation of vessels and the utilisation of port facilities. They also help to promote technical and economic progress by facilitating and encouraging greater utilisation of containers and more efficient use of vessel capacity.”³

The various regulations have also found that consortia operating within their scope provide benefits to shippers, with the current regulation noting that: “Users of the shipping services provided by consortia may benefit from the improvements in productivity which consortia can bring about. Those benefits may also take the form of an improvement in the frequency of sailings and port calls, or an improvement in scheduling as well as better quality and personalized services through the use of more modern vessels and other equipment, including port facilities.”⁴

Taken together, these efficiency and innovation gains, a fair share of which accrue to the shipper customers of carriers participating in consortia, have been found to satisfy the conditions of Article 101(3) of the Treaty with sufficient certainty that such consortia may properly be exempted from Article 101(1) as provided in Article 103 of the Treaty on the Functioning of the European Union (TFEU). These findings remain valid, and recent developments in the liner shipping markets demonstrate why consortia are at least as central today to the efficient operation of the liner shipping industry as they have been in the past.

The block exemption for consortia is also consistent with the international consensus that exempts international liner shipping consortia from national competition laws around the world.

2. Market Developments Since the Last Consortia BER Review: Cost Increases and Bigger Ships

The fundamental characteristics of the liner shipping industry that have been the basis of the Consortia BER since 1995 remain unchanged today. Specifically, the industry is not concentrated; there are no regulatory barriers to carriers entering markets; the industry struggles with overcapacity for structural, cyclical and seasonal reasons, but such excess

³ Commission Regulation No 906/2009, recital 5.

⁴ Commission Regulation No 906/2009, recital 6.

capacity cannot be utilized or easily idled; capital and operating costs are high; the industry is highly competitive with shippers having an array of service choices; and profits (where they exist) and returns on investment typically lag behind those of other major industries. In short, the industry is a very challenging one for vessel operators and is a favorable one for the European importers and exporters that use the services of those vessel operators.

Although the fundamental characteristics of the liner shipping market remain as they have been during earlier Commission reviews of the Consortia BER, some trends that had begun to appear at the time of the Commission's last review of the Consortia BER have accelerated since that last review. The two trends with the greatest relevance to the role of consortia are the substantial increases in the cost of fuel and the related trend towards larger vessels, especially in the trades between Asia and Europe.

According to *Alphaliner*, in January of 2007 there were two container vessels in excess of 10,000 TEUs.⁵ As of December 31, 2012, there were 162 such vessels. By the end of December 2016, based on *Alphaliner's* analysis of orderbooks, there will be an estimated 281 container vessels over 10,000 TEUs. Also according to *Alphaliner*, the next largest container vessel size (7,500 to 9,999 TEUs) has grown from 145 ships in 2007 (total capacity 1,225,433 TEUs) to 326 ships at the end of 2012, with continued projected growth by the end of 2016 to 437 ships. These vessel size increases are in addition to an earlier increase that occurred between 2005 and 2006, when the size of the largest container vessel jumped from 9,500 TEUs to 15,500 TEUs in a single year.

In short, beginning at about the time of the Commission's most recent review of the Consortia BER, an entire new category of very large container vessels has been built and delivered. These new vessels represent a major innovation in efficiency and air emissions reduction in the ocean transportation sector, but they also represent an operational challenge for the carriers that are bringing them to the market.

The primary reason that carriers have invested heavily in these large vessels is to reduce per-unit operating costs. Bunker fuel prices, which are the single greatest variable operating cost in liner shipping, have doubled between 2007 and the present.

In addition to the steady increase in bunker prices over the years, carriers have also seen increased fuel costs because of air emission control areas (ECAs) in Europe and North America. The low sulphur fuel required in these areas carries a price premium over heavy fuel oil (HFO). In 2015, the ECA sulphur limits will become stricter, which will increase costs further.

⁵ A "TEU" is a twenty-foot equivalent unit, which describes the size of the smallest standard shipping container in general use. Most containers are forty feet in length, and would therefore represent two TEUs.

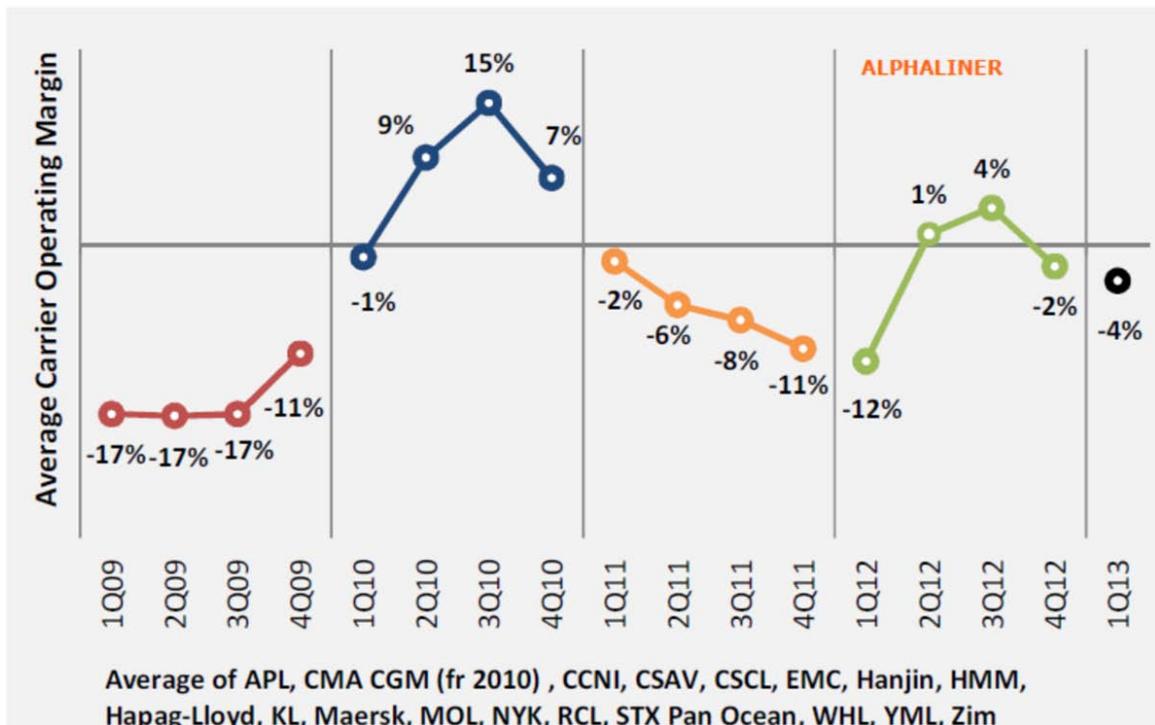
The current differential between HFO and the distillate fuel that would meet the 2015 ECA sulphur limits is approximately 30%. The greatest increase in fuel costs will occur when, pursuant to MARPOL Annex VI, the global fuel sulphur limit drops from 3.5% to 0.5% in 2020 or 2025, essentially requiring distillate fuel for all oceangoing ships worldwide. Based on current average fuel price differentials between HFO and distillate fuels, WSC has estimated that the increased cost of the global 0.5% sulphur limit may be in the range of €55-70 billion per year on a global basis for the worldwide fleet (all sectors). Those estimated increases are in addition to the ECA costs discussed above.

Under any scenario, fuel costs will rise substantially in the coming years, and those increased costs will continue to require continuous improvements in transport efficiency.

At the same time that fuel prices have increased substantially, freight rates have remained flat, meaning that carriers have effectively absorbed the increases in fuel costs. For example, an analysis by *Alphaliner* in May of this year concluded that average global container freight rates rose only 3% in the fifteen years between 1998 and 2013. Once those rates are adjusted for fuel price increases, the real rates have declined by over 15% during that period, according to the *Alphaliner* analysis. As one would expect, the combination of rising costs and falling rates in real terms has produced historically poor overall rates of return on investment in the liner shipping sector. The *Alphaliner* chart below plotting recent operating margins for carriers with public profit and loss information is indicative of the difficult economic environment in which liner shipping operates:

Chart of the week

Average carrier operating margin by quarter : 2009-2013



Source: Alphaliner Weekly Newsletter Volume 2013 Issue 23, June 3, 2013

In this context, the only recourse for carriers is to reduce costs if they are to maintain services. One of the primary strategies that carriers are pursuing to cut per-unit costs for transporting containers is to deploy larger vessels. On a per-slot basis, these vessels use substantially less fuel than older, smaller vessels, thus lowering per-unit costs and improving the overall efficiency of the transportation.

The equation of larger vessels delivering efficiency gains, however, only produces the desired result if those vessels' capacity is efficiently utilized to carry cargo. A 14,000 TEU ship burns less fuel on a per-unit basis than a 7,000 TEU ship, but it still burns more fuel overall. Thus, a 14,000 TEU ship that is half full is less efficient than a 7,000 TEU that is full. The utilization rate is critical to realizing the designed efficiency of the larger vessels. The use of consortia is necessary to capture the efficiency benefits of larger ships. In most cases carriers simply do not have enough cargo to fill ships of this size on their own. Vessel sharing allows carriers to more efficiently utilize these expensive large assets than they could do on their own. That fact is amplified by the "lumpy" nature of liner shipping capacity (i.e., that the smallest economically viable unit of supply is a "string" of enough vessels to provide weekly calls at each

port in a service rotation), a point that is discussed in more detail in the remainder of this section.

The operational case for sharing vessel assets through consortia is a simple one. As the industry has developed, there are many liner shipping companies that provide service on multiple trade lanes around the world. That many carriers operate in multiple trade lanes is the result of several factors. First, industry players naturally seek to grow their businesses by entering markets in which they see opportunity. Second, large international shipper customers often demand transportation on multiple routes. Third, participating in multiple trades provides market diversification for carriers, who can re-deploy assets from markets with low demand to markets with relatively higher demand as commercial conditions dictate.

If every liner operator needed to provide vessel capacity by itself on every trade in which it participated, there would either be a gross oversupply of capacity, thus making the services economically unsustainable, or a shortage of investment and fewer service providers. In short, in the absence of consortia, there would be fewer services and fewer competitors. It is difficult for carriers to provide individual services in major trade lanes in part because the smallest economically viable unit of supply is a vessel string – typically defined in the industry as the number of vessels necessary to provide a weekly service on a given route.

In the Trans-Atlantic, for example, vessel strings tend to consist of five or six vessels. On the North Asia to North Europe route, in comparison, typical strings run between 10 and 12 vessels. The number of vessels necessary to provide such a single, weekly service is the minimum number that must be deployed in order to enter a market. More realistically, a service provider (individual or consortium) in a major trade will have to deploy multiple strings in order to provide the fixed-day-of-the-week schedules required by many shippers.⁶ Thus, with prices for large, efficient vessels ranging from US\$125 million to US\$175 million each, the capital investment required for a substantial Asia-Europe service is between 5 and 8 billion U.S. dollars, an undertaking that few carriers could sustain individually. Absent the ability of carriers to share vessel space through consortia arrangements and thus to spread these investment

⁶ In addition to having a sufficient number of vessels to provide the type of service that shippers require, it is necessary that the vessels deployed on a given service be as close in size to one another as is feasible. That is the case because a given service will not be able to reliably handle cargo space demands if it calls a port one week with a 15,000 TEU vessel, and then calls the next week with a 5,000 TEU vessel. This need for a homogenous composition of vessel strings also complicates the investment and deployment challenges that carriers face. That complication has been exacerbated by the increased size disparity in the global fleet that has been caused by the relatively sudden introduction of very large ships, while at the same time there are many smaller ships in existence that will be commercially serviceable for many years to come.

loads, there would be fewer competitors in each market, inefficiently utilized ship capacity, or both. Both outcomes would result in higher prices and reduced services.

Carriers of all sizes can benefit from vessel sharing consortia. A larger carrier in a trade can order and deploy larger, more efficient ships with confidence that it can share the vessel assets in order to achieve superior capacity utilization. Smaller carriers that may not be able to afford the largest, most efficient assets may obtain the economic efficiencies of large vessels via vessel sharing consortia. New entrants will find an easier time to begin a new service by sharing vessels rather than having to finance a stand-alone service.⁷ The fact that consortia allow the maintenance of more competitors on more routes through the efficient use of vessel capacity and shared services has consistently been recognized by the Commission in enacting its prior and current Consortia BERs, and shippers similarly understand and support the existence of these arrangements as providing more choices and more competition than would exist in the absence of consortia.

With the recent and continuing introduction of very large container vessels into the liner trades, those benefits of consortia are amplified in today's market. In the current situation, in which rising fuel prices and the search for greater efficiencies through the use of larger vessels make consortia an even more important tool for the support of reliable and frequent transportation services, in the words of Article 2(2) of Council Regulation 246/2009 it is plainly not the case that "circumstances have changed with respect to any of the facts which were basic to [the] adoption" of the Consortia BER so as to warrant its repeal. To the contrary, to the extent that circumstances have changed, those changes reinforce the need to continue the Consortia BER in order to provide the legal certainty necessary to support the massive capital investments that carriers continue to make in order to provide modern, more efficient transportation services.

3. It is Legally Appropriate and Administratively Efficient for the Commission to Address the Specific Characteristics of Liner Shipping Consortia through the Consortia BER; the Horizontal Guidelines Would Be a Poor Substitute.

When viewed in the legal and economic context in which the Commission has always viewed the Consortia BER, today's challenging economic realities make a strong case for continuation of the Consortia BER. Notwithstanding that fact, WSC, ECSA, and ICS are aware that the Commission has stated a general preference for reducing or eliminating sector-specific block exemptions. We understand that the basis of this policy preference is to ensure that the

⁷ While there are no regulatory barriers to entry in liner shipping, consortia reduce the risk that ships' capital and operating costs become barriers to entry.

competition laws are applied evenly across economic sectors. It can hardly be argued that even application of the law is not an appropriate goal, and we do not so argue here. However, the TFEU itself recognizes that appropriate application of the law sometimes requires that the Commission provide specific guidance to individual sectors in order to ensure clarity and compliance without undue administrative complexity. Thus, for example, TFEU Article 103(2) states in relevant part that:

“(2) The regulations or directives referred to in paragraph 1 shall be designed in particular:

...

(b) to lay down detailed rules for the application of Article 101(3), taking into account the need to ensure effective supervision on the one hand, and to simplify administration to the greatest extent possible on the other;

(c) to define, if need be, in the various branches of the economy, the scope of the provisions of Articles 101 and 102” (emphasis added)

In May of this year, in the context of an airline alliance investigation, the Commission itself noted the need to take into consideration the attributes of a particular industry sector in applying the competition rules to horizontal cooperations. Thus, in IP/13/456 in Case number 39595, concerning Star Alliance members Air Canada, United and Lufthansa, the Commission stated:

“In light of the specific characteristics of the aviation industry and of the particular circumstances of this case, the Commission considered it appropriate to broaden the existing test for assessing efficiencies, contained in its Guidelines for application of Article 101(3) of the Treaty on the Functioning of the European Union (TFEU).” (emphasis added)

The Commission’s express recognition that there are specific characteristics with respect to certain industries that affect the proper application of the competition laws, as well as the Commission’s willingness to be transparent about how it will take those industry-specific characteristics into account when applying the laws, are to be commended. Undertakings will have higher compliance rates, and both the Commission and industry will have lower administrative burdens, when the rules are clear. Because virtually all liner shipping consortia share a core set of common characteristics, they represent a type of horizontal cooperation that is ideally suited to uniform regulatory guidance in the form of a block exemption.

It is a fundamental premise in competition law that the facts matter. The Horizontal Guidelines, for example, state at paragraph 7 that “[e]ach case must be assessed on the basis of its own facts, which may require a flexible application of these guidelines.” The history of the Consortia BER demonstrates that there is a core, consistent set of facts with respect to liner shipping consortia that can be identified, analyzed, and codified within the guidance provided by the Consortia BER. By the terms of the Consortia BER itself, those consortia that benefit from the BER are “limited to those agreements for which it can be assumed with a sufficient degree of certainty that they satisfy the conditions of Article 81(3) [101(3)] of the Treaty.”⁸

Codification of this common Commission and industry knowledge and experience through a carefully tailored BER does not constitute “special treatment” for the liner industry sector. Instead, it is a means by which the industry, its customers, and the Commission may share a common understanding of the rules under which consortia are to operate.⁹ By definition, then, the Consortia BER does not change the application of the competition laws to the liner shipping industry; it simply makes that application in a particular context much clearer than it otherwise would be. WSC, ECSA, and ICS would be at a loss to understand what policy objective would be served by intentionally rejecting that clarity – a clarity that has been built through almost twenty years of experience, analysis, and refinement of the Consortia BER. Having finally arrived at a Consortia BER that is in all material respects exceedingly well fit for purpose, what would be the benefit – to anyone – of abandoning that guidance?

⁸ Commission Regulation No 906/2009, recital 4.

⁹ It is the combination of the fact that the liner shipping industry relies substantially on consortia to maintain the level of service that shippers demand and the fact that there is a core set of consortia characteristics that recur frequently that makes consortia arrangements appropriate for treatment by block exemption. This differs, for example, from the situation with airline alliances. There, differences in access to landing slots at various airports cause the competitive implications of airline alliances to vary substantially depending on the routes served and the slots held by the participants. In addition, members of airline alliances frequently agree on rate structures, a practice that adds a potentially anti-competitive element that is not present in liner shipping consortia, which are purely operational arrangements. Although the Commission has noted recently the need to recognize sector-specific aspects of airline alliances, the variances in airline alliances make it impractical to do so through a block exemption. Liner shipping consortia, in contrast, because their elements that are related to competition are reasonably consistent across consortia, are appropriate for treatment on a unitary basis through a block exemption. Both approaches are sector-specific, but the block exemption approach, where conditions are sufficiently uniform to make it feasible (as with consortia), provides greater clarity and consistency to a greater number of industry participants without the uncertainty that comes with having the boundaries of acceptable cooperation emerge through years of individual investigations. Put differently, the Consortia BER is simply a more efficient and effective means of applying the law to the particular facts of a specific sector.

The alternative to retaining the Consortia BER, with its well defined and easily understood boundaries, is to regress to reliance upon the general Horizontal Guidelines. As noted above, the immediate effect of repealing the BER would be to replace clarity with uncertainty, without furthering any legitimate competition law policy. As the Horizontal Guidelines make clear, those guidelines are a starting point, not a source of answers to specific questions:

“Given the potentially large number of types and combinations of horizontal co-operation and market circumstances in which they operate, it is difficult to provide specific answers for every possible scenario. These guidelines will nevertheless assist businesses in assessing the compatibility of an individual co-operation agreement with Article 101. Those criteria do not, however, constitute a ‘checklist’ which can be applied mechanically. Each case must be assessed on the basis of its own facts, which may require a flexible application of these guidelines.” (Horizontal Guidelines, Paragraph 7)

Contrast this general approach with the very specific provisions laid down in the Consortia BER. The first contrast between the BER and the HG is applicability. Consortia do not fit well with the categories of agreements covered by the HG. Perhaps the closest match is under Production Agreements, but the fit is imperfect at best, and imperfect in ways that would lead to analytical difficulties if the BER were replaced with the HG. First, the production agreements article of the HG is designed primarily for undertakings in which one or both parties give up their individual means of production and either jointly operate a production facility, rely on third parties, or rely on a single party for the production needs of both parties. See HG paras. 150-152. None of those scenarios accurately describes what happens in a typical liner shipping consortium, in which the parties each maintain their own vessel production by purchasing or chartering ships, and the parties also retain capital and operating cost responsibility for their individual ships.

Contrast that retention of individual cost structure for ship operations with the production agreement Example 1 following paragraph 187 of the HG. In that example, the primary concern is that the parties have abandoned their individual production plants, and have opened a joint plant in a business in which production costs are a major part of variable costs. The example concludes that the commonality of a major variable cost could lead to a direct limitation of competition between the parties. That conclusion – and most importantly the assumptions that lead to that conclusion – are not applicable to liner shipping consortia, because consortia do not lead to commonality with respect to vessel costs, which are the predominant costs in the industry. Moreover, unlike the production agreements described in paragraph 160 of the HG, consortia that fall within the BER may not involve the joint setting of sales prices.

The assumptions of Example 2 following para. 188 of the HG are equally inapplicable to liner consortia for the same reasons as the assumptions of Example 1 are inapplicable, but Example 2 could lead to substantial confusion if the Consortia BER were repealed and the HG became the leading guidance for consortia. Example 2 concludes that a production agreement between Companies A and B, where Company B already has a production agreement with Company D, would increase the likelihood of collusive behavior and result in a reduction of competition. That “likely” outcome predicted by the example is in direct tension with a very conscious and well-considered decision that the Commission made when it last amended the Consortia BER in 2009. Specifically, the Commission, for the purposes of calculating the applicability of the 30% market share threshold, had considered aggregating the market shares of all consortia in a market that were linked by any overlapping membership. Finding that such an approach would not reflect the reality of how consortia operate (i.e., that consortia are subject to competition among the members of a single consortia, as well as competition from outside), the Commission instead retained a simple “one consortia” market share calculation. The HG example employs an “aggregation by association” market share/market power analysis that is substantially at odds with how the issue has been addressed in the Consortia BER. That divergence would be multiplied if the 30% market share safe harbor threshold of the BER were replaced with the indicative 20% market share provision in the HG production agreement provisions.¹⁰

In addition to the fact that liner shipping consortia do not meet the definitions of HG production agreements; in addition to the fact that the HG assumptions about how production agreements affect competition do not square with the reality of how consortia function; and in addition to the fact that those inapplicable definitional and operational assumptions cause the HG production agreement examples to render results that are contrary to the outcomes under the BER, there is the issue of specificity.

The Consortia BER, which as the Commission notes in Question 47 of its RFI has been considerably simplified and streamlined during the years of its existence, provides clear and easily applied rules that are well understood in the industry, including by the operational managers who are most involved in evaluating the efficiencies available from potential consortia arrangements and who may not be conversant with general European competition law (but who are fully aware of the BER). That clarity not only provides legal certainty and ease of application within individual companies; it also provides a “common language” and common

¹⁰ We recognize that there are and will continue to be consortia that fall outside of the BER either because of their market share or because of some other attribute, and that those agreements must be self-assessed. The existence of such agreements does not affect the utility of the Consortia BER for the majority of consortia agreements that fall within the BER, and indeed the BER provides an important touchstone for self-assessment of agreements that do not fall wholly within its terms.

understanding among companies contemplating or operating consortia, including among the lawyers advising those companies. As discussed further in the next section, the ability of two or more parties contemplating a consortium agreement to limit legal risk allows more fluidity in the formation, amendment, and dissolution of consortia, and thus makes those arrangements more efficient.

Application of the Horizontal Guidelines provisions to the specific circumstances of consortia could presumably be adapted after a substantial period of uncertainty and perhaps litigation, but it is difficult to see the policy rationale for trying to make consortia, for which the HG were not drafted, fit the HG mold. This is a very different situation than the one that industry and the Commission recently faced when the Commission considered whether to allow the Maritime Guidelines to lapse. In that instance, the revised HG did fit the realities of the liner shipping sector, and there was no practical need for sector-specific guidance. There, the industry agreed with the Commission that the Maritime Guidelines could lapse without causing confusion or operational disruption. That simply is not the case with respect to the Consortia BER. Here industry urges continuation of the BER not as a matter of some principle that the sector must always have individual guidance, but rather because in this instance the Consortia BER is a far more appropriate, accurate, and predictable means of ensuring compliance without uncertainty, commercial disruption, or litigation.

4. Increasing Uncertainty by Repealing the Consortia BER Would Reduce Innovation and Competition By Making Consortia Less Attractive Generally and by Discouraging Amendments to Consortia Arrangements in Response to Market Conditions.

The presence or absence of legal certainty has real economic effects. It is one thing to engage legal counsel to provide an approximation of relative legal risk – the self-assessment model. It is quite another thing to know that, so long as one falls within the boundaries of the BER, one may enter into a business arrangement knowing that there is little competition law risk. The former situation introduces an element of risk that becomes a factor in deciding whether to enter into a particular business arrangement. Sometimes that risk will be deemed acceptable; sometimes it will not. That means under the first scenario (self-assessment in the absence of a BER) that there will be some cooperations – cooperations that could provide market efficiencies and tangible benefits to shippers – that will be foregone because carriers would not be willing to accept the legal risk that an arrangement might be challenged in the future.

Under the Consortia BER, in contrast, for those arrangements that fall within its terms, legal risk is eliminated. That means that potential consortia arrangements, or amendments to

those arrangements (including terminating those arrangements and entering into different ones) can be evaluated solely on their operational merits. Instead of wondering whether the potential cooperation may be subject to legal risk, the parties can focus on whether the proposed arrangement maximizes productive use of assets, reduces costs, and better serves customers.

From an economic perspective, removing legal risk reduces transaction costs. Those avoided costs obviously include the monetary costs that would be incurred in engaging lawyers and perhaps economists in order to conduct self-assessments in the absence of the Consortia BER. A more important cost that would be imposed if the Consortia BER were repealed, however, would be the chilling effect on innovation. That chilling effect could take several forms. It could result in some carriers foregoing consortia opportunities in the European trades (for example, choosing to forego a Mediterranean port call on a service between Asia and the U.S. via the Suez Canal). Increased legal risk may discourage amendments to existing consortia (which would have been in place without challenge for some period before new opportunities were considered). That increased legal risk could also encourage carriers to remain in an existing consortium rather than form a new consortium, even when changing consortia would make operational and economic sense and would meet more closely the customers' needs.

The potential chilling effect on innovation from increasing legal risk is of particular concern with respect to shipping, which is the original international business. Even a cursory look at the alliances on the major European trades reveals that the companies involved are based in a broad range of countries throughout the world. Although some of those home countries (for example, those in the EU) have a common approach to competition law, that is not the case for many others. From a cultural and legal perspective, therefore, many consortia participants do not start with a common understanding with respect to competition law. Carriers will not form consortia that they cannot evaluate for legal risk, and they cannot evaluate the legal risk if the rules are not clear. Today the rules are uniform and clear worldwide; consortia are exempted from or accepted by regulation as being consistent with competition laws worldwide. Without the Consortia BER, the lack of a common legal understanding would impede the formation, amendment, and dissolution of consortia in response to market conditions and customer needs, thus undermining the benefits that consortia provide for carriers as well as for shippers and increasing the enforcement burden on the Commission.

The likelihood that the formation, amendment, and dissolution of consortia would become less fluid, and thus that their innovation and efficiency benefits would be reduced if the Consortia BER were repealed, parallels one of the Commission's concerns that is reflected

in the BER today. That Commission concern is with the length of lock-in periods. While recognizing that lock-in periods are necessary to provide carriers with some investment certainty, the Commission has reasoned that if lock-in periods are too long, that could stifle innovation by preventing carriers from restructuring their services in response to new market opportunities (for example by terminating existing consortia and forming new ones). Carriers and the Commission may disagree as to where the balance should be struck with respect to lock-in periods. The point here, however, is that the reluctance to make changes to consortia associated with the heightened legal risk that would result from repeal of the BER would have the same effect as an artificially long lock-in period; that is, it would become safer, and thus more likely, that carriers in a consortium would remain in that consortium rather than considering amendments or the formation of different consortia that could be more efficient. That would be a poor policy outcome.

With respect to the point that legal certainty supports fluidity in the formation, amendment, and dissolution of consortia in response to market demands, it is also important to emphasize that virtually every major trading nation in the world either exempts consortia from its competition laws or has made it clear by statute or regulation that consortia of the sort covered by the Consortia BER are legally permissible. If Europe were to repeal the Consortia BER, it would be alone in removing that legal certainty. Although it would be an overstatement to suggest that consortia in Europe would disappear if the BER were repealed, it would also be an overstatement to say that such a repeal would have no negative effect. Over time, it would have a negative effect, reducing efficiency and competition by discouraging the formation of consortia generally and by disfavoring changes to existing arrangements, even if such changes would be more economically beneficial for carriers, shippers, and the international trade of the European Union. Given the importance of maritime shipping to world trade, such an outcome would be detrimental to the European economy.

5. Conclusion

By the time the current version of the Consortia BER expires in 2015, the BER will have provided clear, practical, and efficient guidance to the liner shipping industry, its customers, and regulators for twenty years. Especially with the modernization of the BER in 2009, the regulation provides useful legal certainty for industry while at the same time eliminating concern that a consortium operating within the boundaries of the BER could pose a credible threat to competition. As such, the Consortia BER well fulfills the Article 103(2) TFEU instruction that competition regulations are to be crafted so as “to ensure effective supervision on the one hand, and to simplify administration to the greatest extent possible on the other....”

It is widely agreed that liner shipping consortia increase competition, expand service offerings, and encourage technical innovation. Those benefits of consortia are especially

important today in the face of rising fuel prices, stagnant freight rates, the mandate to reduce air emissions, and economic pressures on carriers to cut costs and maximize the efficient utilization of vessel assets while maintaining quality service. The Consortia BER, by removing legal risk from the mix of factors that must be evaluated by carriers considering consortia, allows those carriers to enter into, amend, and leave consortia based on grounds of economic efficiency, not legal risk avoidance. That in turn, makes consortia more fluid, more efficient, and more responsive to market forces. Consortia are an integral part of the liner shipping industry. But they best serve the interests of all interested parties – shippers, carriers, regulators and the public – when the rules that govern them are plain and transparent. The Consortia BER provides that clarity and transparency, and it should be extended for at least an additional five years.

The World Shipping Council, the European Community Shipowners' Associations, and the International Chamber of Shipping appreciate the opportunity to share these preliminary thoughts with the Commission as the Commission begins its review of the Consortia BER. We are at your disposal to discuss any aspect of this issue, and we welcome an open dialogue as your review continues.