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Protectionism in the Age of Austerity – A Further Unlevelling of the Playing Field?

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PROTECTIONISM IN THE AGE OF AUSTERITY – A FURTHER UNLEVELLING OF THE PLAYING FIELD?

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I. INTRODUCTION – ARE THE CONCERNS RAISED IN 2006 STILL VALID?

In our 2006 article,[1] we highlighted an emerging wave of interventionism by EU Member States that manifested itself in a variety of protectionist measures designed to prevent foreign takeovers and promote national champions. The European Commission had initiated infringement proceedings against several Member States that had invoked industry-specific national regulations in an attempt to prevent takeovers of national companies by foreign competitors, when those transactions had already been cleared unconditionally by the Commission under its exclusive jurisdiction under the EU Merger Regulation ("EUMR").[2]

In a number of further cases, the Commission had been powerless to prevent the (attempted) creation of national champions, as it was unable to assert its jurisdiction over mergers between largely domestic players that were subject to the EUMR's "two-thirds rule."[3] Member States were criticized for applying public interest considerations that were unrelated to competition policy to clear a merger creating a national champion.[4]

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1 Alex Nourry & Nelson Jung, *EU State Measures against Foreign Takeovers: "Economic Patriotism" in All But Name,* 2(2) COMP. POL'Y INT'L 99 (2006).

2 *See, e.g.,* Case COMP/M.4110, E.ON/Endesa, 2006 O.J. (C 114), Case COMP/M.4249, Abertis/Autostrade, 2006 O.J. (C 205), and Case COMP/M.3894, Unicredito/HVB, 2005 O.J. (C 235).

3 Where each of the parties to the concentration achieves more than two-thirds of its aggregate Community turnover within one and the same Member State, it is for that Member State's national competition authority to assess the merger, even when such mergers have cross-border effects. *See* Article 1(2) of Regulation 139/2004 (EUMR).

4 *See, e.g.,* Case COMP/M.3986, Gas Natural/Endesa, C (2005) 4468); Lettre du 28 janvier 2003 du ministre de l'économie, des finances et de l'industrie au conseil de la société Crédit Agricole relative à une concentration dans le secteur bancaire, BOCCRF, Nº 5, 4 mai 2004 p. 364; the Bundeskartellamt decision to block the *E.ON/ Ruhrgas* merger (*Bundeskartellamt WuW/E DE-V 511-525 – E.ON/Ruhrgas*), and; the ministerial authorization overruling the Bundeskartellamt on the grounds of public interest (*WuW/E DE-V 573-598 – E.ON Ruhrgas* and *WuW/E DE-V 643-653 – E.ON/ Ruhrgas*).

The Commission's recent decisional practice demonstrates its continued resolve to block the creation of national—or even European—champions where it considers that such mergers would significantly impede effective competition.

Against this background, we examined the compatibility of a range of protectionist State measures with the Internal Market and queried whether the overriding interests of the Internal Market would justify the abolition of the two-thirds rule.[5]

Nearly six years later, in the wake of a global financial crisis that gives rise to protectionist temptations once again, the rule is still in place despite mounting criticism.[6] The economic crisis and the often painful adjustments arising from the ensuing debt consolidation process provide a seemingly compelling justification for some governments to resort to interventionist industrial policies based on the belief that governments can "pick winners" by creating or protecting national champions.

However, the Commission's recent decisional practice demonstrates its continued resolve to block the creation of national—or even European—champions where it considers that such mergers would significantly impede effective competition.

Last year, the Commission blocked the proposed merger between Olympic Air and Aegean Airlines, stating that it would have resulted in a quasi-monopoly of the Greek air transport market.[7] Despite the fact that the merging parties operate primarily in (and out of) Greece, the Commission was able to establish jurisdiction over this transaction without the two-thirds rule coming into play. Had this transaction occurred in a different sector where the bulk of each

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[5] Alternately, we considered that the two-thirds rule could be included as an additional ground for the referral of mergers back to Member States under Article 9(2)(a) EUMR. We argued that this would allow the Commission to assess the cross-border impact of any merger, even when it concerns essentially domestic players, in exercising its discretion to accede to a Member State request for referral back. *See* Nourry & Jung, *supra* note 2, at 127.

[6] The two-thirds rule has not been abolished despite the Commission's finding in its 2009 report on the functioning of the EUMR that "public interest considerations other than competition policy have been applied in a number of cases falling under this threshold to authorise mergers which could have given rise to competition concerns" and that, therefore, "the present form of the two-thirds rule merits further consideration." *See Communication from the Commission to the Council: Report on the functioning of Regulation 139/2004*, COM (2009) 281 final (June 18, 2009). In 2010, Mario Monti called for improved cooperation between national competition authorities to ensure procedural and substantive convergence between regulators at both the national and the EU level. Monti also proposed abolishing the two-thirds rule. *See* Mario Monti, *A New Strategy for the Single Market*, Report to the President of the European Commission (May 9, 2010).

[7] Case COMP/M.5830, Olympic/Aegean Airlines, 2010 O.J. (C 174) 8. This was the Commission's second prohibition decision in an airline case. The first, in 2007, was a prohibition of the proposed acquisition of Aer Lingus by Ryanair (COMP/M.4439, Ryanair/Aer Lingus, 2006 O.J. (C 274) 10), which also amounted to a merger of two airlines based at the same "home" airport in the national capital.

party's turnover was allocated to their home jurisdiction, the two-thirds rule may have resulted in a different jurisdictional, and possibly substantive, outcome.[8]

More recently, the Commission blocked the merger between NYSE Euronext and Deutsche Börse.[9] Commissioner Joaquín Almunia argued that the merger would have created a near-monopoly in crucial markets to the detriment of thousands of EU companies and harmed innovation in financial services.[10] However, it has been reported that the decision to block the merger was signed off by the Commission after an unusually fierce debate among the 27 Commissioners, where a minority supposedly challenged the verdict because it hindered the emergence of European champions in a global market.[11]

The Commission's quest for an open and contestable Internal Market in the face of resurfacing protectionist tendencies is, of course, not confined to the exercise of its powers under the EUMR. Its agenda to create and maintain a level playing field by tackling protectionist measures is also illustrated by its infringement proceedings against Portugal's "golden shares" and other special rights in GALP Energia, Energias de Portugal ("EDP") and Portugal Telecom.[12]

Overall, the Commission continues to act as a guardian of the functioning of the Internal Market by seeking to ensure that unduly interventionist national industrial policies do not override competition policy objectives.

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[8] It is not clear from publicly available information whether a different method of geographical allocation of turnover in Olympic/Aegean Airlines may have established the Greek competition authority's jurisdiction over this transaction on the basis of the two-thirds rule. In general, it is not inconceivable that different approaches to the geographic allocation of turnover in this specific sector may alter the jurisdictional analysis such that the two-thirds rule could establish jurisdiction of a national competition authority. In previous cases, the Commission has considered various different approaches to turnover allocation in airline mergers, including the country of destination method (allocating the turnover to the country of final destination); the 50/50 method (splitting the turnover between the country of origin and the country of final destination); the point of sale method (allocating the turnover to the country where the ticket sale occurred) and the place of departure method (allocating the revenue from a flight to the Member State where the place of departure of the flight is located – for round trips, this could be done by either splitting the two one-way flights of round trip tickets bought at the same time or allocating the entire turnover to the place of departure where the original outbound flight is located). For a more detailed assessment of each of these methods, see Case COMP/M.4439, Ryanair/Aer Lingus, ¶ 18 et seq.

[9] Case COMP/M.6166, Deutsche Börse/NYSE Euronext, 2012 O.J. (C 440).

[10] Joaquín Almunia, Vice President of the European Commission responsible for Competition Policy, Speech at the Concurrences Conference: Industrial Policy and Competition Policy: Quo Vadis Europa?, New Frontiers of Antitrust 2012 (Feb. 10, 2012), *available at* http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/12/83&format=HTML&aged=0&language=EN&guiLanguage=en.

[11] *See* Alex Barker, Jeremy Grant & James Wilson, *Deutsche Börse-NYSE merger blocked*, Fin. Times, Feb. 1, 2012.

[12] *See* Cases C-212/09, Commission v Portuguese Republic, 2012 O.J. (C 25) 4; C-543/08, Commission v Portuguese Republic, 2011 O.J. (C 13) 5, and; C-171/08, Commission v Portuguese Republic, 2010 O.J. (C 234) 5.

II. STATE-OWNED ENTERPRISES: THE RISE OF STATE CAPITALISM IN RESPONSE TO THE FINANCIAL CRISIS

In reality, SOEs often enjoy certain privileges and immunities that are not necessarily available to their privately-owned competitors.

Beyond the European Union, industrial policies fostering national champions are becoming increasingly popular in the aftermath of the financial crisis, primarily in the guise of State-Owned Enterprises ("SOEs") in emerging economies.[13]

According to recent reports, state-backed companies account for 80 percent of the value of China's stock market and 62 percent of Russia's.[14] Overall, they accounted for a third of the emerging world's foreign direct investment between 2003 and 2010.[15]

One may therefore query what impact the rise of SOEs and state-directed capitalism will have on the competitive landscape globally, irrespective of the extent to which EU policies continue to embrace the concept of a level playing field. The concept of competitive neutrality requires that SOEs should not enjoy net competitive advantages over their private sector competitors simply by virtue of public sector ownership. Although, in principle, the Organisation for Economic Co-operation and Development ("OECD") Principles of Corporate Governance recommend a level playing field,[16] in reality, SOEs often enjoy certain privileges and immunities that are not necessarily available to their privately-owned competitors.[17]

The trend towards an increasingly visible hand gives rise to a number of challenges from an antitrust perspective, not least in respect of merger control where SOEs are taking over foreign

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13 China, for instance, has promoted its strategic industries through a variety of measures, including subsidies, fiscal incentives, export restrictions, trading rights authorizations, local content rules, low wages and labor standards. The Chinese model of capitalism, dubbed the "Beijing consensus," is seen as more successful and more stable by other emerging economies who appear to be gradually abandoning (neo)liberal theories in favor of industrial policy. *See* Damien Geradin & Ianis Girgenson, *Industrial Policy and European Merger Control – A Reassessment* 17 (TILEC Discussion Paper No. 2011-053). *See also* Joe Leahy, *Brazil looks to China for Industrial Policy*, Fin. Times, Apr. 11, 2011. The Brazilian government, which embraced privatization in the 1990s, is now interfering with companies like Vale and Petrobras, and compelling smaller companies to merge to form national champions.

14 *See The rise of state capitalism*, The Economist, Jan. 21, 2012, *available at* http://www.economist.com/node/21543160.

15 *Id*.

16 *See* OECD, OECD Guidelines on Corporate Governance of State-Owned Enterprises (2005), *available at* http://www.oecd.org/dataoecd/46/51/34803211.pdf.

17 For a more detailed assessment of basic competitive advantages of SOEs, see Antonio Capobianco & Hans Christiansen, *Competitive Neutrality and State-Owned Enterprises: Challenges and Policy Options* (OECD Corporate Governance Working Papers No. 1, 2011), *available at* http://www.oecd.org/dataoecd/29/43/46452890.pdf.

companies.[18] In recent decisions where the Commission scrutinized takeovers by SOEs, the Commission assessed whether the SOE involved was an independent economic entity or whether it belonged to a wider economic group, including other enterprises over which the State (in these cases, the Republic of China) enjoyed decisive influence.[19] In its analysis, the Commission pointed out that this type of assessment was required regardless of whether the ultimate parent entity was state-owned or privately owned, thereby reinforcing the concept of competitive neutrality.

Encouragingly, there are recent signs that emerging economies are also taking competitive neutrality considerations seriously in applying their respective competition laws. Developments in China, for instance, indicate that domestic SOEs are not immune from antitrust scrutiny under the Anti-Monopoly Law.[20]

III. FOREIGN INVESTMENT RULES REMAIN PROBLEMATIC

Although there may be greater convergence in the application of national competition laws—insofar as national governments increasingly follow recommendations made by the OECD and the International Competition Network—the risk of foreign investment rules providing a framework to pursue a more protectionist agenda remains and appears to be growing in importance. In March 2012, French President Nicolas Sarkozy stepped up his campaign for a "Buy European Act" for public contracts, insisting that there was a need to protect industry from "savage" trade competition, and threatening to act unilaterally if the European Union failed to take action.[21] In the same week, Brazil's finance minister Guido Mantega insisted that Brazil "cannot keep [its] borders completely free while others are using non-competitive

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[18] Other challenges relate to certain pricing practices by SOEs with market power, including predatory pricing or cross-subsidisation.

[19] *See* Cases COMP/M.6082, China National Bluestar/Elkem, 2011 O.J. (C 274) 3 and COMP/M.6113, DSM/Sinochem/JV, 2011 O.J. (C 177) 2.

[20] In China's first antitrust investigation of its own SOEs, the National Development and Reform Commission is currently assessing how to proceed against two telecom companies. China Telecom and China Unicom are reportedly accused of employing anti-competitive practices to maintain their dominant position in the broadband market. The applicability of China's Anti-Monopoly Law to its own SOEs is further evidenced by the Ministry of Commerce's recent decision to impose conditions on a transaction involving a joint venture between General Electric and the state-owned Shenhua Group.

[21] *See* Hugh Carnegy, *Sarkozy appeals to his populist base,* Fin. Times, Mar. 16, 2012, *available at* http://www.ft.com/intl/cms/s/0/f1455ffa-6f76-11e1-9c57-00144feab49a.html.

mechanisms" and warned that the country will be taking "defensive measures."[22] Other countries, including Germany and Austria, have recently introduced foreign investment rules that create new barriers to foreign investors seeking to acquire stakes in domestic companies operating in a variety of sectors.[23]

Foreign investment legislation allows governments to block transactions that do not have an adverse impact on competition. Such legislation often lacks a clear definition or guidelines against which a "national interest" criterion could be measured, making it more difficult to predict whether or not a proposed transaction might be blocked.[24] This resulting uncertainty may in and of itself dissuade pro-competitive transactions giving rise to consumer welfare-enhancing effects. In Russia, for example, it has become difficult for foreign investors to determine the scope of application of the law relating to foreign investment in companies operating in strategic sectors. This is partly because a transaction may be subject to clearance even if the relevant entity's principal operations do not concern the strategic sectors, since ancillary involvement is sufficient to trigger the operation of that law.[25] While very few transactions have been blocked by the clearing committee,[26] the burdensome approval process and the significant delays caused by it are a major concern for investors.

A high-profile example of what critics have called "resource nationalism"[27] involved BHP Billiton's unsolicited bid for Canada's Potash Corporation of Saskatchewan Inc. Canada eventually blocked the $39 billion deal under its foreign investment laws on the grounds

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[22] *See* Leahy, *supra* note 13.

[23] Under the Austrian Foreign Trade Act 2011 (a law analogous to the one establishing the German regime in 2009), companies operating in areas of internal and external security (defense equipment industry, security services) or general public services, including social security (particularly hospitals, rescue services, fire brigades, energy or water supply, telecommunication services, traffic or education) shall be protected against foreign takeovers by an approval to be issued by the Federal Minister for Economy, Family and Youth.

[24] *See*, *e.g.*, Russia's *Federal Law № 57-FZ, On the procedure of foreign investment in companies having strategic significance for the preservation of national defence and state security*, passed on May 5, 2008 and published in the Rossiiskaya Gazeta on May 7, 2008. The text of the law (in Russian) is available at http://www.rg.ru/2008/05/07/investicii-fz-dok.html.

[25] *See A Legal Overview to Foreign Investments in Russia's Strategic Sectors*, Clifford Chance Client Briefing, Mar. 2011, *available at* http://www.cliffordchance.com/publicationviews/publications/2011/03/a_legal_overviewtoforeigninvestmentsi.html.

[26] In 2010, for example, the clearing committee considered 57 merger applications from foreign investors, clearing 44 of these outright, permitting a further 4 mergers after the imposition of certain conditions and blocking just 3 applications. *See* OECD, 2010 Annual Report on Competition Policy Developments in the Russian Federation, June 15, 2011, *available at* http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=DAF/COMP/AR(2011)21&docLanguage=En.

[27] *See Canada must avoid prairie populism*, Fin. Times, Oct. 25, 2010, *available at* http://www.ft.com/intl/cms/s/0/6bc935dc-e06a-11df-99a3-00144feabdc0.html.

that it would not provide a "net benefit" to Canada.[28] Similarly, in April 2011, Singapore Exchange's A$8.4 billion bid for the Australian Securities Exchange was rejected, with Australian officials commenting that the deal was "not in Australia's national interest" and that the acquisition would only be justifiable "if there were very substantial benefits" such as "greatly enhanced opportunities for Australian businesses and investors to access capital markets."[29]

In March 2012, the Indonesian government issued a decree that will prevent foreign companies from owning more than 49 percent of certain mines; Indonesia is the world's largest tin producer, and a leading exporter of coal, precious metals and other minerals.[30] Similar protectionist measures are being adopted by many African states with substantial mining industries. In Zimbabwe, the government's "indigenization" policy has gone one step further by forcing foreign companies to give a 51 percent share to Zimbabwean nationals, without compensation.[31] The most recent example of "resource nationalism" is Argentina's expropriation of 51 percent of YPF shares owned by the Spanish company Repsol, which is highlighted by the European Commission in its latest Report on Potentially Trade Restrictive Measures as part of a rising trend of trade-related restrictive measures covering foreign direct investment amongst the EU's main trading partners, including the G20 countries.[32]

IV. JUST HOW LEVEL WILL THE PLAYING FIELD BE?

Mario Monti noted in his report on a new strategy for the Single Market that "Europe needs an industrial policy that does not conflict, rather builds on its competition rules."[33] He added that competition rules did not stand in the way of the European companies'

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[28] *See* Bernard Simon, Helen Thomas & William MacNamara, *Canada rejects BHP bid for Potash*, Fin. Times, Nov. 4, 2010, *available at* http://www.ft.com/cms/s/0/7ec4f380-e798-11df-8ade-00144feab49a.html#axzz1r58MtV1t.

[29] *See* Peter Smith, *Australia confirms rejection of SGX-ASX deal*, Fin. Times, Apr. 8, 2011, *available at* http://www.ft.com/intl/cms/s/0/f2809c78-6184-11e0-a315-00144feab49a.html.

[30] *See* Sarah Mishkin & Helen Thomas, *Indonesia limits foreign ownership of mines*, Fin. Times, Mar. 7, 2012, *available at* http://www.ft.com/intl/cms/s/0/e9d9e570-684f-11e1-a6cc-00144feabdc0.html.

[31] *See Wish you were mine*, The Economist, Feb. 11, 2012, *available at* http://www.economist.com/node/21547285.

[32] European Commission Directorate-General for Trade, Ninth Report on Potentially Trade Restrictive Measures identified in the context of the financial and economic crisis, September 2011 – 1 May 2012, June 6, 2012.

[33] *See* Mario Monti, *A New Strategy for the Single Market: At the Service of Europe's Economy and Society*, Report to the President of the European Commission, May 9, 2010, *available at* http://ec.europa.eu/bepa/pdf/monti_report_final_10_05_2010_en.pdf.

Rather than resorting to protectionist industrial policies in a political knee-jerk reaction to an economic crisis, in the long run, creating an environment that stimulates competition on the merits and removes barriers to expansion and growth is indeed more likely to benefit consumer welfare.

search for the best scale and size to compete globally, citing the European Aeronautic Defence and Space Company ("EADS") as an example.

Rather than resorting to protectionist industrial policies in a political knee-jerk reaction to an economic crisis, in the long run, creating an environment that stimulates competition on the merits and removes barriers to expansion and growth is indeed more likely to benefit consumer welfare. By contrast, shielding domestic companies from competition is more likely to leave them underprepared for global competition than to truly assist them, let alone the economy overall.

The Commission's recently-announced proposal to allow local authorities to dismiss tenders from countries that discriminate against EU-based companies[34] are, however, difficult to reconcile with Monti's recommendations. The Commission qualified the proposal by specifying that foreign bidders could not be excluded from the tender process without the Commission's prior approval[35] and that it is intended to encourage others to open their markets,[36] emphasizing that "Europe is and will remain open for business."

Nevertheless, criticisms have been levied against the proposal on several levels: (i) a "protectionist signal" of this kind would undermine the EU's credibility as it seeks to eliminate protectionist measures elsewhere; (ii) the measure could trigger retaliatory action from foreign governments, which could potentially cause further harm to EU businesses, and; (iii) the principal aim of public procurement in obtaining "value for money" for the taxpayer would be undermined if certain bidders were eliminated by reason of the nationality of their incorporation.[37]

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[34] *Commission Proposal for a Regulation of the European Parliament and of the Council on the access of third-country goods and services to the Union's internal market in public procurement and procedures supporting negotiations on access of Union goods and services to the public procurement markets of third countries,* COM (2012) 124 final (Mar. 21, 2012), *available at* http://ec.europa.eu/internal_market/publicprocurement/docs/international_access/COM2012_124_en.pdf.

[35] The Commission also specified that contracts under €5 million would remain open to all bidders.

[36] Michael Barnier, the single market commissioner, has argued that European companies lose roughly €12 billion a year in export sales due to foreign markets not being open to EU businesses.

[37] *See* Alex Barker, Joshua Chaffin & Stanley Pignal, *Germany warns on keeping EU market open*, Fin. Times, Mar. 22, 2012, *available at* http://www.ft.com/cms/s/0/69821548-7374-11e1-94ba-00144feab49a.html.

V. CONCLUSION

It remains to be seen whether the Commission will advance its recent proposals in relation to public procurement contracts, or if an amended form of the measures announced on March 22, 2012 will be taken forward. Aside from these proposals, the Commission's efforts to ensure competition policy in the European Union is not sterilized by interventionist industrial policies is laudable. However, the global playing field is at risk of becoming even less level than before the financial crisis if SOEs are favored over their private sector competitors without an objective justification, and if national foreign investment rules are used to protect national champions or state resources where merger control rules no longer would.