

**INTERNATIONAL GROUP POOLING AGREEMENT  
AND INTERNATIONAL GROUP AGREEMENT OF  
P&I CLUBS UNDER EU COMPETITION LAW**  
—**Review and Prospect**



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## Abbreviations

- CEA** Comité Européen des Assurances (Insurance Europe)
- CLC** International Convention on Civil Liability for Oil Pollution Damage of 1969 (as Amended by Protocol of 1992 and Renamed International Convention on Civil Liability for Oil Pollution Damage of 1992)
- DG Comp** Directorate-General of the Commission Responsible for Competition Policy
- EC** European Community
- ECJ** European Court of Justice
- ECR** European Court Reports
- EEC** European Economic Community
- EU** European Union
- Fund Convention** International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage of 1971 (as Amended by Protocol of 1992 and Renamed International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage of 1992)
- GC** General Court
- IG** International Group of P&I Clubs
- IGA** International Group Agreement
- IPOC** International Oil Pollution Compensation Funds
- OJ** Official Journal of the European Communities
- P&I** Protection and Indemnity
- Pooling Agreement** International Group Pooling Agreement
- Regulation 17/62** Council Regulation (EEC) No 17 of 6 February 1962: First Regulation Implementing Articles 85 and 86 of the Treaty
- Regulation 3932/92** Commission Regulation (EEC) No 3932/92 of 21 December 1992 on the Application of Article 85(3) of the Treaty to Certain Categories of Agreements, Decisions and Concerted Practices in the Insurance Sector
- Regulation 1/2003** Council Regulation (EC) No 1/2003 of 16 December 2002 on the Implementation of the Rules on Competition Laid Down in Articles 81 and 82 of the Treaty

**Regulation 358/2003** Commission Regulation (EC) No 358/2003 of 27 February 2003 on the Application of Article 81(3) of the Treaty to Certain Categories of Agreements, Decisions and Concerted Practices in the Insurance Sector

**Regulation 267/2010** Commission Regulation (EU) No 267/2010 of 24 March 2010 on the Application of Article 101(3) of the Treaty on the Functioning of the European Union to Certain Categories of Agreements, Decisions and Concerted Practices in the Insurance Sector

**STOPIA** Small Tanker Oil Pollution Indemnification Agreement of 2006

**TOPIA** Tanker Oil Pollution Indemnification Agreement of 2006

**TFEU** Treaty on the Function of the European Union

**Treaty of Rome** Treaty Establishing the European Economic Community

**1985 Commission Decision** 85/615/EEC-Commission Decision of 16 December 1985 Relating to A Proceeding Pursuant to Article 85 of the EEC Treaty (IV/30.373—P&I Clubs)

**1999 Commission Decision** 1999/329/EC-Commission Decision of 12 April 1999 Relating to A Proceeding Pursuant to Article 85 and 86 of the EC Treaty and Article 53 and 54 of the EEA Agreement (Cases No IV/D-1/30.373—P&I Clubs, Pooling Agreement)

**2004 Guidelines** Commission Doc. (EC) No 2004/C 101/08: Communication from the Commission-Notice-Guidelines on the Application of Article 81(3) of the Treaty

**2008 Guidance** Commission Doc. (EC) No 2009/C 45/02: Communication from the Commission- Guidance on Commission’s Enforcement Priorities in Applying Article 82 of the EC Treaty to Abusive Exclusionary Conduct by Dominant Undertakings

# 1 Introduction

## 1.1 Topic

As a typical risk-intensive industry, shipping has been associated with marine insurance for centuries. In general, the marine insurance market covers three main business lines: hull insurance, cargo insurance, as well as protection and indemnity (P&I) insurance. Being operated uniquely, P&I insurance underpins safety at sea and has formed a relatively independent market.

Historically, P&I insurance was operated individually by mutual associations located primarily in England and Scandinavia. The oldest Shipowner's Mutual Protection Society, Britannia Steam Ship Insurance Association Limited, was created in 1855. And the first Norwegian P&I association, Assuranceforeningen Skuld, was established in 1897.<sup>1</sup> By the turn of the 20th Century, most of today's existing major P&I Clubs had been set up and the global P&I insurance market was gradually formed. In this process, a further development was the entry into pooling arrangements by various Clubs. The purpose of pooling is to spread risks over certain financial limits between all members within the pool. It culminated in the 1980s and 1990s with the shaping of the International Group of P&I Clubs (IG) operated under the International Group Pooling Agreement (Pooling Agreement) and the International Group Agreement (IGA).<sup>2</sup>

“The thirteen principal underwriting member clubs of the International Group of P&I Clubs between them provide liability cover for approximately 90% of the world's ocean-going tonnage. Individually competitive, the International Group of P&I Clubs

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<sup>1</sup> Bull (2004) p.532

<sup>2</sup> British Maritime Technology (2005)

brings together the collective influence of the mutual clubs as a force for security and stability in international maritime trade.”<sup>3</sup>This brief self-introduction, with an undertone of concerns over competition, indicates the multi-faceted status of the IG: on one hand playing an unparalleled function of global marine liability insurance, on the other, actually or potentially being caught by antitrust investigations on account of oligopoly via collective dominance.

Under the jurisdiction of the European Union (EU) competition law, the IG has been through two completed investigations, which were recorded as 85/615/EEC-Commission Decision of 16 December<sup>4</sup> (1985 Commission Decision) and 1999/329/EC-Commission Decision of 12 April 1999<sup>5</sup> (1999 Commission Decision). The Pooling Agreement and the IGA, after modification, were granted individual exemptions and ruled as compatible with Articles 101 and 102 of the Treaty on the Function of the European Union (TFEU)<sup>6</sup>. The 1999 Commission Decision was valid till February 2009 and from August 2010 the Commission has reopened its third competition investigation to the Pooling Agreement and the IGA and it is still in process.

It is of interest at this time to systematically review the pre-1999 Commission’s competition measures to the IG and map out the prospects of the Pooling Agreement and the IGA under the Commission’s reopened probe from 2010. The dissertation seeks to offer a comparative analysis of the 1985 and 1999 Commission Decisions, in which approach divergences and deficiencies are addressed. Based on this retrospection, the post-1999 variation of legal environments related to the ongoing Commission’s probe is illuminated and then a reappraisal of the Pooling Agreement associated with the IGA is made under the shifted analytic framework. The final part goes to observations and suggestions on this topic.

The purpose of this dissertation is partly to look back at history, providing legal comments on the EU’s competition measures to the Pooling Agreement and the IGA, and partly to

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<sup>3</sup> <http://www.igpandi.org/Home>

<sup>4</sup> [1985] OJ L376/2

<sup>5</sup> [1999] OJ L125/12

<sup>6</sup> (ex Article 85 and 86 EEC Treaty; 81 and 82 EC Treaty) The new numbering of the EU competition provisions will be used throughout this article.

look to the future, offering prospects in consideration of potential lobbying by the parties concerned.

## **1.2 Synopsis**

Chapter 1 presents the scope of the article and reason for choosing this topic. Following, the purpose of the dissertation and an outline are set forth.

Chapter 2 lists the legal sources utilised in the dissertation.

Chapter 3 provides an overview of the P&I insurance market and addresses the specific issues of the Pooling Agreement and the IGA under the EU competition law.

Chapter 4 systematically reviews the 1985 and 1999 Commission Decisions to the Pooling Agreement and the IGA with comparative critiques.

Chapter 5 offers the prospects of the Pooling Agreement and the IGA under the Commission's third probe in process.

Chapter 6 completes the dissertation with a summary of major findings and an overall outlook.



## **2 Legal Sources**

### **2.1 TFEU**

As a starting point, the Pooling Agreement and the IGA are regulated by Articles 101 and 102 TFEU, the twin pillars of the EU competition law. All the problems are examined under the framework of these two Treaty's provisions with an additional reference to Article 106 in the outlook of policy conflicts between competition promotion and environmental protection.

### **2.2 EU Secondary Legislation**

Meantime, the application of Articles 101 and 102 TFEU to the Pooling Agreement and the IGA is subject to the EU secondary legislation including Council Regulations, Commission Regulations and Commission Notices. The 1985 and 1999 Commission Decisions are reviewed under Council Regulation No 17 of 6 February 1962: First Regulation implementing Articles 85 and 86 of the Treaty (Regulation 17/62) while the reopened investigation from 2010 is reappraised under Council Regulation No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty (Regulation 1/2003), the 2004 Commission Guidelines on the application of Article 81(3) of the Treaty (2004 Guidelines) and the 2008 Commission Guidance on its enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings (2008 Guidance). Commission Regulation No 3932/92 of 21 December 1992 on the application of Article 85(3) of the Treaty to certain categories of agreements, decisions and concerted practices in the insurance sector

(Regulation 3932/92) and its successor Commission Regulation No 267/2010 of 24 March 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to certain categories of agreements, decisions and concerted practices in the insurance sector (Regulation 267/2010) are also remarked upon with respect to the inapplicability of insurance block exemption to the Pooling Agreement and the IGA.

## 2.3 Case Law

Certainly, the relevant leading cases of the EU courts and prominent decisions by the Commission are indispensable to the discussion and hence annotated throughout the dissertation to elaborate on numerous specific issues. *FEDETAB*<sup>7</sup> is quoted to certify that the IG Clubs, being non-profit-making, cannot escape Articles 101 and 102 TFEU. *Belasco*<sup>8</sup> is cited to make an allusion, which was sidestepped by the 1999 Commission, that annual recommendations by the IG, even non-binding, should be treated as “agreements” under Article 101 TFEU. *Delimitis v. Henninger*<sup>9</sup> is referenced to clarify the narrow approach to block exemption set down by the European Court of Justice (ECJ). A reference to *Langnese-Iglo GmbH & Co KG v. Commission*<sup>10</sup> is made so as to criticise the leapfrog to Article 101(3) over Article 101(1) by the 1985 Commission Decision in the legal reasoning. *Compagnie Maritime Belge v. Commission*<sup>11</sup> is referred to justify simultaneous application of Articles 101 and 102 TFEU to the Pooling Agreement and the IGA. A group of cases including *United Brands*<sup>12</sup>, *Tetra*<sup>13</sup> and *Oscar Bronner*<sup>14</sup> illuminate the approaches of Article 102 TFEU prevailing before the 2008 Guidance to the Pooling Agreement and the IGA, *inter alia*, “objective justification” and “sliding scale test” to “special responsibility”. *GlaxoSmithKline*<sup>15</sup> in contrast to *CECED*<sup>16</sup> shows the ambivalence of environmental consideration in the implementation of the EU competition

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<sup>7</sup> Joined Cases 209/215 to 218/78 [1980] ECR 3125, 3278

<sup>8</sup> Case 246/86 [1989] ECR 2117

<sup>9</sup> Case C-234/89 [1991] ECR I-935

<sup>10</sup> Case T-7/93 [1995] ECR II-1533

<sup>11</sup> Case C-395/96 P [2000] ECR I-1365

<sup>12</sup> Case 27/76 [1978] ECR 207

<sup>13</sup> Case C-333/94P [1996] ECR 5951

<sup>14</sup> Case C-7/97 [1998] ECR I-7817

<sup>15</sup> Case T-168/01 [2006] ECR II-2969

<sup>16</sup> [2000] OJ L 187/47



law. The lasted ECJ's ruling of *Alrosa*<sup>17</sup> reaffirms the Commission's "margin of appreciation" established by the early joined cases of *Consten & Grundig*<sup>18</sup> and provides the IG with some enlightenment on the commitment procedure. A comprehensive list of case law is incorporated into the section of references.

## 2.4 International Conventions

Additionally, the International Convention on Civil Liability for Oil Pollution Damage (CLC) of 1969 (as amended by Protocol of 1992 and renamed CLC of 1992) and the International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage (Fund Convention) of 1971 (as amended by Protocol of 1992 and renamed of Fund Convention 1992) are referred to as the background law of the polluter pays principle related to the minimal cost for tankers. The Small Tanker Oil Pollution Indemnification Agreement (STOPIA) of 2006 combined with the Tanker Oil Pollution Indemnification Agreement (TOPIA) of 2006, the appendix therein, is mentioned as well.

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<sup>17</sup> Case C-441/07P *Commission v. Alrosa Company Ltd.*

<sup>18</sup> Joined Cases 56 to 58/64 [1966] ECR 299



## **3 P&I Insurance Market and Operation of IG under Competition Policy**

### **3.1 Existing Circumstances of P&I Insurance**

#### **3.1.1 Market Players and Share of P&I Insurance**

P&I insurance can trace its roots back in the mid-1850s<sup>19</sup> as a supplement to hull insurance as extra collision liability. Today P&I insurance has formed an autocephalous sector specializing in third party liability and expenses arising from the operation of ships as principals.

In a general sense, modern P&I insurance is operated in two patterns, mutual association with unfixed calls and commercial underwriting with fixed premium, respectively. The latter is a “niche market”, which focuses on the lower risk of smaller tonnage and covers merely around 10% of the world’s P&I insurance market. The fixed premium facilities primarily include five commercial underwriters as follows: British Marine Limited, Charterers Club, Navigators P&I, Osprey and RaetsMarine. Among them, the bellwether, British Marine Limited only reached 13.5 million entered tonnage with 131 million dollars premium income in 2010. The remaining 90% of the market—850.3 million owned tonnages with 3.3 billion dollars accounting year premium<sup>20</sup>, as of 20 February 2010—is dominated by thirteen IG Clubs<sup>21</sup>. They are namely American Club, Britannia, Gard, Japan Club, London Club, North of England, Shipowners, Skuld, Standard Club, Steamship Mutual, Swedish Club, UK Club and West of England. Their business and/or residences

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<sup>19</sup> *Ibid.* 1 p.532

<sup>20</sup> Tysers (2011)

<sup>21</sup> Here the market share of the non-IG P&I clubs (*e.g.* Korea P&I Club) is negligibly small.

are mostly located in the Member States of TFEU/EEA, where the staple market of P&I insurance exists and the EU competition policy prevails.

### 3.1.2 Oligopoly of P&I Insurance Market via Collective Dominance

Although the aforementioned comparative statistics relate to 2010, it maps out the whole picture of the P&I insurance market in the past three decades. No remarkable fluctuation in the market share has been recorded from the birth of the IG in 1981. This illustrates the fact that the IG Clubs cover the overwhelming majority of the world's P&I insurance market leaving very limited room for other fringe players outside of the IG to compete in terms of pricing and service. The latest example is that of the South of England Protection and Indemnity Association. An independent mutual club which mainly insured larger tonnage which the IG would not accept normally for reasons of age or class, it went into provisional liquidation and ceased trading in October 2011.<sup>22</sup>

The ECJ confirmed in the *AKZO*<sup>23</sup> case that a market share of 50 per cent or more is normally a fair indication of dominance. More accurately, being a preliminary parameter, high market share is usually applied by the EU competition authority as the starting point for assessing market power and thereby identifying market type in respect to the competitive process. Here, the proxy of strong market power, the over-50 percent market share of the IG, just causes the possibility of anti-trust investigation, rather than initiating the proceedings directly. The following test is to scrutinize other competitive factors in the relevant market including the extent of comparative advantage to nearest rival<sup>24</sup>, market entry barrier, etc.

In the case of the Pooling Agreement and the IGA, the fact that a huge gap exists between the IG and its contenders satisfies the test of *Hoffmann-La Roche*<sup>25</sup> very clearly. Much light should be shed on market entry barriers inseparable from the essence of P&I insurance. Barriers inherent in the nature of the market will include “economies of scale or

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<sup>22</sup> Lloyd's List (2011)

<sup>23</sup> Case C-62/86 [1991] ECR I-3359

<sup>24</sup> First held in the judgment of *Hoffmann-La Roche* (para 42) Case 85/76 [1979] ECR 461

<sup>25</sup> *Ibid.* 24

scope, and the risk of having to make large capital investments to enter the market that may turn out to be irrecoverable (referred as to as ‘sunk costs’).<sup>26</sup> The P&I insurance market is where prominent entry barriers exist in form of economies of scale. Extremely high level of P&I insurance covering catastrophic risks means that the law of large numbers could only work on a large number of risk units. Otherwise, an insufficient spread of risk underwritten below the minimum scale could swallow the sunk costs of the underwriter easily when an astronomical claim emerges. Therefore, the IG holds a long-standing dominance in the P&I insurance market. This conclusion remains constant under the new horizon of the 2008 Guidance, of which “over-40 percent market share” and “for a significant period of time” are easily satisfied.

The economist illustrates the workings of the competitive process by reference to four models. The two extremes are perfect monopoly and perfect competition: in real world it is rare to find either. The other two principal types of market are workable competition and oligopoly. An oligopoly is a market in which some degree of competition remains but there are only a handful of competitive undertakings with significant market power. The oligopoly was annotated by the Commission in its decision of *Gencor/Lonrho*<sup>27</sup> via supply and demand analysis, and was also addressed by the General Court (GC) subsequently. The above market power analysis on both quantitative and qualitative dimensions indicates that the P&I insurance market does coincide with the oligopoly-type. On the EU competition law level, oligopoly of the P&I insurance market means that there is no room for applying *de minimis* rule established by *Volk v. Vervaecke*<sup>28</sup> and then codified as Commission’s Notice on agreements of minor importance<sup>29</sup>. The test of “appreciable” effect on competition between Member States is easily satisfied.

An oligopolistic market is nearly always a marked degree of interdependence, which is not a recognized feature in markets that enjoy workable competition.<sup>30</sup> It is so-called collective dominance that primarily attracted the Commission’s attention in *Compagnie Maritime Belge v. Commission*<sup>31</sup>, where plural undertakings on a specific market were

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<sup>26</sup> Goyder (2009) p.302

<sup>27</sup> [1997] OJ L11/30

<sup>28</sup> Case 5/69 [1969] ECR 295

<sup>29</sup> Issued in 1970 with subsequent alterations till 2001

<sup>30</sup> *Ibid.* 26 p.15-17

<sup>31</sup> *Ibid.* 11

united by certain economic links to behave as a sodality through arrangements. As far as the IG, such economic links were achieved via the collaboration under the Pooling Agreement and the IGA, which falls under the jurisdiction of Articles 101 and 102 of TFEU simultaneously. Based on this, the intervention by the EU competition authority is inevitable.

## 3.2 Operation of IG

### 3.2.1 Root of IG and Its Function

In individual operation of the P&I associations, large risks would jeopardize its professional performance, even maintenance. Pooling excessive risks is sensible to the P&I associations for risk management and ultimately favourable to the shipowners and operators. With the purpose of higher-level mutual assistance, the principal P&I associations entered into alliance in the form of the IG with its hard core, the Pooling Agreement and the IGA.

The Pooling Agreement is a mutual agreement between the IG Clubs to reinsure each other by sharing claims proportionally with no premium paid. It defines the types of the claim to be pooled and provides a multi-layer mechanism for sharing all claims in excessive of 8 million dollars up to, currently, approximately USD 6.9 billion<sup>32</sup>. Its operation could be illustrated as the following chart<sup>33</sup>.

	Pollution only	Non-pollution	
		Overspill	
General Excess Loss Contract Layer 4		US\$ 1bn Collective Overspill One reinstatement	US\$ 3.05bn
Layer 3		US\$ 1bn	US\$ 2.05bn
Layer 2	US\$ 500m	US\$ 500m	US\$ 1.05bn
Layer 1 25% Reinsured to Hydra	25% US\$ 500m	75% US\$ 500m	US\$ 550m
Upper Pool Reinsured to Hydra	25% US\$ 20m	75% US\$ 20m	US\$ 50m
Lower Pool	US\$ 22m		US\$ 30m
Club Retention	US\$ 8m		US\$ 8m

<sup>32</sup> <http://www.igpandi.org/Group+Agreements/The+Pooling+Agreement>

<sup>33</sup> *Ibid.* 20

Through the pooling, *viz.* claim-sharing system, the IG Clubs share a common interest in loss prevention and underwriting philosophy considering the “long tail” nature of protection and indemnity risks.

The IG also recognizes that the persistence of the Pool Agreement depends on the goodwill and equity between the member clubs. The mutual interdependent relationship would risk being eroded in the absence of a proper self-governing measure. So just like other industry associations, the IG operates pursuant to its constitution, the IGA, which prescribes the rights and duties of the member clubs and concerns the administrative affairs.

The IGA as last revised in 2008, is an essential measure in ensuring the proximity and equilibrium between the IG Clubs in the operation of the Pooling Agreement. Briefly, it regulates the manner in which clubs can accept entries from shipowners who wish to move their insurance from one club to another; specifies how clubs may quote rates and the information which they should obtain from each other before quoting premium rates and contains a requirement for clubs to disclose in their annual financial statements a ratio relating to their expenses, the Average Expense Ratio.<sup>34</sup>

### **3.2.2 Competition Issues of Pooling Agreement and IGA**

Judging from experience, there is no business model other than the Pooling Agreement with the IGA proven to be more compatible with the nature of P&I risk. The majority of the world’s shipowners and operators rely upon the unparalleled liability cover provided by the IG. However, in the view of the EU competition authority, certain aspects of the Pooling Agreement and the IGA cause concerns as follows, which will be thoroughly discussed in Chapter 4 and Chapter 5:

1) High minimum common level of cover is considered to impede the IG Clubs from competing on the lower level as well as limit the range of cover to the prejudice of consumers;

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<sup>34</sup> <http://www.igpandi.org/Group+Agreements/The+International+Group+Agreement>

- 2) Release calls, viz. the charge of withdrawing ships from the club for its proportionate share of outstanding loss, could be abused as the barrier to market entry as well as the dissimilar condition to equivalent transactions;
- 3) Restricted quotation applied to the ships intending to transfer to a new club as well as new acquired ships are deemed to inhibit internal competition on premiums within the IG;
- 4) Minimum cost for tankers constitutes price fixing;
- 5) Reinsurance provisions lacking criteria and procedures to a third-insurer are regarded as the refusal of access to essential facilities.



## **4 Pre-1999 EU Competition Measures to Pooling Agreement and IGA**

### **4.1 Sketch of Previous Commission's Competition Investigations**

It is widely accepted within the EU that competition *per se* is not the final goal but a portal of economic welfare. However, economic welfare originally, as a concept of macroeconomics, is rooted in hypotheses-testing of empirical market data. This measure, to some extent, deviates from legal certainty. The experience of the EU competition authority shows that nothing except the hybrid of common law and civil law reasoning styles is helpful to reconcile legal certainty and economic analysis. Effective implementation of competition policy depends on only a handful of core rules in a case-by-case approach. Articles 101 and 102 TFEU, the twin pillars of the EU competition law, will be construed in the light of case law to draw a proper conclusion with commentary on the Pooling Agreement and the IGA.

Additionally, the implementation of the EU competition law has undergone modernization from Regulation 17/62 to Regulation 1/2003. The previous Commission's investigations into the Pooling Agreement and the IGA were recorded as the 1985 and 1999 Commission Decisions. The pre-1999 EU competition measures should be analyzed under the auspices of Regulation 17/62.

For ease of retrieval and reading, a chronological table of the pre-1999 EU competition measures to the Pooling Agreement and the IGA is provided here as a brief retrospect.

Year	Date	Events and Related Statutes
1981	18 June	According to Article 4 of Regulation 17/62, the IG made the first notification to the Commission concerning the IGA and intended to obtain a negative clearance or, alternatively, an exemption.
1983	18 Feb.	Thinking that certain clauses of the IGA failed to satisfy the conditions of The Article 101(3) TFEU, the Commission sent a Statement of Objections to the IG after a preliminary examination, prior to a final decision under Article 15(6) of Regulation 17/62.
1983	1 Nov.	After discussion, the IG submitted a memorandum proposing certain amendments of the IGA to the Commission.
1984	12 July	The Commission issued the second Statement of Objections in the opinion that some clauses of the IGA still infringed Article 101(1) TFEU and could not be exempted upon Article 101(3).
1984	27 July	The IG re-modified IGA and requested again for a negative clearance or alternatively an exemption.
1984	2 Aug.	The Commission informed the IG that the proceedings under Article 101(1) TFEU concerning the IGA would be continued till all the issues in the Statement of Objections are settled.
1985	20 Feb.	The IG notified the Commission of the third modified IGA.
1985	16 Dec.	The Commission made the decision granting a ten year exemption to the IGA pursuant to Article 101(3) TFEU: disapplying the prohibition of Article 101(1).

- 1995 20 Feb. The IG requested a renewal of the exemption granted on 16 December 1985.
- 1997 2 June The Commission issued a Statement of Objections to the IG holding that the Pooling Agreement and the IGA infringed the competition rules of TFEU.
- 1998 7 July Adopting the Statement of Objections, the IG made formal notification to the Commission for exemption of its amended version of the Pooling Agreement.
- 1998 21 Oct. Adopting the Statement of Objections, the IG made formal notification to the Commission for exemption of its latest version of the IGA.
- 1999 12 Apr. The Commission made the decision: 1) adjudging there was no contravention of Article 102 TFEU by the Pooling Agreement and the IGA both as amended; 2) granting an exemption to the Pooling Agreement and IGA pursuant to Article 101(3) TFEU, valid from 20 February 1999 to 20 February 2009.

The following legal assessment will be based on the facts in this chronological table and the issues listed in 3.2.2.

## **4.2 Prerequisite: Compatibility of IG Clubs to Undertakings in Articles 101 and 102 TFEU**

For the purpose of the EU competition law, the term of “undertaking” in Articles 101 and 102 TFEU is treated in a teleological approach and receives a wide definition of functional rather than institutional. It is clarified by a number of precedents under the EU judicature, ranging from earlier case of *Mannesman v. High Authority*<sup>35</sup> to recent *Pavlov*<sup>36</sup>, that any

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<sup>35</sup> Case 19/61 [1962] ECR 357, 371

<sup>36</sup> Cases C-180/98 [2000] ECR I-6451

entity engaged in an economic activity offering goods or services on a given market, regardless of other factors such as legal status, is considered an undertaking. So generally speaking, the IG Clubs providing insurance service fall into the scope of “undertakings” under Articles 101 and 102 TFEU.

Notwithstanding, the non-profit making basis of the IG clubs deserves further clarification as the boundary case. The view of Directorate-General of the Commission responsible for competition policy (DG Comp) is that “competition is not just about prices and profits. Non-profit undertakings are still competing albeit not with the goal of profit. And, although they cannot reduce profit, they can reduce all other elements of cost. Thus competition is still very important in order to make them more efficient.”<sup>37</sup> This position was previously upheld by the ECJ in the ruling of *FEDETAB*<sup>38</sup> that “it cannot escape [Article 101 TFEU] simply because it has been made by a non-profit-making association.” More precisely, in the case involving the insurance sector on this issue, *Fédération française des Sociétés d'Assurance v. Ministre de l'Agriculture*<sup>39</sup>, the ECJ kept the same position and concluded that a non-profit-making organization managing an optional pension scheme is an undertaking within the meaning of Articles 101 and 102 TFEU. Being non-profit-making *per se* could not evade the fact that it was competing with other private insurance companies. It is worth noting that a legal exception herein was offered by another French insurance case *Poucet v AGF and Pistre v Cancava*<sup>40</sup> before the ECJ for drawing the borderline, which confirmed that “undertaking” could not cover non-profit-making insurance organizations operating social security scheme based on “national solidarity”.

Given the above precedents, clearly it is not intended by the EU competition authority to provide asylum for the entities alleging non-profit-making to escape Articles 101 and 102 TFEU in respect of “undertakings”. Being unrelated to the legal exception of operating social security scheme aforesaid, the IG Clubs “compete between themselves as well as with other mutual and profit-making insurers in some segments of the P & I insurance

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<sup>37</sup> Bennet (2000) p.61

<sup>38</sup> *Ibid.* 7

<sup>39</sup> Case C-244/94 [1995] ECR I-4013

<sup>40</sup> Joined Cases C-159/91 to C-160/91 [1993] ECR I-637

business.”<sup>41</sup> On this ground, the IG Clubs fall into the scope of “undertaking” and the applicability of Articles 101 and 102 TFEU to the Pooling Agreement and the IGA is satisfied.

### **4.3 Legal Assessment of Pooling Agreement and IGA under Article 101(1) TFEU**

#### **4.3.1 Subcategory for Pooling Agreement and IGA under Concept of Agreements in Article 101(1) TFEU**

Theoretically, the agreements within the meaning of Article 101(1) TFEU can be categorized into two groups, namely hardcore cartels and ancillary restraints. The first type is defined by DG Comp as “the arrangement(s) between competing firms designed to limit or eliminate competition between them, with the objective of increasing prices and profits of the participating companies and without producing any objective countervailing benefits”<sup>42</sup>. The second type is comprised of the agreements of which certain clauses may fall into the scope of Article 101(1) TFEU outwardly, whereas *de facto* they are vehicles of other prime objectives like service cooperation or sharing specialization rather than anti-competition in the market.

In practice, hardcore cartels are mostly found in business sectors with limited product differentiation and often involve market division, quantity restriction, *etc.*, which undermine the competitive process directly. Accordingly, these blatantly anti-competitive agreements have received much more intensive monitoring by DG Comp and heavy fines have been imposed in a series of cases, notably the €462 million that *Hoffmann-La Roche (Vitamins Cartel)*<sup>43</sup> was fined for being involved in the Vitamin Cartel in 2001. Moreover, a straight approach to hardcore cartels has been adopted by the EU courts. The ECJ originally held in *Consten & Grundig*<sup>44</sup> that when the object of anti-competition is established, there is no further need to examine the effects of the agreement concerned.

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<sup>41</sup> *Ibid.* 5 para 50

<sup>42</sup> DG Comp. (2002)

<sup>43</sup> [2003] OJ L6/1

<sup>44</sup> *Ibid.* 18

Despite only one sort of confusing decision by the GC in *GlaxoSmithKline v. Commission*<sup>45</sup> recently, most of the standing cases such as *Miller International v. Commission*<sup>46</sup> and *Parker Pen*<sup>47</sup> have reaffirmed this *illegal per se* doctrine established by *Consten & Grundig*<sup>48</sup>.

At the other end of the scale, ancillary restraints will be examined more precisely in the economic context. The main authority is *Societe La Technique Miniere v. Maschinenbau Ulm*<sup>49</sup>, in which the ECJ also introduced the well-known counterfactual test that the competitive process must be comparatively judged between the *status quo* and the assumed consequence without the agreements of ostensible anti-competition. This approach was also applied by the GC in *O<sub>2</sub> (Germany) GmbH & Co OHG v. Commission*<sup>50</sup> recently.

Even stigmatized as a “cartel” by laymen based on oligopoly of the P&I insurance market for years<sup>51</sup>, the Pooling Agreement was regarded appropriately as “in essence a claim-sharing agreement”<sup>52</sup> by the 1999 Commission Decision. At first sight, the restrictive provisions of claim-sharing agreement prevent the P&I clubs from providing insurance on diversified levels. However, the supply side of P&I insurance corresponding with economies of scale and sunk costs analysis in 3.1.2 justifies the indispensability of claim sharing within the IG. “The minimum dimension required to offer such cover can only be attained by insuring more than 50% of world-wide tonnage”<sup>53</sup> and therefore there is only room for a *fait accompli* soloist, the IG. Without the facility of claim sharing, no club could independently offer cover up to the current amount. It indicates that the Pooling

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<sup>45</sup> *Ibid.* 15

<sup>46</sup> Case 19/77 [1978] ECR 131

<sup>47</sup> Case T-77/92 [1994] ECR II-549

<sup>48</sup> *Ibid.* 20

<sup>49</sup> Case 56/65 [1966] ECR 235

<sup>50</sup> Case T-328/03 [2006] ECR II-1231

<sup>51</sup> Joe Hughes, chairman and chief executive of American Club, took issue with those who persisted in the description of the IG as a “cartel”. “To describe the International Group as a cartel is totally misguided. This betrayed a fundamental misunderstanding of its nature. A cartel is a group of for-profit suppliers of goods or services who combine to create a malignantly dominant market position in order to inhibit competition and to impose high prices on the consumers of those goods or services with the aim of achieving exceptional profitability for themselves at the expense of those consumers with no benefit, direct or indirect, to the wider community. By contrast, the International Group is an association of not-for-profit shipowner-consumer co-operatives, a combination that gives it a benignly dominant position in the best interests of the shipowner-consumers themselves. Its purpose is to provide the lowest prices and the broadest cover in the insurance of marine liability risks for those shipowner-consumers.” --speaking at the annual Houston Marine Insurance Seminar on the theme “The P&I World in Transition”, 4th Oct 2010

<sup>52</sup> *Ibid.* 5 para 14

<sup>53</sup> *Ibid.* para 68

Agreement increases underwriting capacity of individual clubs objectively and gains credit in the counterfactual text aforesaid.

On these grounds, the Pooling Agreement and the IGA were treated by the Commission as ancillary restraints, which may inhibit competition only by its “effect” rather than “object” in Article 101(1) TFEU. Under this preferential subcategory, the Pooling Agreement and the IGA went through a number of modifications listed in the foregoing chronological table. The relevant legal analysis is provided in 4.3.2 amid the characteristics of P&I insurance.

### **4.3.2 Application of Article 101(1) TFEU to Pooling Agreement and IGA**

#### **4.3.2.1 Structure of Article 101 TFEU and Internal Order of Application**

For the sake of understanding the pre-1999 Commission’s approach to the Pooling Agreement and the IGA under Article 101(1) TFEU, it is necessary to make allusion to the integral structure of Article 101 TFEU firstly. Paragraph (1) is “primarily designed to assert jurisdiction”<sup>54</sup>, which could embrace extensive agreements questionable in terms of competition. The following paragraph (3), in the form of exemption provider, actually is dedicated to set out concrete assessment element of the whole article. This two-fold structure of Article 101 TFEU differs from its counterpart, Sherman Act Section 1 of succinct style, which is a hybrid of jurisdictional and assessment provisions.

The *pro forma* split between paragraph (1) and (3) determines that to a large extent, the appraisal of economic context under the former has no alternative but to refer itself to the latter. Put differently, the assessment element in Article 101 TFEU “is found in paragraph (3), and only to a more limited extent in paragraph (1)”<sup>55</sup>. This viewpoint could be circumstantiated by the case of *Gottrup Klim v. DLG*<sup>56</sup>, where the issue in determining the applicability of Article 101(1) TFEU was whether the restrictive rules were necessary to ensure the cooperative functioning properly. The test of necessity is identical or comparable to the criterion of indispensability in Article 101(3)(a) TFEU.

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<sup>54</sup> *Ibid.* 26 p.111

<sup>55</sup> *Ibid.* 26 p.112

<sup>56</sup> Case C-250/92 [1994] ECR I-5641

On the other hand, at the end of last century, case law of the EU judiciary indicated that the scrutiny under paragraph (1) should be exhausted before the invocation of paragraph (3). Only when the issue is thoroughly examined under paragraph (1) but still intractable, it is the turn of paragraph (3) to be considered in respect of applicability. Any short cut to Article 101(3) TFEU circumventing the legal appraisal under Article 101(1) TFEU would render a legitimate flaw. In *Langnese-Iglo GmbH & Co KG v. Commission*<sup>57</sup>, the GC denied the postponed legal assessment of market factors under Article 101(3) TFEU by the Commission and held that it should have been done in the appraisal of Article 101(1) TFEU. Similarly, in *European Night Services*<sup>58</sup>, the GC emphasized that the Commission must give good reasons for deciding that an agreement infringes Article 101 TFEU. For lack of such reasoning, the decision was quashed.<sup>59</sup>

This stringent test under Article 101(1) TFEU set by the GC precedents around 2000 should be understood with an eye toward the modernisation of the rules implementing Article 101(3) TFEU. By virtue of Article 9 of Regulation 17/62, the application of Article 101(3) TFEU was under the exclusive competence of the Commission. By contrast, national courts and authorities had no alternative but entrenched themselves within Article 101(1) TFEU when faced with competition issues. However, the Commission's monopoly of Article 101(3) TFEU has no place in the new system of Regulation 1/2003. Under the EU judiciary as the level playing field, the Commission, which was prone to direct application of Article 101(3) TFEU, has to overcome the path dependence and keep in line with national courts and authorities, for which the usual practice is to make fuller analyses under Article 101(1) TFEU.

Understanding the structure of Article 101 TFEU and the internal order of application is of vital importance to the implementation of this key competition provision. The divergence between the 1985 Commission Decision and the 1999 Commission Decision on this point brings about different treatments received by the sub-issues from 4.3.2.2 to 3.3.2.5.

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<sup>57</sup> *Ibid.* 10

<sup>58</sup> Case T-374, 375, 384 and 388/94 [1998] ECR II-3141

<sup>59</sup> Korah (2007) p.87



#### **4.3.2.2 Minimum Common Level of Cover**

In the policy years before 1998, the ceiling of common cover under the Pooling Agreement was fixed at USD 18 billion. However, this unduly high minimum level of cover failed to pass the test of “indispensable to proper functioning of the Pooling Agreement”<sup>60</sup> and consequently restricted competition within the meaning of Article 101(1) TFEU.

The 1997 Statement of Objections considered that the exorbitant minimum level of cover had objectively impeded clubs from contending in lower level of cover, where substantial demand should be satisfied. Taking the Commission’s opinion into account, the Pooling Agreement adjusted the figure to USD 4.25 billion in the 1998 notification.

Being dissociated from the over-high portion, the new minimum common level of cover was re-qualified as a necessary arrangement for the functioning of the Pooling Agreement. On this ground, the 1999 Commission Decision finally concluded that the lowered common level of cover would no longer fall into the scope of Article 101(1) TFEU.

#### **4.3.2.3 Release Calls**

When a member enters one or more ships in a P&I association, the shipowner agrees implicitly to share the liabilities of the membership as a whole for the policy years in which the ship is insured, and accepts liability for the payment of any deferred calls or supplementary calls which the P&I association may consider necessary to balance the income and expenditure of those policy years. The member’s obligation to pay such calls for any policy year which has not yet been closed continues even if its participation is terminated or ceased for any other reason.

In such circumstances, it can be inconvenient for the association to have to continue to pursue the member for deferred calls or supplementary calls and it may also be

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<sup>60</sup> *Ibid.* 5 para 74

inconvenient for the member to have a continuing uncertain liability for such calls.<sup>61</sup> The solution provided by the IGA at the outset was that the IG Clubs were entitled with a lump sum charge on the basis of calculation, which once paid, would release the member from liability to pay any future deferred call or supplementary call.

Release call levying was designed to prevent liability escaping in the case of transfer and preserve the principle of mutuality. However, the Commission felt dubious about this solution, which could be used maliciously as deterrence against transfer among clubs and should be modified by certain parallel alternative measure. Subsequently, the IGA of 1985 was modified in this connection as “the operator has the option of paying the release call or providing a bank guarantee for his share of outstanding liabilities”<sup>62</sup>.

In the 1985 Commission Decision, even vaguely defined as “not clear-cut”<sup>63</sup> or merely “potentially”<sup>64</sup> restrictive effects in Article 101(1) TFEU, the rules relating to release calls were still examined under Article 101(3) TFEU concerning indispensability of the restriction and granted the exemption as the final treatment. However, in the 1999 Commission Decision, the appraisal of the rules relating to the release calls was completed within Article 101(1) TFEU with no need of invocation of Article 101(3) TFEU.

The variation could be read in the light of precedent *Gottrup Klim v. DLG*<sup>65</sup>, where indispensability of restriction in Article 101(3)(a) TFEU was introduced to the test of Article 101(1) TFEU. The 1999 Commission Decision concluded that release call levying with the alternative of bank guarantee was not “disproportionate”<sup>66</sup> to the proper functioning of the Pooling Agreement, given the fact that an effective payment could be deferred to the liquidation of standing liability through guarantee. As a result, the rules relating to release calls were excluded from the items with the meaning of Article 101(1) TFEU in the conclusion part as to restriction of competition<sup>67</sup>. The new approach, switched in 1999, also kept in turn with the GC’s ruling of *Langnese-Iglo GmbH & Co KG v.*

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<sup>61</sup> Williams (2008) p.122

<sup>62</sup> *Ibid.* 4 para 16

<sup>63</sup> *Ibid.* 4 para 27

<sup>64</sup> *Ibid.* 4 para 53

<sup>65</sup> *Ibid.* 56

<sup>66</sup> *Ibid.* 5 para 86

<sup>67</sup> *Ibid.* 5 para 102

*Commission*<sup>68</sup>, which emphasized that the Commission must give legal reasoning of soundness under Article 101(1) TFEU before resorting to Article 101(3) TFEU. Whether the rules relating to release calls could escape Article 101(1) TFEU directly or be caught with subsequent exemption of Article 101(3) TFEU is of practical importance to the burden of proof. In the 1985 Commission Decision, the burden of proof lay with the IG when it invoked Article 101(3) TFEU for acquiring the redeeming virtues. In contrast, the 1999 Commission Decision, the IG was free from such onus to justify the rules relating to release calls.

#### **4.3.2.4 Restricted Quotation**

In the original IGA of 1981, a potential new club was prohibited to offer a lower quotation, provided the rate of the holding club was reasonable. This rule of quotation restriction also covered new ships of the “going” member and only could be challenged before the expert committee of the IG exclusively.

After discussions with the Commission from 1983 to 1985, the IGA reserved the burden of proof between new clubs and holding clubs concerning the reasonability of rate quotation before the expert committee. The new club was rebuttably presumed free to offer the quotation on the condition that the holding club must be notified without delay of “a contractually binding commitment at the quoted rate having been entered into between the operator and the new club by 30 September of the year preceding that for which the new insurance policy is to be effective”<sup>69</sup>. This pre-30 September procedure also applied immediately to the new ships acquired by the operator.

However, the subsequent implementation of the pre-30 September procedure was far removed from how it was envisaged: from 1986 to 1994, a total of eleven requests were recorded, of which only one transfer was finally done.<sup>70</sup> It suggested the new procedure had not promoted rivalry efficiently and incurred the 1997 Statement of Objections maintaining that the quotation procedures in existence were still against Article 101(1)

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<sup>68</sup> *Ibid.* 10

<sup>69</sup> *Ibid.* 4 para 14

<sup>70</sup> *Ibid.* 5 Statistics form Reference (1)

TFEU. One year apart, the IG notified an amendment that narrowed the scope of its application to costs of claims, reinsurance and administrative costs being excluded. Annual disclosure of past five-year average expense ratio for each club was also introduced to increase the transparency of administrative costs.

This amendment presented a breakthrough in free quotation and was accepted by the 1999 Commission Decision on the level of claim sharing. The Commission recognized that “[...] any claim-sharing agreement requires some degree of discipline between the participants in that agreement on the rates corresponding to the costs that they share. No club would be ready to share claims with another club that would be offering a lower rate for covering these same claims. No customer would remain with the first club because it would know that it could obtain from the second club exactly the same cover, covered also by all the P&I Clubs, but for a lower rate.”<sup>71</sup> The counterfactual test (referred in 4.3.1) was applied tacitly by the Commission to justify the inherence of the restricted quotation on the level of claim sharing. Meanwhile, the Commission thought that internal administrative costs had no relevance with the cost of claim sharing and accordingly free quotation and competition should be introduced to it. For the same reason, on the retention level, the 1999 Commission Decision penetrated a series of modification to the restricted quotation and pointed out that “[...] indeed, for non-shared costs there is no need to ensure that the clubs do not undercut each other. The clubs which could achieve a reduction of these costs below the level of their competitor's costs should be able to charge lower rates.”<sup>72</sup>

Having no contribution to the claim sharing arrangement, the restricted quotation on the retention level constituted “price fixing” in Article 101(1)(a) TFEU. It interposed party autonomy between the potential new club and the shipowner, and reduced the possibility of lower rates, the incidence of membership transfer and ultimately competition between the clubs. A parenthetical remark here is that the 1985 Commission Decision neither applied the counterfactual test nor differentiated between the level of claim sharing and the level of retention under Article 101(1) TFEU. Instead, it gulped down the issue of restricted quotation and resorted to Article 101(3) TFEU outright without appropriate digestion. Comparatively, the 1999 Commission Decision illustrated more credible and accurate legal

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<sup>71</sup> *Ibid.* 5 para 89

<sup>72</sup> *Ibid.* 5 para 92

reasoning in this connection. This improvement could be read as a positive response by the Commission to the GC's ruling of *Langnese-Iglo GmbH & Co KG v. Commission*<sup>73</sup> as well as *European Night Services*<sup>74</sup>.

#### 4.3.2.5 Minimum Cost for Tankers

Under the IGA, the underwriting activities of tankers used to be at the unified minimum rate called ETC (estimated total cost). In the 1985 revised version, ETC was softened and reserved in the form of annual recommendation by the IG with the principle of total cost including administration element. Theoretically, this particular rule should go through two-stage test under Article 101(1) TFEU. The preliminary issue is whether such a non-binding rate recommendation of cost for tankers could fall into the scope of "agreement" in Article 101(1) TFEU. If so, subsequently, what is the proper treatment for the minimum cost for tankers?

Concerning the first question, the 1985 Commission Decision did not made any exposition. However, a few years later in the decisions of *Belasco*<sup>75</sup>, the ECJ affirmed that the recommendation by association, even if non-binding, should be treated as agreements between the members. It was regrettable that this authority was not quoted by the 1999 Commission Decision, which evaded the issue of non-binding, instead imputing the minimum cost for tankers to its over-deterrence of depriving reinsurance<sup>76</sup> directly.

With respect to the second question, under the pressure of the Statement of Objections, the principle of total cost was further neutralized in 1998. The IGA extended the approach of excluding the administrative costs (referred in 4.3.2.4) to the minimum cost for tankers and prescribed that "quotations for tankers must make fair and adequate provisions for all relevant elements of cost other than internal administrative costs"<sup>77</sup>. The modified rules on the minimum cost for tanker received the similar treatment to restricted quotation in the

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<sup>73</sup> *Ibid.* 10

<sup>74</sup> *Ibid.* 58

<sup>75</sup> *Ibid.* 8

<sup>76</sup> *Ibid.* 5 para 99

<sup>77</sup> *Ibid.* 5 para 39

1999 Commission Decision. As far as the retention level, the minimum cost for tankers was deemed to represent “price fixing” listed in Article 101(1)(a) TFEU.

#### **4.4 Implementation of Article 101(3) TFEU to Pooling Agreement and IGA in Old System of Regulation 17/62**

##### **4.4.1 Questionable Alternative Pleading upon Article 2 and Article 4 of Regulation 17/62**

Regulation 17/62 was approved by the Council and went into effect in 1962 as the first regulation setting out the procedural application of Article 101 TFEU. Being the backbone of Regulation 17/62, Article 2 tailed by Article 4 framed the implementary route of Article 101 TFEU. The preliminary test was to determine whether negative clearance under Article 101(1) TFEU could be satisfied. If failed, the conditions of exemption under Article 101(3) TFEU would be further examined. Nevertheless, the envisaged route was blurred by the undertakings in practice, alternative pleading for negative clearance or exemption. This tactic was also used by the IG in its original notification.<sup>78</sup>

As analyzed in 4.3.2, the leapfrog to exemption upon Article 101(3) TFEU disregarding the assessment under Article 101(1) is not good legal reasoning under the system of Regulation 17/62. To some extent, it was the alternative pleading by the IG that nourished the inexact reasoning of Article 101 TFEU by the 1985 Commission Decision. The applicability of negative clearance upon Article 2 of Regulation 17/62 remained untouched for one and half decades and was eventually ascertained by the 1999 Commission Decision. To sum up, comparing with the 1985 Commission Decision, the 1999 Commission Decision narrowed the application scope of Article 101(3) TFEU, confirming that the amended minimum common level of cover and rules relating to release call would not infringe Article 101(1) anymore and only leaving the restricted quotation and minimum cost for tankers insofar as the retention level to be further examined under Article 101(3).<sup>79</sup>

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<sup>78</sup> *Ibid.* 4 para 1

<sup>79</sup> *Ibid.* 5 para 79 and para 102

#### **4.4.2 Essence of Regulation 17/62: Notification and Authorization**

The chronological table in 4.1 and the sub-issues analysis in 4.3.2 illustrate how the Commission implemented the competition policy to the Pooling Agreement and the IGA, *inter alia*, notification and authorization, by virtue of Article 4 combined with Article 9 of Regulation 17/62.

Article 4 provided the undertaking concerned with a preliminary administrative procedure, in which the undertaking got the opportunity to notify the Commission and adjust the practice in issue. All the amendments achieved would narrow the gap and pave the way for the final Commission Decision. In practice, most agreements notified, the Pooling Agreement and the IGA alike here, fell into the gray area between entirely pro-competition and absolutely anti-competition. This preliminary administrative procedure did have the merit of legal certainty by providing concrete objection and instruction.

Article 9 authorized the Commission with sole power to declare Article 101(1) TFEU inapplicable pursuant to Article 101(3). In the nascent implementation of the EU competition law, the top priority was to centralize case law and make the application uniform. Exclusive competence of the Commission eliminated the inconsistent application on the level of state courts and authorities.

Notification and authorization as the essence of Regulation 17/62 had not been altered until the implementation of Regulation 1/2003 (to be discussed in 5.2) at the beginning of this century. The following discussion (4.4.3 and 4.4.4) will be based on this essence as the procedural cornerstone.

#### **4.4.3 Unfeasible Proposal: Block Exemption**

On the premise that the restricted quotation and minimum cost for tankers do fall within the scope of Article 101(1) TFEU, logically, the next test is whether they could be covered by a block exemption as the “fast track” to Article 101(3) TFEU. Only when a block

exemption is not available, it is turn of an individual exemption to provide the final treatment. For the sake of a tight argument, consideration of the block exemption to the Pooling Agreement and the IGA cannot be skipped, even it is found as an unfeasible proposal in hindsight.

In the context of Pooling Agreement and the IGA, Regulation 3932/92 was *prima facie* relevant and attracted the attention of the 1999 Commission Decision.<sup>80</sup> Article 102(b) of Regulation 3932/92 prescribed that “co-reinsurance groups in order to reinsurance mutually is eligible for the insurance block exemption”. The 1999 Commission Decision sidestepped the compatibility of claim-sharing arrangements to this prescription, but derogated the applicability of Article 102(b) by invoking Article 111(a). Hereunder, the combined market share of the IG Clubs far exceeded 15%, the upper limit for applying Article 102(b). The limitation of applicability based on market share stemmed from the Commission’s reform of block exemption regulation since 1999, of which the starting point was to benefit small or medium undertakings with legal certainty by replacing lengthy “white lists” with “safe harbour” in market percentage. Without question, the IG holding the dominant position was out of the Commission’s auspices intended. On this ground, the restricted quotation and minimum cost for tankers were finally excluded from the scope of block exemption.

One more point noteworthy here is that even though the 1999 Commission Decision stated that “it is not clear from case law whether the insurance block exemption also covers claim-sharing arrangements between insurance mutuals”<sup>81</sup>, in fact, the ECJ had set down the narrow approach to block exemption in *Delimitis v. Henninger*<sup>82</sup>. Being secondary legislation to apply Article 101(3) TFEU, the block exemption should be construed rigidly. Only when the agreement in issue squares neatly with the provision of block exemption will the safe harbour be provided for the undertaking concerned. Similarly, in the post-1986 maritime transportation, “the various investigations of the practices of the members of liner conferences illustrate the narrowness of block exemption regulation”<sup>83</sup>. In the light of these, the Commission’s negative position underlying the vague wording of

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<sup>80</sup> *Ibid.* 5 para 103

<sup>81</sup> *Ibid.* 5 para 104

<sup>82</sup> *Ibid.* 9

<sup>83</sup> Greaves (2010) p.130



“not clear” should be perceived regarding the application of block exemption to the Pooling agreement and the IGA.

#### **4.4.4 Final Treatment: Individual Exemption**

When the Pooling Agreement and the IGA, particularly the restricted quotation and minimum cost for tankers, could not be embraced by the “safe harbour” of block exemption, the last escape from Article 101(1) TFEU is the individual exemption upon Article 101(3). Article 101(3) sets down four separate and cumulative conditions for declaring Article 101(1) inapplicable, namely, contribution to economic welfare; fair share of benefit to consumers; indispensability of restriction and non-elimination of competition. Credit obtained by a restraint for passing any particular condition by a considerable margin cannot be taken advantage of at a later stage if the restraint fails to satisfy a subsequent condition for exemption.<sup>84</sup> A series of tests on both positive and negative sides has to be completed.

##### **4.4.4.1 Contribution to economic welfare**

As the main goal of competition policy, the concept of economic welfare is materialized under Article 101(3) TFEU in terms of “improving the production or distribution” or “promoting technical or economic process”. The restricted quotation and minimum cost for tankers essentially both are price measures of P&I insurance. Whether these rules on the retention level, outside the Pooling Agreement, can contribute to economic welfare should be assessed in view of premium setting of P&I insurance.

Insurance premium is a typical cyclical market, where “prices are pushed down due to fierce competition between rival insurers, for many of whom the distinction between market share and profitability has become blurred”<sup>85</sup> until losses become apparent. In the field of P&I insurance, mutual associations underwrite “at cost” and profit is not included in the computation of calls. The basic equation for underwriting is that calls plus

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<sup>84</sup> *Ibid.* 26 p.156

<sup>85</sup> *Ibid.* 37 p.57

investment income should equal claims plus expenses plus reinsurance premiums.<sup>86</sup> In fact, the principle of “at cost” without profit making is more likely to be jeopardized by price-cutting rather than pricing fixing. When free pricing prevails in the P&I insurance market, anarchy is foreseeable under ultra competition and does no good to sustainability of the supply on the basis of cost.

The restricted quotation and minimum cost for tankers are designed to guarantee net premium on the basis of cost, which is highly linked to loss claims *ex post* and *ex ante*. Even on the retention level, such rules avert the feast or famine cycle of price and thereby endow the supply of P&I insurance with predictability and stability. Furthermore, by means of a high degree of linkage between premium and risk, the restricted quotation and minimum cost for tankers create incentives for loss prevention with due diligence, and consequently better safety performance by the shipowners in seaborne trade. Less damaging incidents occur at sea, and the economic process enjoys more efficiency.

In the appraisal of contribution to economic welfare, different approaches were adopted by the 1985 and 1999 Commission Decisions, but neither of them seems to be laudable in retrospect. The 1985 Commission Decision contended that “improvement in production or distribution” of insurance service was satisfied.<sup>87</sup> However, the reasoning to this positive condition was then virtually subject to the negative condition “indispensability of restriction”. Sub-arguments composed of “preserving the principle of mutuality”, “stability of premiums” and “continuation of the pool arrangement”<sup>88</sup> did justify that the IGA was indispensable to the operation of P&I insurance, but it is extremely dubious to equate “maintenance” of P&I insurance operation with “improvement” of insurance service, as far as I see.

14 years later, the 1999 Commission Decision substituted “promotion of economic progress” for “improvement in production or distribution”. Notwithstanding the transferred argument, the legal reasoning remained more or less discursive. As mentioned in the end of 4.4.1, the 1999 Commission Decision confirmed that the restricted quotation and minimum cost for tankers insofar as the retention level were left to be further examined under Article

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<sup>86</sup> Hazelwood (2010) p.98

<sup>87</sup> *Ibid.* 4 para 39

<sup>88</sup> *Ibid.* 4 para 35, para 36 and para 37

101(3) TFEU. Paradoxically, the appraisal of the first condition of Article 101(3) TFEU here did not centered on the retention level but rushed back to the pooling level by concluding that “the IG’s arrangements, therefore, contribute to economic progress by ensuring that P&I insurance cover of up to EUR 3.9 billion (USD 4.25 billion) is available in the market.”<sup>89</sup> Comparatively, “promotion of economic progress” is more justifiable than “improvement in production or distribution” in the scenario of intangible financial service like P&I insurance with a long-tail nature, particularly the restricted quotation and minimum cost for tankers. However, it should be limited to the retention level, of which the analysis would have been more credible if the necessity of price stabilization in the P&I insurance market and its positive impact on loss prevention and economic efficiency had been concerned.

#### **4.4.4.2 Fair Share of Benefit to Consumers**

The welfare measure advocated by mainstream economists is overall social welfare, which comprises both “consumer welfare and producer welfare”<sup>90</sup>. Nonetheless, the primary goal served by the EU competition policy is to maximize consumer welfare. This is the background for understanding “fair share of benefit to consumers” as the second positive condition of Article 101(3) TFEU, which is easily satisfied here by the restricted quotation and minimum cost for tankers.

Firstly, due to the essence of P&I Clubs that “they are mostly mutual associations, where the members are both insured and insurers”<sup>91</sup>, identification between producer and direct consumers is established. In the “consumer owned” business, no gap could be formed to block the economic welfare gained in 4.4.4.1 floating to shipowners. However, this consumer benefit under privity of contract was requested to entertain third parties in the case of *Cobelpa VNP*<sup>92</sup>. Given the overarching position of P&I insurance in the maritime industry chain, the credits gained under the first condition pass downstream on to final consumers smoothly. Stable supply of P&I insurance guarantees sufficient compensation

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<sup>89</sup> *Ibid.*5 para 106

<sup>90</sup> Whish (2008) p.4

<sup>91</sup> *Ibid.* 86 p.1

<sup>92</sup> [1977] OJ L242/10

available to passengers and other customers of the shipowners. Loss prevention also gains efficiency in favor of all potential consumers downstream in the long term.

The 1985 and 1999 Commission Decisions kept the same position with *Cobelpa VNP*<sup>93</sup> in this connection<sup>94</sup>. The former did a more detailed analysis while the latter merely embedded this issue into the discussion of “promotion of economic progress”. Notwithstanding this disparity in form, they both retained the flaw of legal reasoning referred to in 4.4.4.1. The appraisal of “fair share of benefit to consumers” did not concentrate on the retention level but spilled over into the pooling level.

#### **4.4.4.3 Indispensability of Restriction**

The first negative condition of indispensability relates to the concept of necessity and proportionality. The restriction could justify itself on two aspects: it is the only solution without alternative, and not out of proportion. This was held by *Cooperative Stremsel-en Kleurselafabriek v. Commission*<sup>95</sup> at the heart of its judgment.

In the context of the restricted quotation and minimum cost for tankers insofar as the retention level, the question of necessity is settled with no hurdle considering how the risk assessment is carried out in the underwriting of P&I insurance. Modern P&I associations apply an empirical approach to the individual characteristics, requirements and risk profile of a particular member.<sup>96</sup> Assuming that the restricted quotation and minimum cost for tankers are only applicable to the pooling level, the separate risk assessment over the retention level should be provided objectively and accurately as a prerequisite. However, severability with respect to risk assessment between the pooling level and retention level is not feasible due to the fact that “as risk assessment is based on subjective parameters (such as vessel safety measures and training of the crew), it would be easy for a club to manipulate this assessment by decreasing the relative weight of the retention costs and

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<sup>93</sup> *Ibid.* 92

<sup>94</sup> *Ibid.* 4 para 41 and *Ibid.* 5 para 108

<sup>95</sup> Case 61/80 [1981] ECR 851

<sup>96</sup> *Ibid.* 86 p.98

increasing the weight of the shared cost.”<sup>97</sup> For the sake of preventing quotation of discriminatory rate, preserving the principle of mutuality and accordingly continuing of the pool arrangements, the restricted quotation and minimum cost for tankers, even on the retention level, are borne out of necessity in the absence of any viable alternative.

Under the parameter of proportionality, it is hard for the restricted quotation and minimum cost for tankers to spill over the boundary when the pre-30 September procedure of de-administrative costs is incorporated. The rules indeed have been tailored strictly. The mechanism which is thus set up appears to the Commission to constitute an acceptable compromise between the legitimate interests of the clubs in maintaining stable membership and the interests of the operators who now take advantage of competition between clubs with respect to rates and services offered.<sup>98</sup>

By comparison, the 1999 Commission Decision discussed indispensability of restriction mainly on the side of necessity while the 1985 Commission Decision shed more light on the side of proportionality. Different approaches lead to the same conclusion, notwithstanding a more cogent explanation would have been provided if the arguments on both sides had been combined.

#### **4.4.4.4 Non-elimination of Competition**

The final condition concerns the question of to the extent of the effect of the agreements could have with respect to eliminating competition. The analysis cannot be made apart from the uniqueness of P&I insurance, the system of levying calls, which differs from single premium or regular premium in general insurance. Before the commencement of the policy year, “club managers calculate the total ‘premium’ for the year as a figure of 100% and then proceed to call up, as an advance call, a proportion of that total, say 75%, leaving the remaining 25% to be collected by way of supplementary calls.”<sup>99</sup> Moreover, levying supplementary calls is further subject to a proviso of flexibility that any such estimate shall be without prejudice within the right of the directors to adjust at a greater or lesser

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<sup>97</sup> *Ibid.* 5 para 111

<sup>98</sup> *Ibid.* 4 para 49

<sup>99</sup> *Ibid.* 86 p.104

percentage than indicated. Under this rate mechanism of so called “insurance on credit”, quotation in advance is not final binding and hence could not determine the premium competition single-handedly. Taking supplementary calls into account, it is not a corollary for the restricted quotation and minimum cost for tankers to eliminate competition on the level of actual total calls.

The Commission also recognized that “competition among the P&I clubs on the elements of rate reflecting the cost of claim (the elements subject to the quotation procedure) is a very important parameter of competition, but it is not the only one. Clubs remain free to compete on non-price parameters (such as the level of claim-handling service) as well as on the part of the rate which reflects the administrative costs.”<sup>100</sup> Indeed, price rivalry is not the fundamental competition in the P&I insurance market, where service quality carries weight in the competitive process. More concerns should be bestowed on long-term competition of loss prevention, claim handling and counseling service rather than price-cutting of short-termism. On this ground, the restricted quotation and minimum cost for tankers are far away from the elimination of competition here.

Additionally, it is laudable that the 1999 Commission Decision underlined that elimination of competition could not be established, “despite the fact that IG covers 89% of the world wide market for P&I insurance”<sup>101</sup>. It implicated that “dominant position” in Article 102 TFEU could not be read intuitively as a synonym for “elimination of competition” in Article 101(3) TFEU. This was later reaffirmed by the GC in the judgment on the *TAA* appeal<sup>102</sup> with the opinion that “the prohibition on eliminating competition is a narrower concept than that of the existence or acquisition of a dominant position”.

#### **4.4.4.5 Conclusion**

Given that four separated and cumulative conditions in Article 101(3) TFEU were all fulfilled, the restricted quotation and minimum cost for tankers as far as the retention level

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<sup>100</sup> *Ibid.* 5 para 114

<sup>101</sup> *Ibid.* 5 para 113

<sup>102</sup> Case T-395/94 [2002] ECR II-875

were granted the individual exemption as the final treatment by the Commission, valid from 1999 until 2009.

## **4.5 Legal Assessment of Pooling Agreement and IGA under Article 102 TFEU**

### **4.5.1 Relevance of Article 102 TFEU to Pooling Agreement and IGA**

As the twin of Article 101 TFEU, Article 102 concerns abuse of the dominant position including but not limited to (a)-(d). As a matter of fact, the instances hereunder largely overlap with the conducts proscribed by Article 101(1) TFEU. Since the Pool Agreement and the IGA are granted the individual exemption and deemed compatible with Article 101 TFEU, it appears reasonable to question whether they still risk being targeted by Article 102, which to some extent shares identity with the former.

3.1.2 has elaborated that P&I insurance is a long-standing oligopolistic market, owing to collective dominance of the IG Clubs. From the perspective of the Commission as the authority, the oligopolistic market is unquestionably the most intractable arena to implement competition policy. On the demand side, buyers are highly susceptible to potential abuse of dominance due to inelastic demand with limited room for bargain. On the supply side, “oligopolies often manage to adjust their relationships with competitors to mutual advantage”<sup>103</sup>. Whereas collective dominance had been conspicuous at the heart of oligopoly for a long period, the Commission did not illustrate the simultaneous applicability of Articles 101 and 102 TFEU to it until *Italian Flat Glass*<sup>104</sup>. On the strength of this Commission Decision, double straightjackets were put on oligopolies, with Article 102 combining with Article 101 to cope with collective dominance via “economic links”. Afterwards, this reinforced approach was assented to and reiterated by the ECJ in *Compagnie Maritime Belge v. Commission*<sup>105</sup> as follows: “it is clear from the very wording of [Article 101 and Article 102] that the same practices may give rise to an

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<sup>103</sup> *Ibid.* 26 p.375

<sup>104</sup> [1989] OJ L33/44

<sup>105</sup> *Ibid.* 11

infringement of both provisions. Simultaneous application of [Articles 101 and 102 TFEU] cannot be ruled out *a priori*.”

As a conclusion, oligopoly via collective dominance may contravene two main headings of the EU competition law synchronously. In this scenario, the credits gained in the examination upon Article 101 TFEU could not transfer to the appraisal under Article 102. The Pooling Agreement and the IGA, though acceptable under the former one, still needs scrutiny by the latter. The 1999 Commission Decision slurred over the relevance of Articles 102 TFEU to the Pooling Agreement and the IGA, which should be made out as the prerequisite for discussion.

## **4.5.2 Appraisal of Abuse**

### **4.5.2.1 Conception, Classification and Approach**

The wording of Article 102 TFEU, “such abuse may [...] in particular [...] consist in”, means that the items in (a)-(d) hereunder are not intended to exhaust all examples. The deductive approach adopted by Article 102 shows more flexibility comparing with Article 101 and leaves open a wide margin to various new circumstances. Academically, abuses are often classified into exploitative and exclusionary. Exploitative abuses are imputable to the detriment of consumers directly while exclusionary abuses, on the other dimension, are engaged in undermining the competitive process where contenders are involved.

It is remarkable that “the authentic English text of the Treaty uses the single word ‘abuse’, but most of the other languages use the double concept of ‘abusive exploitation’”<sup>106</sup>. It implies that, as the starting point, exploitative abuse was the main target of Article 102 TFEU, which places importance primarily on the protection of consumers, for example prohibiting the imposition of unreasonable terms and conditions. It corresponds to “consumer welfare” (referred in 4.4.4.2) adopted by the EU competition authority as the policy goal.

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<sup>106</sup> *Ibid.* 59 p.136



However, the concept of abuse was expanded to the dimension of exclusion in the leading authority *Hoffmann-La Roche*<sup>107</sup> as follows: “the behavior of an undertaking in a dominant position which is such as to influence the structure of a market where, as the result of the very presence of the undertaking in question, the degree of competition is weakened and which, through resources to methods different from those which condition normal competition in products or services on the basis of the transactions of commercial operators, has the effect of hindering the maintenance of the degree of competition still existing in the market or the growth of the competition.” New concerns addressed the distortion of market structure via weakening competition by the dominant, *i.e.* exclusionary abuse.

There is no denying that prominence of institutional legislation has long been given to Article 101 TFEU in the implementation of the EU competition policy, leaving the application of Article 102, to which less resources were devoted, at the formalistic level. The disequilibrium in this connection had not been ameliorated until the Commission adopted and published the 2008 Guidance (to be discussed in 5.3), which became to represent a reform-minded approach more economic and effect based by introducing new parameters and tests. Before the innovation of this much awaited 2008 Guidance, nonetheless, case law of the EU Courts and the Commission predominated in the analysis of Article 102 TFEU. The 1999 Commission Decision was made under this pre-2008 reign of case law. Not surprisingly, only the principles distilled from the precedents could be applied to the following appraisal of exploitative and exclusionary abuses at that time, even though from today’s perspective they may be in conflict with the modernised 2008 Guidance.

#### **4.5.2.2 Non-Exploitative Abuse: Minimum Common level of Cover**

As explained in 4.5.1, even though not imputable under Article 101 TFEU, the minimum common level of cover is still object to appraisal by Article 102 TFEU. The relevant fact

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<sup>107</sup> *Ibid.* 24

has been stated in 4.3.2.2 and it *prima facie* constitutes “limiting production to the prejudice of consumers”<sup>108</sup> within the meaning of Article 102(b) TFEU.

Two leading authorities were provided by the ECJ to draw the boundary between exploitative abuse and ostensible abuse on limiting production, *United Brands Company and United Brands Continentaal BV v. Commission*<sup>109</sup> and *British Petroleum v. Commission*<sup>110</sup>. In *United Brands*<sup>111</sup> involving resale of bananas, the ECJ acknowledged that limiting production could be justified for the assurance of quality as a legitimate interest. The *BP*<sup>112</sup> case in the scenario of supply shortage showed another reasonable defence based on certain external causes. They combined to offer a template of objective justification to certain behaviors of limiting production, which may be perceived as exploitative abuse outwardly but indeed should fall outside the scope of Article 102 TFEU for being legal *per se*.

The 1999 Commission Decision did not directly quote these two precedents, however the articulation of objective justification was present in the legal reasoning to the minimum common level of cover. Empirical analysis on large claims and successful experience of shipping industry thereunder were provided to obtain the justification that “from an objective point of view, the new level of cover cannot be considered incapable of meeting customer needs”<sup>113</sup>. In view of this, exploitative abuse on limiting production could not be established in the context of the minimum common level of cover.

#### **4.5.2.3 Non-Exclusionary Abuse: Reinsurance Provisions**

Before the 1997 Statement of Objections, the Pooling Agreement had set forth the conditions in regards to offering reinsurance to mutual insurers outside the IG but without procedure rules. Even worse, stock insurers had never been considered for such reinsurance arrangements. These unilateral provisions barely on the framework level left

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<sup>108</sup> *Ibid.* 5 para 128

<sup>109</sup> *Ibid.* 12

<sup>110</sup> Case 77/77 [1978] ECR 1513

<sup>111</sup> *Ibid.* 12

<sup>112</sup> *Ibid.* 110

<sup>113</sup> *Ibid.* 5 para 131

too much discretion to the IG in determining whether or not reinsurance could be offered to a third insurer and therefore constituted exclusionary abuse within the meaning of “dissimilar conditions” in Article 102(c) TFEU. Adopting the 1997 Statement of Objections, the IG notified amendments to Appendix X of the Pooling Agreement 1998, which supplemented detailed criteria and appropriate procedures governing reinsurance offers to mutual insurers as well as stock insurers.

The obligation to refrain from exclusionary abuse since *Hoffmann-La Roche*<sup>114</sup> was later named by the ECJ as “special responsibility” not to impair undistorted competition in *Nederlandsche Banden-Industrie Michelin v. Commission*<sup>115</sup> and reached a crescendo at *Tetra Pak International SA v. Commission*<sup>116</sup> where the oligopoly of over 90% market share was imposed on more onerous duty in the competitive process. Similarly, in *Oscar Bronner v. Mediaprint*<sup>117</sup>, AG Jacobs referred that there may be wider duties to help rivals where the super-dominant position is found. From today’s perspective, this “sliding scale approach” to special responsibility seems controversial and no more favored by the 2008 Guidance. Its factual protection of competitors weakened the protection of consumers as the first priority in the EU regime of competition law. Nonetheless, it offered some stretching notions to deal with different situations in different market structure at that time. One example is the creation and development of “essential facilities”. It is of high relevance to the oligopolistic market, *inter alia* P&I insurance here structured by reinsurance.

The doctrine of “essential facilities” derived from a series of cases in transport sector involving utilization of harbours or ports such as *Sea Containers v. Stena Sealink*<sup>118</sup> and *Maritime Container Network*<sup>119</sup>. By virtue of these Commission Decisions, the duty was imposed on the dominant undertaking to open its facility on a non-discriminatory basis to rivals by request for business operation. Otherwise, the dominant undertaking could be condemned for exclusionary abuse. However, this initial notion was shrunk by the ECJ in

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<sup>114</sup> *Ibid.* 24

<sup>115</sup> Case 322/81 [1983] ECR 3461

<sup>116</sup> *Ibid.* 13

<sup>117</sup> *Ibid.* 14

<sup>118</sup> [1994] OJ L 15/8

<sup>119</sup> [1994] OJ L 104/34

*Oscar Bronner*<sup>120</sup> to the extent of indispensability. Only if there are no alternatives or substitutes for the facility and it is unreasonably difficult for a competitor to replicate it, would the dominant company be obliged to grant access to it.<sup>121</sup>

The 1999 Commission Decision tacitly absorbed the essence of aforesaid case law and addressed that “independent insurers are not able to obtain reinsurance for large P&I cover, owing to their limited market shares”.<sup>122</sup> As the starting point, the doctrine of “essential facilities” was adopted for appraisal of the reinsurance provisions under Article 102 TFEU. Should there had been no adoption of the Statement of Objections, the IG as the oligopoly would doubtless have constituted escaping special responsibility and thereby exclusionary abuse. However, this was not the case. The IG finally provided objective conditions in relation to the provision of reinsurance and adequate procedures allowing any independent P&I insurers to acquire reinsurance from the IG.<sup>123</sup> On this ground, exclusionary abuse on refusing access to essential facilities could not be established in the context of the reinsurance provisions.

#### **4.5.2.4 Conclusion**

With analysis to case law above annotated, it is safe to reach the conclusion that the amended Pooling Agreement and the IGA would no longer give rise to an infringement of Article 102 TFEU.

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<sup>120</sup> *Ibid.* 14

<sup>121</sup> *Ibid.* 26 p.362

<sup>122</sup> *Ibid.* 5 para 135

<sup>123</sup> *Ibid.* 5 para 136

## **5 Prospects of Pooling Agreement and IGA under Reopened EU Competition Probe**

### **5.1 Delineation of Reopened Commission's Competition Probe and Altered Legal Environment**

The validity period of the 1999 Commission Decision granting exemption for ten years expired in February 2009. Afterwards, it should come as no surprise that the Commission reopened the competition probe into the Pooling Agreement and the IGA, which was launched in August 2010.

Comparing with the previous two competition reviews in the past thirty years, there is no specific complaints from the side of shipowners on this occasion and consequently the IG believes that the Pooling Agreement and the IGA “may be expected to benefit ‘automatically’ from exemption as long as there are no material changes in the way in which the Group is structured and operates and there are no major changes in the basic structure of the P&I market.”<sup>124</sup> However, the Commission disapproves of allowing exemption to roll forward *a priori*, albeit no conclusive proof of contravening competition rules has been new found to prompt the proceedings. The DG Comp officials have begun background research and canvassed shipowner views.<sup>125</sup> Hopefully the direction of the investigation as well as the new issues will become clear as time goes by.

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<sup>124</sup> IG (2008)

<sup>125</sup> Arthur J. Gallagher (2011)

It is clear that the Commission is undertaking a very serious and in-depth probe to the Pooling Agreement and the IGA presently. The third investigation is doomed to be substantive and much more than a ritual one, bearing in mind that in the first decade of the new century past, being tranquil exemption period in the IG's eyes, the external legal environment has experienced fundamental alteration. The modernised Regime of Regulation 1/2003, having far reaching impact on the implementation of Article 101 TFEU, has been established to replace the old system of Regulation 17/62. The long awaited 2008 Guidance has been finalized from the Discussion Paper and provides the new approach to Article 102 TFEU. After the incident of *Erika*<sup>126</sup>, the IG has been deeper involved in the oil pollution liability regime with STOPIA and TOPIA incorporated since 2006. The IG's unparalleled performance in this arena is envisaged to obtain environmental consideration by the Commission in its implementation of competition policy, but it is still hard to reach a palatable conclusion considering the ambivalence between the 2004 Guidelines and the TFEU on this point. Anything less than overall scrutiny to these eventful themes before the observation and suggestion will not help the prospects of the Pooling Agreement and the IGA under the reopened Commission's competition probe.

## **5.2 Modernised Regime of Regulation 1/2003 and Its Impact on Appraisal of Pooling Agreement and IGA under Article 101 TFEU**

### **5.2.1 Self-Assessment instead of Notification and Authorization**

It has been stated in 4.1 that the EU regulatory regime of competition experiences two stages: the early years under Regulation 17/62 and the new era with the adoption of Regulation 1/2003. The previous two EU competition reviews to the Pooling Agreement and the IGA were both under the auspices of Regulation 17/62. With the theme of centralized notification and authorization, the old system of 17/62 was well suited for the EU in its youth of limited Member States. "It enabled the Commission to build up a coherent body of precedent cases, and to ensure that the competition rules [in particular Article 101 TFEU] were applied consistently."<sup>127</sup> However, it had the unintended

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<sup>126</sup> MV Erika, a tanker with roughly 20,000 tons of fuel oil as cargo, sank off the coast of Brittany in 1999, releasing massive oil and causing the greatest marine pollution to France in 20<sup>th</sup> Century.

<sup>127</sup> EU (2004)

consequence of a massive backlog of notifications, most of which would turn out to be non-imputable before the Commission but would deplete limited administrative resources. This situation could not be resolved as time went by and meanwhile the enlargement of the union increased the Commission's stress in this connection.

In order to allocate administrative resources effectively and ensure supervision in the changed circumstances, the Commission initiated a momentous modernisation, with Regulation 1/2003 taking the place of Regulation 17/62 starting in May 2004. The most notable change in Regulation 1/2003 is the abolition of the notification and authorization system of Regulation 17/62 and the introduction of a legal exception system of direct applicability to Article 101(3) TFEU. According to Article 1 of Regulation 1/2003, Article 101 TFEU now takes direct effect as a whole and prior decision under Regulation 17/62 by the Commission is no longer required as a prerequisite for the application of Article 101(3) TFEU.

This development is reasonable to the Commission considering sufficient experience has been gained by making decisions on numerous individual cases in the past 40 years of competition policy implementation. Nonetheless, on the position of undertakings, the new system that shifts from prior notification and authorization to *ex post* control indicates that self-assessment of legal risk has to be carried out. To the IG, it means that the individual exemption under the notification and authorization system is not available anymore. Hence the self-assessment of the Pooling Agreement and the IGA now has to be completed with regard to its compatibility with Articles 101(1) and 101(3) TFEU as if they were conflated.

### **5.2.2 No Help from Renewed Insurance Block Exemption Regulation 267/2010**

Firstly, the block exemption is still of no help to the Pooling Agreement and the IGA under the new regime of Regulation 1/2003. The tide has not and will not turn from the previous Commission's Decisions on this point. In principle, the block exemption has no position in the modernised regime of Regulation 1/2003 but rather just is an exposition of the provisions of Article 101(3) TFEU for enforcement purposes. Moreover, in particular, the Commission on principle dislikes sectoral block exemptions unless the characteristics of

the sector are so special, and the lobbying power of its members so great, that a tailor-made block exemption is inevitable.<sup>128</sup> This standpoint could be strongly perceived from the renewal of insurance sector block exemption, which appears relevant to the Pooling Agreement and the IGA.

As the successor of Regulation 3932/92 (referred in 4.4.3), Commission Regulation No 358/2003 of 27 February 2003 on the application of Article 81(3) of the Treaty to certain categories of agreements, decisions and concerted practices in the insurance sector (Regulation 358/2003) was supposed to expire in 2010. Even having received outright dissent from the CEA<sup>129</sup>, the European insurance and reinsurance federation that represents all types of insurance and reinsurance undertakings, the Commission insisted on its original proposal on the renewal of Regulation 358/2003. It finally narrowed the scope of exemption and applied a harsher calculation of market share as what we see now in Regulation 267/2010. These variations are disadvantageous to all insurers and indicate more intense enforcement of competition rules to the whole insurance sector.

With this background, it is a sobering thought to thoroughly reduce the relevance of insurance block exemption to the Pooling Agreement and IGA especially when the bias of block exemption against the oligopoly, here the IG, is aggravated by the new formula of calculating market share in Regulation 267/2010.

### **5.2.3 Conceivable Procedure of Commitment Decision**

On the basis that the renewed insurance block exemption, Regulation 267/2010, still can not provide any help to the Pooling Agreement and the IGA, the self-assessment of potential competition issues will return to the criteria laid down by Article 101(3) TFEU in the modernised procedure stipulated by Regulation 1/2003. Although the notification and authorization system has been abolished, the negotiated settlement procedure at the time of Regulation 17/62 is inherited by Regulation 1/2003 and codified as Article 9, *inter alia*, the commitment decision.

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<sup>128</sup> *Ibid.* 26 p.612

<sup>129</sup> CEA (2009)



Roughly analogous to the US consent decree, Article 9 empowers the Commission to early terminate its proceedings without any formal finding of competition law violation. The Commission is entitled to adopt decisions giving legal force to commitments proposed by the undertakings concerned, instead of making prohibition decisions upon Article 7. This commitment procedure is introduced into Regulation 1/2003 and operated by the Commission to “increase the administrative efficiency in public enforcement by securing early closing of cases, and thereby saving of resources, where there are no hard-core violations which require punishment and where the parties cooperate with the public authority by showing their willingness to take action to address the negative effects of their behaviour”<sup>130</sup>. Recital 13 of Regulation 1/2003 excludes the finable infringements from the application scope of Article 9 and foresees a formal settlement procedure to ancillary restraints of competition.

It has been construed in 4.1.1 that the Pooling Agreement and the IGA by nature of claim sharing are operated with no hard-core violation of competition law. Simply ancillary restraints are envisaged to receive a treatment upon Article 9, rather than Article 7, by the Commission under the modernised regime of Regulation 1/2003. When the potential competition issues of the Pooling Agreement and the IGA eventually materialize, the commitment decision will be the fitting instrument from the Commission’s point of view. On the IG’s side, it would be optimal as well because securing of the commitment decision circumvents a protracted Commission’s investigation and the possible appeal before the EU judicature involving excessive legal costs and uncertainty in the future.

While such consensual preference of the Commission and the IG for the likely commitment decision can be understood, it should be pointed out that the Commission has not issued any substantive guidance on the application of the commitment decision under Article 9, despite the fact that other aspects of the self-assessment regime initiated by regulation 1/2003 have been clarified by various soft law in the meantime. However, the legal lacuna left by the secondary legislation on this point has been more or less filled lately by the final judgment of *Alrosa*<sup>131</sup> where the Commission’s exercise of the

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<sup>130</sup> Cengiz (2010) p.130

<sup>131</sup> *Ibid.* 17

commitment decision was first challenged before the EU judicature. By virtue of this leading case, the ECJ has provided “interesting guidance on the nature and scope of the Article 9 procedure and on the obligations of the Commission when resorting to it in a particular case”.<sup>132</sup>

In the case of the Pooling Agreement and the IGA, the focus of the reopened probe will be placed on certain provisions that narrowly escaped from the previous Commission Decisions but have provoked controversy later in the sectoral practice. Several industry reports<sup>133</sup> concurrently infer that, with the imputation of disproportionality, the release call may be the prime target in the new round investigation. 5.5 in the end will provide some observation and suggestion to help the release call acquire the redeeming virtues of Article 101(3) TFEU under the envisaged commitment procedure and the enlightenment from *Alrosa*<sup>134</sup>.

### **5.3 2008 Guidance and Its Consequence on Assessment of Pooling Agreement and IGA under Article 102 TFEU**

#### **5.3.1 Approach Shifted from Formalistic to Economic-Focused**

4.5.2 has justified that the Pooling Agreement and the IGA, by adopting the Statement of Objections, should not be longer condemned for abuse of dominance. This position of the 1999 Commission Decision is not likely to be changed, but rather strengthened when the prolonged Discussion Paper finally results in the 2008 Guidance on exclusionary abuse of dominance, which applies a more economic-focused approach to the enforcement of Article 102 TFEU.

It is widely oppugned by many academics and consultants<sup>135</sup> that as to whether certain conduct would or nor lead to anti-competitive foreclosure, case law of the EU Courts and decision-making practice of the Commission used to slide into formalistic analysis. In

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<sup>132</sup> Latham & Watkins LLP. (2011)

<sup>133</sup> *Ibid.* 2 and 129

<sup>134</sup> *Ibid.* 17

<sup>135</sup> *Ibid.* 59 p.469

order to shift this approach and provide greater clarity and predictability on the application of Article 102 TFEU, DG Comp published the 2005 Discussion Paper and finalized it as the 2008 Guidance.

The 2008 Guidance introduces some new factors for assessment and tests into the analytic framework of Article 102 TFEU. Albeit the scope of the 2008 Guidance is limited to exclusionary abuses and not extended to exploitative abuses, it is helpful to grasp the trend led by the Commission on the enforcement of Article 102 TFEU and provide the outlook accordingly in the case of the Pooling Agreement and the IGA.

### **5.3.2 Substitute Efficiency Defence for Objective Justification to Minimum Common Level of Cover**

The primary approach shift in the 2008 Guidance is about competition defence, from the concept of “objective justification” to the doctrine of “efficiency defence”. As elaborated in 4.5.2.2, objective justification was distilled from *United Brands*<sup>136</sup> and *BP*<sup>137</sup>. The 1999 Commission utilized this concept to justify the minimum common level of cover. It also appeared in the 2005 Discussion Paper but is left out by the 2008 Guidance.

In the 2008 Guidance, a new doctrine of efficiency defence is established by paragraph 30, which sets four cumulative conditions (a)-(d). This in fact “imports the test of [Article 101(3) TFEU] into [Article 102]”.<sup>138</sup> Comparing with objective justification, efficiency defence additionally requires in paragraph 30(c) that the efficiency must be advantageous to the consumer as a new factor of assessment.

It is not clear whether the Commission will extend this efficiency defence to exploitative abuses in the near future. If so, then it is likely to be welcomed by the IG since the Pooling Agreement and the IGA have gained sufficient credits in the exam of consumer benefit under Article 101(3) TFEU (illustrated in 4.4.4.1 and 4.4.4.2). Just by legal analogy, the IG could mirror the tried-and-tested arguments to Article 102. Conversely, if there is no such

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<sup>136</sup> *Ibid.* 12

<sup>137</sup> *Ibid.* 110

<sup>138</sup> Gravengaard (2010)

reform in a short term, with respect to exploitative abuses, the IG could still rely on objective justification, which is robust enough to withstand the new probe, as long as there is no material change of the minimum common level of cover.

### **5.3.3 Replace Sliding Scale Test with Balancing Test to Reinsurance Provisions**

Under the parameter of exclusionary abuse, 4.5.2.3 also made mention of access to essential facility, *inter alia*, the provision of reinsurance as the special responsibility of the oligopolistic IG. The “sliding scale approach” to special responsibility established by a series of precedents before the EU judicature, nevertheless, made some controversy. It appeared to protect particular competitors much more than consumers.

This ambiguity is quenched by the 2008 Guidance’s opening remark, which reiterates that “the Commission is mindful that what really matters is to protect an effective competitive process and not simply protecting competitors.”<sup>139</sup> The 2008 Guidance does not follow the traditional methodology to make the division between refusals to supply good or services, intellectual property rights and access to essential facility. Instead, paragraph 81 sets down a new approach of universal applicability.

It could be inferred that the “sliding scale approach” to special responsibility is no more favoured by the Commission when the “balancing test” is established here. In the light of the new formula of greater clarity and certainty, no new deficiency is found to offset the quality of non-exclusionary abuse that has been affirmed by the 1999 Commission Decision. Conversely, the new balancing test that “the likely negative consequences to consumers must outweigh the negative consequences of a supply obligation to the dominant undertaking”<sup>140</sup> is hard to pass owing to the identification (explained in 4.4.4.2) between the insurer and insured in the “consumer owned” business of P&I insurance. Hence, it is not too ambitious to say that the amended reinsurance provisions will stay further away from the allegation of exclusionary abuse under Article 102 TFEU in the future.

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<sup>139</sup> The 2008 Guidance Para 1

<sup>140</sup> *Ibid.* 139 Para 81(3)

## **5.4 Increasing Complex Regime of Oil Pollution Liability Underpinned by IG and Ambivalent Environmental Consideration between 2004 Commission Guidelines and TFEU**

### **5.4.1 Developing CLC and Fund Convention underpinned by IG**

During the past several decades, oil pollution has been centralized as the key risk in the shipping industry followed by the increasing size of tankers. The landmark case of *Torrey Canyon*<sup>141</sup> in 1967 initiated international focus to make global compensation schemes for oil pollution damage, which resulted in the CLC of 1969 and the Fund Convention of 1971. Two combined conventions established channeling liability to the shipowner, its P&I insurer and the oil pollution fund financed by the oil companies. Furthermore, they were combined with some new protocols to form the revised version of 1992. The compensation regime of 1992 CLC and Fund Convention preliminarily satisfied chronological ascending liability, notwithstanding further measures were provoked by a second milestone incident of *Erika*<sup>142</sup> in 1999.

Following the sinking of *Erika*<sup>143</sup>, the international liability and compensation regime (1992 CLC and Fund Convention) relating to persistent oil spills from tankers was reviewed by the clubs and the International Oil Pollution Compensation Funds (IOPC).<sup>144</sup> As the compromise between the IG and IOPC on the distribution of increasing liability, a new Supplementary Fund Protocol 2003 was approved and took effect from 2005 to “treble the amounts available for oil pollution compensation as compared with previous scheme.”<sup>145</sup> Under the Supplementary Fund Protocol 2003, two agreements have been reached, namely, STOPIA 2006 and TOPIA 2006. On the side of the IG, a greater burden of oil pollution compensation is imposed by these two agreements. Minimum limit of the IG for small tankers under CLC is raised from SDR 4.5 million to SDR 20 million and

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<sup>141</sup> The *Torrey Canyon* was a supertanker capable of carrying a cargo of 120,000 tons of crude oil, which was shipwrecked off the western coast of Cornwall, England in March 1967 causing an environmental disaster. At that time, the tanker was the largest vessel ever to be wrecked. --[http://en.wikipedia.org/wiki/Torrey\\_Canyon](http://en.wikipedia.org/wiki/Torrey_Canyon)

<sup>142</sup> *Ibid.* 129

<sup>143</sup> *Ibid.* 129

<sup>144</sup> *Ibid.* 86 p.181

<sup>145</sup> *Ibid.* 1 p.198

50% of the compensation from the Supplementary Fund will be indemnified by the tanker-owner members of the IG.<sup>146</sup> Also taking into account that the traditional “pay to be paid” rule is eroded by the prevailing direction action against the P&I insurer under CLC, the IG no doubt has over the years displayed flexibility and continues to play an unparalleled role in the increasing complex regime of oil pollution liability.

#### **5.4.2 Ambivalent Environmental Justification to Minimum Cost for Tankers**

In fact, the increasingly complex compensation scheme for oil pollution underpinned by the IG is not workable if it departs from the polluter pays principle, which has been institutionalized as the minimum cost for tankers in the IGA. However, the 1999 Commission Decision did not give a clear articulation of environmental consideration as a compelling justification to the minimum cost for tankers. It is interesting that earlier the same year in the *CECED*<sup>147</sup> case, the environmental benefit was recognized by the Commission, with the acknowledgement that the higher energy efficiency of new model would cause less pollution. This case ignited a theoretical contention as to whether environmental benefits could constitute “technical or economic progress” to balance against competition restraints, on which the 2004 Guidelines notwithstanding cast doubts. Literally, the 2004 Guidelines simply referred to “efficiency gains” but made no mention of the public interests justification like environmental or other social benefits. Considering the 2004 Guidelines was mostly rooted on case law and decision-making practice, silence on environmental consideration could be viewed as a departure from *CECED*<sup>148</sup> that did provide the exemption on environmental grounds. Protecting the environment is now a policy of the EU, but it is not entirely clear that the Commission should promote it at the expense of competition.<sup>149</sup>

Such a dim view to environmental consideration is concomitant to the doctrine of “pure economic efficiencies”, which has been later affirmed by the GC in *GlaxoSmithKline v.*

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<sup>146</sup> *Ibid.* 86 p.181

<sup>147</sup> *Ibid.* 16

<sup>148</sup> *Ibid.* 16

<sup>149</sup> *Ibid.* 59 p.94

*Commission*<sup>150</sup>. But it needs to be reappraised in a bigger picture when “Article 3(1)(g) of the Treaty of Rome, which establishes the maintenance of competition as a main activity of the Community”<sup>151</sup>, has been deleted from the opening articles of the TFEU. Bearing mind that “Article 3(1)(g) has been cited by the ECJ in several seminal cases in the development of European competition law, including *Continental Can*<sup>152</sup> and *Crehan*<sup>153</sup>, which concerned conflicting policy objectives”<sup>154</sup>, it may not be sensational that the EU judicature could change their position regarding the priority of competition policy in the EU legal order when invocation of Article 3(1)(g) is not available anymore. It was explicitly affirmed by the ECJ in *Eco Swiss China Time Ltd. v. Benetton International*<sup>155</sup> that “the provision of [Article 101 TFEU] may be regarded as a matter of public policy within the meaning of the New York Convention”. Should competition policy is treated equally with the other public policies including environmental task before the EU judicature, “pure economic efficiencies” will not necessarily be accented as the highest ranking.

On the grounds that the TFEU has taken effect from December 2009, the conflicts between competition promotion and environmental protection may be brought into the open and it is imperative for the Commission to reconcile the policy boundaries. Korah suggests that “it would be better to use [Article 106(2) TFEU] to reconcile conflicting [the EU] policies in relation to bodies entrusted with a task in the general interest because competition would then give way only to the extent necessary for the performance of the task”<sup>156</sup>, to which the IG’s operation under 1992 CLC is identical or comparable. The 1992 CLC stipulates that any shipowner of a tanker ( $\geq 2000$  tons of oil as cargo) is required to maintain compulsory insurance or other financial security for pollution liabilities. This obligation is mostly fulfilled by effecting P&I insurance and obtaining a “Blue Card” issued by the IG’s Club. Without the Blue Card, the CLC certificate cannot be issued by the authority and the shipowner will risk the detention of the vessel and criminal liability.<sup>157</sup> This being the case, the IG is entrusted with compulsory insurance for ascending oil pollution liability and thereby environmental consideration may provide a new alternative justification to the

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<sup>150</sup> *Ibid.* 15

<sup>151</sup> *Ibid.* 26 p.632

<sup>152</sup> Case 6/72 [1973] ECR 215

<sup>153</sup> Case C-453/99 [2001] ECR I-6297

<sup>154</sup> *Ibid.* 26 p.632

<sup>155</sup> Case C-126/97 [1999] ECR I-3055

<sup>156</sup> *Ibid.* 59 p.94

<sup>157</sup> *Ibid.* 86 p.180

minimum cost for tankers in the third investigation the to the Pooling Agreement and the IGA.

## 5.5 Observations and Suggestions

### 5.5.1 Remaining Issue: Wide Margin Discretion on Amount of Release Call

After an overall appraisal of the altered legal environment relating to the Pooling Agreement and the IGA, a fundamental rectification of the whole system seems to be overreached. It is legitimate for the IG to hold cautious optimism with regards to the net result of the third Commission's competition investigation. The remaining competition issue lies in the release call, which after modification was deemed as compatible with Article 101 TFEU by the previous two Commission Decisions but has received oft-repeated critiques from the shipping industry afterwards. The new concerns are raised as to the wide margin of discretion on the amount of release calls enjoyed by the IG Clubs. The prestigious insurance broker Tysers points out that "at the moment Clubs fix release calls at any figure they choose, with the current range varying from 0% to 30% in excess of any deferred call"<sup>158</sup>. Arthur J. Gallagher calls into question alike that "over the past 10 years, we have seen release calls as low as 0% and as high as 40% on policy years of similar maturity"<sup>159</sup>.

The release call is devised to fund the unbudgeted call arising on the policy year when the retiring member was in the Club. In the extreme case where there is no deficit in certain policy year, it is arguable to continue any release call levying. Even though release call levying *per se* was justified by the previous two Commission Decisions, the IG Club's exercise of this discretionary power on the call amount has not been addressed. It is vulnerable to the allegation of "apply[ing] dissimilar conditions to equivalent transactions" in Article 101(1) TFEU or "not indispensable" in Article 101(3). The divergence in approaches taken by the previous two Commission Decisions concerning whether the release call should be directly justified within Article 101(1) or further invoke exemption of Article 101(3) (explained in 4.3.2.3) is no longer of practical importance under the

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<sup>158</sup> *Ibid.* 20

<sup>159</sup> *Ibid.* 125



post-modernised EU competition law regime. When the notification and authorization system is abolished and Article 101(3) becomes directly applicable, Article 101(1) and Article 101(3) “may have been conflated and operated as if they were a single provision”.<sup>160</sup> In the “self-assessment world”, the IG bears the burden of proof to justify the release call under Article 101 TFEU as a whole. When the release call deviates from the proper functioning of the Pooling Agreement and causes ancillary restraints of competition (e.g. preventing the free flow of business to underwriters outside the IG), it will receive the commitment procedure prescribed by Article 9 of Regulation 1/2003, certainly, in the light of the latest ruling case of *Alrosa*<sup>161</sup>.

### 5.5.2 Enlightenment of *Alrosa* and Legal Advice

At the heart of the final judgment in *Alrosa*<sup>162</sup>, which upholds the Commission’s appeal and annulled the previous ruling of the GC, the ECJ has clarified that “the underlying administrative efficiency rationale and the participatory nature of commitment regime required application of a different, lighter standard in the judicial review of the proportionality of commitment decisions than that applied in the judicial review of prohibition decisions”<sup>163</sup>. Under this leniency, the acceptable scope and means of commitments proposed by undertakings could be wider than the remedies that the Commission could impose in an infringement decision following a full length investigation. It means that in the new era with the adoption of Regulation 1/2003, the ECJ retains and develops its deferential position of judicial review to the Commission’s “margin of appreciation”, which was established by *Consten & Grundig*<sup>164</sup> as far back as 1960s.

*Alrosa*<sup>165</sup> carries substantial importance to the IG, which is envisaged to offer the commitment likewise in exchange for possible earlier termination of investigation. The Commission’s extended discretion on Article 9 of Regulation 1/2003 assented by the ECJ’s ruling and its flexible timing of the commitment decisions in practice drive the risk-averse

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<sup>160</sup> *Ibid.* 26 p.106

<sup>161</sup> *Ibid.* 17

<sup>162</sup> *Ibid.* 17

<sup>163</sup> *Ibid.* 130 p.148

<sup>164</sup> *Ibid.* 20

<sup>165</sup> *Ibid.* 17

undertaking to offer onerous conditions as far as it could secure a commitment decision, since speculation on the Commission's action will be full of uncertainty. The Commission may always decide to conduct a full investigation with the aim of taking a prohibition decision if the settlement negotiations fail.<sup>166</sup> *Alrosa*<sup>167</sup> signals that under the EU judicature, it is legitimate, albeit probably not optimal, for the Commission in the new era with the adoption of Regulation 1/2003 to occupy a vantage position *vis-à-vis* the undertakings concerned and hence it is advisable for the IG to propose a "bullet-proof" commitment on the computation of the release call amount to be on the safe side. An operable solution is to set the ceiling, "perhaps based on 5% in excess of the average unbudgeted call made by each Club over a certain number of years"<sup>168</sup>. Additionally, a reduction in number of policy years subject to release calls, at the moment three years, may be over-needed but the IG may consider offering such a half-hearted proposal for securing a commitment decision.

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<sup>166</sup> *Ibid.* 130 p.136

<sup>167</sup> *Ibid.* 17

<sup>168</sup> *Ibid.* 20

## 6 Epilogue

In the world's P&I insurance market, the IG is a long-standing oligopoly of *fait accompli* owing to large economies of scale. The IG Clubs achieve and maintain such collective dominance via the Pooling Agreement and the IGA that fall into the application scope of Articles 101 and 102 TFEU simultaneously. However, it should be clarified that the Pooling Agreement and the IGA are merely ancillary restraints to competition rather than hardcore cartels. As a starting point, it determines what treatments the IG has received and will receive from the EU competition authority.

Concerning the previous two Commission Decisions, further analyses to non-profit making basis and non-binding recommendation of the IG are added for the sake of a tight argument to these boundary cases. In regards to the application of Article 101 TFEU, the 1985 Commission Decision was prone to direct invocation of paragraph (3) to all issues by reason of exclusive competence of the Commission on granting exemption as well as the IG's questionable alternative pleading for negative clearance or exemption under the old regime of Regulation 17/62. The 1999 Commission Decision overcame this path dependence and gave a more cogent legal reasoning under Article 101(1) TFEU that applied the counterfactual test and differentiated between the pooling level and the retention level. The minimum common level of cover and rules relating to release call, after modification were deemed compatible with Article 101(1) TFEU while the restricted quotation and minimum cost for tankers insofar as the retention level were left to be further examined under Article 101(3). The narrowed application scope of Article 101(3) TFEU to the Pooling Agreement and the IGA was of practical importance to the burden of proof under the notification and authorization system. Comparatively, the IG's onus to acquire

the redeeming virtues upon Article 101(3) TFEU was partly relieved by the 1999 Commission Decision.

Even though the 1999 Commission Decision stated that it was not clear from case law whether the insurance block exemption could also cover the Pooling Agreement and the IGA, it should be remarked that in fact the narrow approach to block exemption had been established before the EU judicature and consequently Regulation 3932/92 could only be construed rigidly. When Regulation 3932/92 was not applicable to the oligopolistic IG, the individual exemption was the final treatment to the Pooling Agreement and the IGA.

In regards to the appraisal of four conditions for providing the individual exemption, the 1985 and 1999 Commission Decisions both retained certain flaws in legal reasoning. On the point of “contribution to economic welfare”, the 1985 Commission Decision virtually shifted the argument to “indispensability of restriction” and made a dubious conclusion that equated “maintenance” of P&I insurance operation with “improvement” of insurance service. The 1999 Commission Decision touched “promotion of economic progress”, whereas its argument did not center on the retention level but rushed back to the pooling level paradoxically. Such a digression also existed in the appraisal of “fair share of benefit to consumers” by both Commission Decisions. A fair inference could be drawn from the feast or famine cycle of insurance premium and the “at cost” principle of P&I insurance. The restricted quotation and minimum cost for tankers, even on the retention level, endow the supply of P&I insurance with predictability and stability; create incentives for loss prevention and consequently better safety performance by the shipowners. Through these means, the economic process enjoys more efficiency. On the point of “indispensability of restriction”, the 1999 Commission Decision discussed indispensability of restriction mainly on the side of necessity while the 1985 Commission Decision shed more light on the side of proportionality. Different approaches lead to the same conclusion, notwithstanding a more cogent explanation would have been provided if the arguments on both sides had been combined. On the point of “non-elimination of competition”, it is laudable that the 1999 Commission Decision recognized that “dominant position” in Article 102 TFEU could not be read intuitively as the synonym for “elimination of competition” in Article 101(3) TFEU and price rivalry is not the fundamental competition in the P&I insurance market, where service quality carries weight in the competitive

process. Regrettably, both Commission Decisions made no allusion to the unique calls levying system of P&I insurance, under which quotation in advance is not final binding and hence could not determine the premium competition single-handed. Taking supplementary calls into account, it is not a corollary for the restricted quotation and minimum cost for tankers to eliminate competition on the level of actual total calls.

In regards to the application of Article 102 TFEU to the Pooling Agreement and the IGA, the 1999 Commission Decision made a relatively simple discussion with no reference to the approaches adopted. Actually, before the 2008 Guidance, the methodology of implementation of Article 102 TFEU was led by case law. A series of precedents are incorporated and annotated to help understand the Commission's reasoning. "Objective justification" was tacitly adopted by the Commission to the minimum common level of cover in respect of non-exploitative abuse. The doctrine of "access to essential facilities" as the "special responsibility" was also utilized by the Commission in the assessment of the reinsurance provisions with respect to non-exclusionary abuse. These approaches distilled from the bygone authorities may be in tension with the modernised the 2008 Guidance from today's perspective but they indeed offered useful notions to deal with different situations like the case of the IG at that time.

Looking ahead, the prospects of the Pooling Agreement and the IGA under the reopened Commission's competition probe cannot be provided without the analysis of altered legal environment. First and foremost, the modernised Regime of Regulation 1/2003, having far reaching impacts on the implementation of Article 101 TFEU, has been established to replace the old system of Regulation 17/62. To the IG, it means that the individual exemption under the notification and authorization system is no longer available and meanwhile the order of application between Article 101(1) and Article 101(3) TFEU is no longer of practical importance. Upon Regulation 1/2003, the self-assessment of the compatibility of the Pooling Agreement and the IGA with Articles 101(1) and 101(3) TFEU must now be completed as if the two Articles were conflated. The renewed insurance block exemption, regulation 267/2010, is still of no help. It should be perceived from the harsher formula of market share hereunder that the bias of block exemption against the oligopolistic IG is even aggravated. On these grounds, the Pooling Agreement and the IGA as the ancillary restraints of competition are envisaged to receive the

commitment decision, which inherits the negotiated settlement procedure at the time of Regulation 17/62 and is codified as Article 9 of Regulation 1/2003.

Meanwhile, the publication of the long awaited 2008 Guidance shifts the application of Article 102 TFEU from formalistic to economic-focused. Some new factors of assessment and tests are introduced and available to the IG. “Efficiency defence” could be a proper substitute for “objective justification” to minimum common level of cover and “balancing test” would replace “sliding scale test” to reinsurance provisions. Under the parameter of the 2008 Guidance, which places emphasis on the protection of consumers rather than competitors, the Pooling Agreement and the IGA will stay further away from the allegation of dominant abuse.

One interesting issue sidestepped by the 1985 and 1999 Commission Decisions is the environmental justification for the minimum cost for tankers. The increasing complex compensation scheme to oil pollution underpinned by the IG cannot work if it deviates from the polluter pays principle and accordingly it is conceivable for the minimum cost for tankers to obtain environmental justification. However, it is still hard to reach a clear-cut conclusion in view of the ambivalence between the 2004 Guidelines and the TFEU on this point. Hopefully the policy conflicts between competition promotion and environmental protection may be reconciled by the invocation of Article 106(2) TFEU considering the IG’s Clubs are entrusted with compulsory insurance of “general economic interest”.

After an overall appraisal of the altered legal environment relating to the Pooling Agreement and the IGA, a fundamental rectification of the whole system seems to be excessive. It is legitimate for the IG to hold cautious optimism on the net result of the third Commission’s competition investigation. The remaining issue lies in the release call, which after modification was deemed to be compatible with Article 101 TFEU by the previous two Commission Decisions but has received repeated critiques from the shipping industry afterwards. The new concerns are raised as to the wide margin of discretion on the amount of release calls enjoyed by the IG Clubs. The latest leading case of *Alrosa* providing interesting guidance on Article 9 procedure carries substantial importance to the IG, which is likely to offer the commitment when the problem of the release call is materialized. The ECJ’s ruling of *Alrosa* signals that in the new era with the adoption of

Regulation 1/2003, the Commission still enjoys a “margin of appreciation” established as far back as 1960s in practice of decision-making. Particularly in the commitment procedure, it will drive the risk-averse undertaking to offer onerous conditions as far as it could secure a commitment decision. Therefore, it is advisable for the IG to propose a “bullet-proof” commitment on the computation of the release call amount to be on the safe side.





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