

EU transportation: coordination in maritime mergers and strategic alliances

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In July and August this year, the European Commission (Commission) adopted two merger decisions in the field of maritime transport services. In Maersk/PONL¹ the Commission decided to clear the acquisition by A P Møller-Mærsk (Maersk) of Royal P&O Nedlloyd (PONL) subject to conditions. In part, the conditions were designed to remove the concerns of the Commission relating to potential co-ordination between the merged entity and its competitors arising from their mutual membership of liner conferences and consortia. In NYK/Lauritzen Cool/LauCool JV² (LauCool) the Commission decided to clear NYK Reefers' (NYK) acquisition of a 50 per cent stake in Lauritzen Cool (the other 50 per cent would be held by J Lauritzen). The joint venture would manage a pool of specialised reefer vessels, and NYK would contribute its own management activities and vessels to the joint venture. The Commission analysed two potential negative effects of the merger. First, whether the combined share of reefer capacity on different trades accounted for by the pool and the vessels contributed by NYK would be so substantial that there was a risk that effective competition would be significantly reduced. And second, whether the merger would create a risk of co-ordination as a result of, on the one hand, the existence of vessel sharing agreements and pools in the market (creating links between the parties and their competitors) and, on the other hand, the presence that both parent companies would retain in the upstream market for long term chartering of reefer capacity. This article only discusses the Commission's analysis of co-ordination as a result of vessel sharing agreements and, in particular, pools existing in the market and to which the merging parties are members.

Both decisions shed some light on the principles that the Commission applies in its assessment of co-ordinated effects in markets where the merging companies are parties to co-operative arrangements such as liner conferences, consortia or pools. The assessment focuses on the links between competitors that these arrangements create, which may lead to parallel behaviour. In particular, the Commission will as part of its assessment under the merger control rules assess whether the merger strengthens those links, thereby increasing the risk of co-ordinated behaviour.

Below, we first analyse the Commission's assessment of co-ordinated effects arising from mergers in markets where conferences and consortia exist. This is done on the basis of the Maersk/PONL decision. We then discuss the assessment of co-ordinated effects arising from mergers in bulk markets, where pools exist but where there are no conferences or consortia. This is done on the basis of the LauCool decision. Finally, drawing on the principles that can be derived from these two decisions, we analyse the extent to which (outside merger cases) the creation of and participation in strategic alliances in themselves may raise concern of co-ordination under article 81 EC.

Co-ordinated effects of mergers involving members of conferences and consortia

This was addressed in Maersk/PONL. The risk of co-ordinated effects resulting from the acquisition arose because both Maersk and PONL were members of several liner conferences and consor-

tia in the relevant markets. In some instances those memberships overlapped.

The background

Liner shipping conferences can generally be described as groups of vessel-operating carriers, which engage in price fixing and capacity regulation. These activities are exempted from the prohibition contained in article 81 EC by Council Regulation 4056/86.³ Conferences are required to set common or uniform freight rates and may make a common policy on the discounts or rebates, which may be offered to shippers in the geographical area covered by the conference. In addition, conferences fix surcharges and ancillary charges per trade, country, port or direction as relevant.⁴

Competition within conferences depends on the extent to which members rely on the joint tariffs set by the conference, or enter into individual service contracts with independent rate fixing. However, even in conferences where individual service contracts play an important role, internal competition will be restricted as the joint surcharges and ancillary charges are also imposed on cargo that transits under individual service contracts. These joint charges represent an important part of the total price for the sea leg of a journey in relation to which conference members do not compete.

Liner consortia are operational agreements between carriers on a trade-by-trade or global basis for the provision of a joint service. Unlike conferences, consortia do not price fix but nevertheless facilitate extensive co-operation between members. This co-operation ranges from vessel sharing, exchange of space or slots in vessels, equipment interchange, joint operation or use of port terminals and related services, temporary capacity adjustments to the participation in a revenue or a cargo pool, joint marketing and the issuing of a joint bill of lading. It is exempted from the prohibition contained in article 81 EC by Commission Regulation 823/2000.⁵

Competition between the members of a consortium will depend on the consortium structure and degree of integration of members' activities. However, a certain amount of commercially sensitive information is in general exchanged within consortia as part of the co-operation. In addition, consortia may operate within a conference and members can thus cumulate the benefit of both the conference and the consortia block exemptions.

As part of its analysis of the effects on competition of a proposed merger between carriers, the Commission takes into account the existence of conferences and consortia in the market by reference to the parties' memberships therein, the market shares accounted for by the conferences and consortia and the links between them. In that analysis, the Commission starts from the general assumption that competition within conferences and within consortia is restricted, and that the members of conferences and of consortia adopt a uniform conduct in the market. Where one or more of the parties to a merger are members of conferences or consortia, the merger may further reduce whatever internal competition exists and may also reduce the external competitive constraints that a conference or consortium faces by eliminating competition from previously independent carriers.

In P&O/Royal Nedlloyd⁶ the Commission for the first time considered to what extent the parties' membership in different consortia and conferences had to be taken into account in the assessment of the operation. It concluded that after the operation the parties would be contractually linked to other shipping lines with which they consequently would not be in full competition. The Commission therefore investigated whether the operation would strengthen the cohesion within an existing conference or consortium, which would create or strengthen a dominant position. That case law was further developed in Maersk/Safmarine⁷ and in Maersk/Sealand.⁸ These cases, however, did not give rise to substantial concern and the analysis was therefore less detailed than in Maersk/PONL.

The decision in Maersk/PONL

In Maersk/PONL the Commission set out, in general terms, the effects that the transaction might have on conferences and consortia depending on the parties' membership.⁹ Its analysis follows that in the earlier decisions mentioned above, but is more detailed and provides some guidance on specific issues not considered earlier. The Commission identified two general scenarios that may give rise to concern:

- In cases where the merging parties are currently in the same conference or consortium and remain members after the merger, the concentration would not change the total market share of the conference or consortium. Depending on the structure of the conference or consortium (see below), however, this could lead to a strengthening of the internal cohesion and eventually lead to the merged entity controlling the conference (the first scenario).
- In some instances Maersk was in a conference or consortium, but not PONL, even though it was active on the same trade. If Maersk maintained its membership, PONL could be expected to be integrated into the conference or consortium. The market share of the conference or consortium would rise. If only PONL was in a conference or consortium, the merger would create a link between Maersk and the conference and/or the consortium. This link would enable Maersk to take part in the exchange of information within the conference and/or the consortium. Maersk could use the commercially sensitive information exchanged therein to adapt over time its conduct on the market, thus increasing the risk of market sharing or lessening of competition between itself and the other members of the conference or the consortium. Even without integrating itself into the conference or the consortium, Maersk would no longer be an independent competitor because it controlled a member of the conference or the consortium (the second scenario).

Based on the above, the Commission carried through its analysis of co-ordinated effects in as many as 22 different trades. The analysis in relation to North Europe–North America trade on which the TACA conference and the Grand Alliance consortium operate is illustrative of its approach.

The first scenario

The Commission analysed whether the merger would lead to a strengthening of the internal cohesion in TACA, by taking into account:

- the reduction in the number of members in the conference post merger (from seven to six);
- the commercial weight that the merged entity would have within the conference (some 20 to 30 per cent of the volume of the conference); and
- the conference voting system in order to determine whether Maersk post-merger would have a controlling vote.

Finding that the number of members would remain relatively high (six), that the merged entity would not gain so substantial a commercial weight within the conference as to control it, and that the voting rules would not confer control upon Maersk, the Commission considered that the merger would not appreciably strengthen the coherence within TACA.

The second scenario

Second, the Commission analysed the impact that the transaction would have on the Grand Alliance that operates within TACA. PONL was a member of the Grand Alliance, but Maersk was not. The Commission's analysis in this respect is two-pronged. The Commission first pointed out that even without integrating itself into the consortium, Maersk would following the merger seize to be an independent competitor and would be in a position to gain access to commercially sensitive information enabling it over time to adjust its behaviour to that of its competitors. It also considered that Maersk would be able to influence operational decisions within the consortium. The Commission therefore aggregated the market share of Maersk and the Grand Alliance, which would reach some 40 to 50 per cent.

Then, as the second element of its analysis in relation to the Grand Alliance, the Commission considered that the link between Maersk and the Grand Alliance could influence the structure within TACA. All Grand Alliance members (except one) were also members of TACA and together represented a significant share of the TACA volume. That share would increase post merger resulting in members representing some 70 to 80 per cent of the TACA volume also being interlinked through the Grand Alliance. As a result, the internal cohesion in TACA would be strengthened, thereby increasing the risk of co-ordination.

Conclusion

On the above basis, and considering that the competitive constraints on the parties and TACA/the Grand Alliance were limited (there were only few independent competitors in the market, all accounting for significantly smaller shares and one of whom Maersk was linked to through a slot charter agreement), the Commission found that the transaction raised serious doubts as to its compatibility with the common market stemming from the co-ordinated effects likely to follow from the above links.

To alleviate this concern, Maersk committed to withdraw PONL from the Grand Alliance. This was sufficient to remove the serious doubts identified, as the link between Maersk and the Grand Alliance would be severed. The merged entity's combined share would be limited (10 to 20 per cent) and the Grand Alliance would be an effective competitor with an aggregate share of some 20 to 30 per cent.

Co-ordinated effects of mergers involving members of a pool

The background

Prior to the transaction in LauCool, Lauritzen Cool functioned as pool manager for the Leonina Fleet, a pool of specialised reefer vessels. Lauritzen Cool did not (including following the transaction) own any vessels, but chartered its capacity in on arm's length basis. Its core activities—the commercial management, operation and marketing of the fleet of reefer vessels in the pool—were conducted independently of its parents and the pool members. Each member provided its vessel capacity to the pool but did not influence Lauritzen Cool's actual operation and marketing. Vis-à-vis the market, the pool held itself out as a single entity.

The Commission's analysis

The Commission analysed the market characteristics in the bulk reefer sector in order to determine whether the market was conducive to co-ordination. In particular, it compared the co-operative arrangements existing in this sector with liner conferences and consortia. It observed that highly integrated consortia and conferences engaging in joint tariff setting were not present in the bulk reefer sector. This suggests that the Commission took account of the more effective price competition leading to more effective competition than in the case of consortia, most of which operate under the umbrella of joint tariffs and charges set by a conference.

The Commission furthermore observed that pools present themselves to the market as single entities providing a joint service, suggesting that the Commission took account of the fact that pool members generally do not retain competing activities outside the pool and that pools compete with each other.

As to the vessel sharing agreements in the bulk reefer market, the Commission noted that these do not typically involve any joint operation or joint marketing of services and are basically used as a means of procuring additional cargo space for an operator's own customers. As a result, they will not lead to strong links between the parties to the agreement.

On the above basis, the Commission considered that, as opposed to the liner shipping sector, the structural characteristics of the bulk reefer sector were not conducive to co-ordinated effects. That conclusion appears to be largely based on the absence of conferences, which in effect are price fixing mechanisms between carriers that continue to operate individual services, and the existence of effective competition outside the LauCool pool, dispelling any concern of co-ordinated effects. The Commission also found that barriers to entry in the market were low and that there was competition between different geographic trades.

Co-ordinated effects of strategic alliances

Article 81 EC prohibits agreements and concerted practices between undertakings that have as their object or effect to appreciably restrict competition.¹⁰ In assessing the effect of an agreement entered into between two or more competitors that may restrict competition, the European Commission will take into account the position of the parties in the market affected by the co-operation (and possibly in upstream, downstream or neighbouring markets), as well as the position and number of competitors and other indicators of competition in that (those) market(s). One of the elements that the Commission also may take into account is the existence of links between a significant number of competitors, in particular in markets that are concentrated, as the creation of additional links may 'tip the balance' and make co-ordination in the market more likely.

The 'network effects' that several agreements of a certain type can create, may also be one of the elements that exceptionally lead the Commission to withdraw the benefit of block exemptions on the basis that competition in the market is not effective and that the effect of an otherwise exempted agreement therefore is incompatible with article 81 EC.¹¹

Furthermore, while liner conferences and liner consortia are block exempted, co-operation between liner carriers going beyond the scope of those block exemptions will need to be assessed on the basis of the general principles for the application of article 81 EC.

The present section discusses co-ordinated effects of strategic alliances under article 81 EC. The term strategic alliances is in this respect used to broadly describe co-operative arrangements between competitors in relation to their operations. As such the term covers consortia, pools, vessel sharing agreements and other co-operative arrangements that creates links between the participating carriers.

The analysis of co-ordinated effects in merger cases focuses on

the effect that the merger produces on links between members of conferences or consortia. Such links, which the merger may create or strengthen, may lead to conference or consortia members behaving in parallel.

A separate issue is whether the participation in a strategic alliance leads to parallel behaviour caught by article 81 EC, because competition between the alliance and its members is restricted, or because competition between distinct alliances is restricted. The first scenario may arise where members retain individual activities outside the alliance that compete with the alliance. The second scenario may arise where carriers are members of several alliances that as a result are interlinked, and those alliances compete. Below, we address these issues by drawing on the principles that can be derived from the Commission's analysis in Maersk/PONL and in LauCool.

It would seem possible to derive the following principles from the above cases. First, where a strategic alliance operates a joint service, members are likely to exchange commercially sensitive information within the alliance. Where commercially sensitive information is exchanged, there is a risk that members use that information to align their independent behaviour outside the alliance. To alleviate such concern, the members may obviously seek to limit the information they exchange. However, any concern of co-ordination would also seem to be removed if the parties agree not to retain independent competing activities outside the alliance. A case in point is the pools that operate in the bulk sectors, most of which provide a joint service. Many pools operate on the basis of non-compete (or exclusivity) provisions requiring the participants to contribute all their capacity in the pool's segment to the pool. One difficulty that may arise, however, is the formulation of such provisions to make them effective without imposing restrictions going beyond the strictly necessary. If for example a strategic alliance is highly specialised, focusing only on a particular type of goods/vessels/geographic region, it may be difficult to ascertain whether the scope of the co-operation coincides the definition of the relevant market as it would be applied by a competition authority, or whether the alliance in fact only operates within a segment of that market. In such cases, the parties should be careful to avoid concern of market sharing if they retain independent activities that may in fact compete within the same market as the alliance.

Second, less integrated strategic alliances will in most cases not require the exchange of sensitive information and the links, in many cases, will not be so strong as to lead members to behave uniformly. Membership of one alliance may therefore not in itself give rise to any concern of co-ordination. One example of such an alliance could be the vessel-sharing arrangements referred to in LauCool. However, the presence of several strategic alliances in the same market (even if less integrated) may lead to concern if these alliances are interlinked. In assessing whether the links within a strategic alliance might be strengthened in a manner leading to concern of parallel behaviour, regard should be had to the number of members with overlapping memberships in other alliances, their relative weight (commercial or under voting rules) in the alliances, and the strength of the links created. Regard should also be had to the constraint exercised by independent competitors and the general competitive structure of the market. In LauCool the Commission did not find any cause for concern of co-ordination as a result of the pools in the market, largely due to the effective price competition between different pools and between pools and independent operators, as a result of the absence of conferences.

Conclusion

Mergers in markets where liner conferences, consortia and other strategic alliances play an important role, may raise concern of co-ordinated effects that significantly restricts competition. That

concern will be more prominent in liner shipping as a result of conferences and consortia than in the bulk sectors, where competition is more efficient and alliances generally are less integrated. Nevertheless, as the Commission moves forward with its pending review of the competition rules in the maritime transport sector, the block exemption for liner conferences may disappear, which may alleviate much of the concern of co-ordinated effects.

The principles that can be derived from the two merger decisions discussed here provide guidance to carriers contemplating mergers or strategic alliances with competitors. They also give an indication of some issues that it may be relevant to take into account in considering new forms of co-operation prompted by a removal of the liner conference block exemption. While it is clear that concern may arise under certain conditions, the principles applied by the Commission leave room for co-operation between competitors in the maritime transport markets as long as it does not lead to a significant restriction of competition.

Notes

- 1 Case No. Comp/M.3829 – Maersk/PONL, decision of 29 July 2005.
- 2 Case No. COMP/M.3798 – NYK/Lauritzen Cool/LauCool JV, decision of 19 August 2005.
- 3 Council Regulation (EEC) No. 4056/86 laying down detailed rules for

the application of articles 85 and 86 [now 81 and 82] of the Treaty to maritime transport.

- 4 See the Commission's decision in Maersk/PONL, paragraph 28.
- 5 See the Commission's decision in Maersk/PONL, paragraph 30. Liner consortia are block exempted pursuant to Commission Regulation (EC) No 823/2000 of 19 April 2000 on the application of article 81(3) of the Treaty to certain categories of agreements, decisions and concerted practices between liner shipping companies, as amended.
- 6 Case No IV/M.831 – P&O/Royal Nedlloyd, decision of 19 December 1996.
- 7 Case No IV/M.1474 – Maersk/Safmarine, decision of 7 May 1999.
- 8 Case No IV/M.1651 – Maersk/Sea-Land, decision of 6 October 1999.
- 9 See paragraph 32 of the decision.
- 10 Provided certain conditions are fulfilled article 81(3) provides that such agreements may nonetheless be exempted from the prohibition in article 81(1) EC.
- 11 For example, the block exemption for liner consortia in regulation 823/2000 provides in article 12 that the Commission may withdraw the benefit of the exemption where it finds in a particular case that an agreement exempted under article 3 or article 13(1) of the Regulation nevertheless has certain effects which are incompatible with the conditions laid down by article 81(3) or are prohibited by article 82. That is for example the case where in a given trade, competition from outside the conference within which the consortium operates or from outside a particular consortium is not effective.

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Arnold & Porter opened its Brussels office in August 2003 and it has since expanded to a team of 10 competition/antitrust lawyers. Most recently, Luc Gyselen, a senior official with the Directorate General for Competition (DG Comp) at the European Commission, joined the office as a partner. Heading the European competition practice from Brussels is EU competition expert Marleen Van Kerckhove. Ms Van Kerckhove and Mr Gyselen are joined by partner Susan Hinchliffe, who is permanently based in Brussels, and Tim Frazer, head of the UK competition practice, who divides his time equally between Brussels and London. The team collaborates with the head of Arnold & Porter's global antitrust practice, William Baer, who is based in Arnold & Porter's DC office but also spends a significant portion of his time in Brussels.