Crisis Cartels and the Triumph of Inudstrial Policy Over Competition Law in Europe

Andre Fiebig
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I. INTRODUCTION

The application of European competition law as codified in the Treaty Establishing the European Community is primarily the responsibility of the European Commission, which has traditionally been accorded much discretion by the European courts. Although the Commission is the “Guardian of the Treaty,” it is comprised of 20 Commissioners appointed by the Member States. It is therefore inevitable that they each are exposed to political influences which are not necessarily coincidental with the objectives of the EC Treaty. The exposure to political influences combined with the responsibility of applying the competition law inevitably creates some tension. This tension is particularly evident in the relationship between industrial policy and competition law. The Commission’s position on crisis cartels is one instance where industrial policy has triumphed over competition law. Although crisis cartels, as horizontal collusion to limit production, represent the most reprehensible types of anti-competitive practices, the Commission has been willing to bend the prohibition on cartels to

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support European industry under certain circumstances. This not only distorts the application of the competition rules, it imposes a serious social cost on Europeans.

II. THE MEANING OF THE TERM “CRISIS CARTEL”

Neither the European Commission nor the European Court of Justice has expressly adopted a definition of the term “crisis cartel.” Based on the Commission’s practice in applying the European competition laws, the term “crisis cartel” can be defined as agreements between most or all competitors in a particular market to systematically restrict output and/or reduce capacity in response to a crisis in that particular industry. There are three components to the definition. First, there must be an agreement between most or all of the competitors in a specific market. Although a cartel can be comprised of two or more members, the Commission applies the crisis cartel label only to horizontal agreements to reduce capacity which include most of the competitors in the particular sector. Agreements between only a few of the firms in a specific industry to reduce excess capacity are referred to as joint structural capacity reductions. Second, the objective of the cartel must be to systematically restrict output and/or reduce capacity. As discussed below, the Commission requires that as a condition to its approval the participants in the crisis cartel adopt a plan to systematically reduce capacity. Finally, the cartel must be

5. See COMMISSION OF THE EUROPEAN COMMUNITIES, 13TH REPORT ON COMPETITION POLICY 1984 55, para. 61 (1984) [hereinafter 13TH REPORT]. There are two types of joint structural capacity reductions. The first of these falls under the heading “reciprocal specialization.” 23RD REPORT, supra note 3, at 49, para. 86. In the early 1980s, for example, two British petrochemical companies, Imperial Chemicals Industries (ICI) and British Petroleum (BP) entered into an agreement whereby BP specialized in low density polyethylene and ICI in polyvinylchloride. The Commission permitted the agreement because “the closures of the older plants reduced capacity in sectors that were suffering from structural overcapacity.” COMMISSION OF THE EUROPEAN COMMUNITIES, 14TH REPORT ON COMPETITION POLICY 1984 71, para. 84 (1988). See BPCI/ICI, 1984 O.J. (L 212) 1. See also ENI/Montedison, 1987 O.J. (L 5) 13; COMMISSION OF THE EUROPEAN COMMUNITIES, 17TH REPORT ON COMPETITION POLICY 1987 70, para. 74 (1988).
6. See 23RD REPORT, supra note 3, at 48, para. 84; 12TH REPORT, supra note 4, at 45, para. 39.
7. See 23RD REPORT, supra note 3, at 48, para. 85; 12TH REPORT, supra note
in response to a crisis in the relevant industry. The term “crisis” in this context refers to a situation of prolonged structural excess capacity in a particular industry causing many or most of the incumbent firms to operate at a loss.

The difficulty in defining crisis cartels in the context of European competition law is that the Commission uses a definition of excess capacity that is broader than the definition generally used in economic theory. The Commission applies the term “excess capacity” to the difference between the industry’s maximum possible output using existing facilities and the actual output of that industry. In contrast, an economist would say that an industry is experiencing excess capacity when the incumbent firms are producing at an output level which is below that at which average costs are at a minimum. Under this definition an industry may be producing at full capacity even though it has not achieved maximum possible output. This occurs when the firm is producing at the lowest level of its average total costs curve and this level is less than maximum output. For example, where a firm is producing 100 widgets at a cost of $10 each, but the lowest point on its average cost curve is 150 widgets at a cost of $7 each, there is excess capacity of 50 widgets.

In addition, the excess capacity must be structural. According to the Commission, structural excess capacity exists, where over a prolonged period all of the undertakings concerned have been experiencing a significant reduction in their

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8. Based on the requirements established by the Commission, a crisis cartel is not permissible in service industries. For example, the Commission has taken the position in response to overcapacity in the air transport sector that it will “never” accept cartels aimed at reducing capacity. See Comments of Competition Commisar Van Miert, reported in Ministers Discuss the Crisis—No Cartel Will be Authorized, Either to Reduce Capacities or to Set Prices, Says Mr. Van Miert, AGENC EUROPE, 27/28, 1993 at 5. See also David Gardner, No Backtracking on ‘Open Skies’ policy, says Brussels, Fin. TIMES, Sept. 28, 1993, at 20.

9. See 23RD REPORT, supra note 3, at 48, para. 84; 12TH REPORT, supra note 4, at 43, para. 38. The terms “overcapacity” and “surplus capacity” are sometimes used synonymously with “excess capacity.”

10. 23RD REPORT, supra note 3, at 48, para. 84; 12TH REPORT, supra note 4, at 43, para. 38.


12. See 23RD REPORT, supra note 3, at 47, para. 82; 12TH REPORT, supra note 4, at 43, para. 39.
rates of capacity utilization, a drop in output accompanied by
substantial operating losses and where the information avail-
able does not indicate that any lasting improvement can be
expected in this situation in the medium-term.13

Unfortunately, the Commission has not specified the minimum
amount of time excess capacity must exist in order to be con-
sidered as structural. In the context of one crisis cartel permit-
ted by the Commission, the excess capacity which justified the
crisis cartel had plagued the industry for over ten years.14 In
a more recent case, however, the excess capacity existed only
for about a year prior to the time the Commission’s exemption
came into force.15

III. CAUSES OF EXCESS CAPACITY

A. Business Cycles

Since the existence of excess capacity is the justification
for crisis cartels, it is important to identify its various causes.
Excess capacity has been explained by reference to business
cycles.16 Demand in many industries—particularly commodity
industries—is cyclical.17 Since supply does not immediately
follow oscillations of demand, an unexpected fall in demand for
a particular product will, at least in the short-term, create a
situation where the capacity of the industry to supply a partic-
ular product exceeds the actual demand for that product.

An actual fall in demand is, however, not necessary to
create excess capacity. Excess capacity may also be created in
an industry which is susceptible to business cycles because of
an incorrect estimation of the development of demand. A
manager’s decision to expand capacity is determined by her
assessment of the future development of demand for a particu-

13. 12TH REPORT, supra note 4, at 43, para. 38. See also Community Guidelines on State Aid for Rescuing and Restructuring Firms in Difficulty, 1994 O.J. (C 368) 12, 16.
lar product. The challenge facing the manager tends to be greater in those industries in which fixed costs are high and the creation of additional capacity time-consuming. In the semiconductor industry, for example, a new chip factory requires a capital investment of approximately $2 billion and two years' time. There is an incentive to create excess capacity because a firm which correctly anticipates a significant increase in demand for a particular product or service will generally realize greater profit than a firm which waits until demand increases until it decides to expand its capacity. Conversely, an incorrect anticipation of the direction of demand can result in excess capacity.

The incentive to expand capacity without waiting for an increase in demand is accentuated by the uncertainty and implications of losing market share. In industries characterized by high fixed costs and relatively low product differentiation, managers generally tend to favor expanding or at least maintaining capacity even if it results in excess capacity. In such industries, managers fear reducing capacity because it would hinder their ability to respond promptly to an ensuing rise in demand.

B. Strategic Behavior of Incumbent Firms

Excess capacity may also be the result of strategic behavior of incumbent firms to deter potential market entrants. A potential entrant's decision to enter a particular market is primarily influenced by the perceived profit to be made from that entry relative to the costs of entry. One important factor in determining whether sufficient profit could be achieved

18. See MICHAEL PORTER, COMPETITIVE STRATEGY TECHNIQUES FOR ANALYZING INDUSTRIES AND COMPETITORS 325-28 (1980) (identifying the factors which managers should use to determine whether to expand capacity).

19. Certain industries are characterized by high fixed costs. When the demand for the goods produced by these industries drops, firms may be able to relatively quickly reduce their variable costs. However, fixed costs are not only expensive to dismantle, they are expensive to restart once demand returns. Moreover, there is an incentive not to reduce fixed costs since this will increase marginal costs.

20. See Paul Taylor, Brighter Prospects In View, FIN. TIMES, IT Supplement, Mar. 3, 1999, at IV.

21. See id. ("Overcapacity in the semiconductor market is made worse by companies' fear of losing market share. This encourages chipmakers to delay closing the surplus plant."); Timothy Aeppel, Why Too Much Stuff Means Little Now, WALL ST. J., Dec. 4, 1997, at A2.
upon entry is the level of excess capacity existing in the particular industry. The likelihood of market entry in a particular industry operating at 90% capacity is much greater than market entry into an industry operating at 60% capacity. Thus, strategic increases in capacity by the incumbent firms may serve to deter market entry. Assuming that demand does not correspondingly increase, this strategic behavior will result in excess capacity. Increases in capacity may also be the result of strategic efforts of the incumbent firms to force an existing market participant from the market. This is possible—particularly in commodity industries—because an increase in capacity unrelated to a corresponding increase in demand will generally have the effect of lowering the price for a particular product in a given market. If the competitors force the price below a level at which other firms in the market cannot maintain a sufficient profit to at least cover their costs, these other firms will be forced from the market. This is generally true for smaller competitors or competitors not belonging to corporate groups which are able to cross-subsidize their loss-making activities until the price for the particular good or service increases. An example of strategic behavior resulting in the creation of excess capacity can be found in the European airline industry. Most if not all of the Member States are dominated by one major airline which is able to absorb losses due to sustained periods of excess capacity. One way in which they have protected their position when faced with competition from a smaller rival has been to drive prices below a sufficiently profitable level by maintaining or increasing excess capacity.

22. See PORTER, supra note 18, at 325-28.
23. The theory of ex ante increases in capacity as a strategy of entry deterrence was first formalized by A. Michael Spence, Entry, Investment and Oligopolistic Pricing, 8 BELL J. ECON. 534 (1977), and subsequently expanded upon by a number of authors, most notably B. Curtis Eaton & Richard G. Lipsey, The Theory of Market Pre-emption: The Persistence of Excess Capacity and Monopoly in Growing Spatial Markets, 46 ECONOMICA 149 (1979), and Avinash Dixit, The Role of Investment in Entry Deterrence, 90 ECON. J. 95 (1980).
26. See id. The same situation existed recently in the steel industry. See
C. Irrational Behavior

Traditional economic models assume that entrepreneurs are rational actors. Based on this assumption, one would expect that capacity would fluctuate relative to demand. However, there are several psychological factors which may be used to explain how excess capacity is created. First, isomorphic behavior may contribute to excess capacity. Because the development of demand can never be predicted with complete accuracy, there is uncertainty associated with the decision to expand capacity. The longer it takes to build new capacity, the greater the uncertainty. Managers and entrepreneurs, as well as humans in general, when faced with uncertainty tend to adopt the behavior of other individuals similarly situated. When faced with the necessity to adopt a particular strategy or policy, a business manager will tend to give special credence to similar strategies adopted by other companies. This “herd behavior” has the potential of creating excess capacity.

In addition, overly optimistic forecasting may result in excess capacity. Empirical studies have shown that entrepreneurs tend to be overconfident about their abilities and overly optimistic about the future. Entrepreneurs may enter a new market or expand production based on unrealistic expectations of their future rather than realistic expectations of the development of demand. This has the potential of increasing capacity in a particular industry in excess of demand.


28. See Aeppel, supra note 21, at A2 (explaining the “psychology of overcapacity”).


D. State Intervention

Excess capacity may also exist because of exogenous market distortions. The state may create excess capacity when it interferes with market forces, for example, through subsidies to inefficient firms. When a firm receives a subsidy, it is protected to a certain degree from the market mechanism which would otherwise force it to reduce its capacity to a level where it could achieve a profit. For example, one of the main causes of excess capacity in the Community's synthetic fibers industry in the late 1970's which eventually led to the creation of a crisis cartel was the fact that several of the major producers were state-owned companies receiving substantial subsidies. This same scenario is evident in the European air travel sector and the automobile industry. The protection accorded by state subsidies frustrates the ability of the market to achieve equilibrium and results in excess capacity.

IV. POLICY OPTIONS

A. Market Forces

Excess capacity depresses prices and generally has a negative impact on the profits of the firms. When faced with declining profits due to prolonged excess capacity, firms tend to put pressure on politicians for a response. Perhaps the most obvious policy option is for the government to allow the market forces to address the problem. By driving prices below total average costs, excess capacity forces the incumbent firms to incur losses. This will persist until demand or efficiency increases or capacity decreases. In the absence of government intervention or private restraints of competition, capacity will

31. See René Jollet, Cartelisation, Dirigism and Crisis in the European Community, 3 WORLD ECON. 403, 412 (1981). The Commission eventually had to step in and request the Member States not to grant assistance to firms in this industry which would contribute to an increase in existing production capacity. COMMISSION OF THE EUROPEAN COMMUNITIES, 8TH REPORT ON COMPETITION POLICY 49, para. 42 (1979) [hereinafter 8TH REPORT].


generally decrease because the less efficient firms, i.e., those with high average cost curves, will be forced from the market or the existing firms will unilaterally reduce their capacity.\textsuperscript{34} The European Commission has itself indicated that in a free-market economy this is the most common way of dealing with excess capacity resulting in substantial losses.\textsuperscript{35}

\textbf{B. State Intervention}

Another possible policy response would be for the state to intervene in the market and induce the firms to eliminate some of the excess capacity. For example, in the event of a situation of excess capacity in the coal or steel industries, Article 58 of the Treaty of Paris allows the Commission to establish a system of production quotas to reduce supply and thereby increase prices to a level at which the incumbent firms can make a profit.\textsuperscript{36} The EC Treaty does not contain a similar provision and, since the Community institutions can only act where they have the express authority to do so, there is some question whether the Community would be in the position to order capacity reductions.

Nonetheless, there are other means available for the state to induce capacity reductions. For example, a state could pay the firms to reduce capacity. Although this is a form of state aid\textsuperscript{37} prohibited by Article 87(1) of the EC Treaty,\textsuperscript{38} the Com-

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\textsuperscript{34} For example, Kimberly-Clark Corp., one of the world's leading tissue producers, unilaterally decided to reduce excess capacity because the excess capacity in the industry was forcing prices below a level at which Kimberly-Clark could realize a sufficient profit. See Robert Langreth, \textit{Kimberly-Clark's Sweeping Cutbacks Should Ease Overcapacity, Analysts Say}, \textsc{Wall St. J.}, Nov. 24, 1997, at A3. See also Paul J. Deveney, \textit{Samsung Joins Effort to End Glut In Chip Market}, \textsc{Wall St. J.}, June 9, 1998, at A12; Dean Takahashi, \textit{Cirrus to Reduce Chip Manufacturing By 70\%, Lay off 400 to 500 Employees}, \textsc{Wall St. J.}, Sept. 25, 1998, at B6; Dean Takahashi & Quentin Hardy, \textit{Motorola to Halt Building Virginia Plant}, \textsc{Wall St. J.}, Sept. 17, 1998, at B8; Haig Simonian, \textit{Ford Warns of Action to Cut Capacity}, \textsc{Fin. Times}, Jan. 8, 1997, at 17.

\textsuperscript{35} See 23RD REPORT, \textit{supra} note 3, at 47, para. 82. See also Stichting Baksteen, \textit{supra} note 15, at 19, para. 20; Synthetic Fibres, \textit{supra} note 14, at 22, para. 30.


\textsuperscript{37} The concept of aid is difficult to define but is commonly understood as an advantage granted or otherwise facilitated by the state. \textit{See Case 61/79,
mission will allow such aid if it is part of a feasible, coherent and far-reaching plan to restore the firms' long-term viability and will lead to an irreversible capacity reduction. Moreover, the rules on state aid contained in the EC Treaty do not apply to the Community institutions. Thus, this policy option is available to the Commission.

Yet a third manner in which the state could intervene in the market to address a situation of excess capacity is to restrict the flow of imports into the relevant geographic market. The demand which was once satisfied by foreign imports will then be shifted to domestic producers thereby increasing their capacity utilization rates. This form of state intervention typically is in the form of the imposition of duties, quotas or even bilateral agreements with foreign countries to restrict the flow of goods. The restriction of imports as a solution to excess capacity is a politically attractive option since it does not require the domestic industry to reduce capacity. Consumers suffer the net welfare loss as a result of such restraints.

C. Cartels

A third possible approach to address a situation of excess capacity would be for the state to allow firms to agree among themselves to reduce capacity. Several firms may agree to acquire another producer and then close that production facility, or the incumbent firms may agree on a mutual reduction


38. Article 87(1) prohibits all forms of aid granted by a Member State or through state resources which distorts or threatens to distort competition and has an effect on trade between Member States. EC TREATY art. 87(1).


41. See, e.g., Steven Berry et al., Voluntary Export Restraints on Automobiles: Evaluating a Trade Policy, 89 AM. ECON. REV. 400 (1999).

42. See WERNER BENISCH, WEGE DES ABBAUS VON BRANCHENÜBERKAPAZITATEN,
in capacity based on a defined quota or formula. In both cases, competition law plays an important role since the agreement would essentially amount to a cartel. Thus, the cartel approach is only a legitimate policy option if such cartels are permissible under the applicable competition laws.

V. COMPETITION LAW APPLIED TO CRISIS CARTELS

A. Infringement of Article 81(1) of the EC Treaty

Crisis cartels could fall under the prohibitions on anti-competitive practices codified in Article 81 and Article 82 of the EC Treaty. According to Article 81(1) of the EC Treaty, “all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market” are prohibited. The application of Article 81(1) depends on three requirements, each of which is fulfilled in the case of crisis cartels. First, there must be an agreement, a decision by associations of undertakings, or concerted practice between undertakings. The concept of “agreement” in the context of Article 81(1) encompasses not only formal contracts but all situations where “the undertakings in question have expressed their joint intention to conduct themselves on the market in a specific way.” Thus, in cases of crisis cartels there is generally no issue whether the first element of an infringement of Article 81(1) is fulfilled. In fact, even those undertakings which were not actually parties to the agreement but “cooperated with it and knowingly associated themselves with its overall objectives” will be considered part of the cartel.


43. EC Treaty arts. 81, 82.
44. Id. art. 81(1).
47. LdPE, supra note 46, at 33, para. 41.
Second, there must be an effect on trade between Member States. Given the broad interpretation of this requirement, crisis cartels will have an effect on trade between Member States because they typically involve the leading firms from within the Member States of the Community. The fact that the parties to the agreement may even be located in one Member State does not indicate the absence of an effect on trade between Member States. Even agreements limited to one Member State can have an effect on trade between Member States. This applies in particular to crisis cartels which generally involve a large portion of the undertakings active in a particular market.

Finally, there must be an appreciable restraint of competition within the European Community. According to the Commission, a restraint of competition occurs if the agreement or concerted practice results in a price level for the product or service which is above the price level which would be determined by conditions of free competition. One type of restraint that is expressly prohibited by Article 81(1) is an agreement between firms to limit or control production. Since crisis cartels not only result in higher prices but also limit production, they are, in the words of the Commission, “usually caught by Article 85.”

48. See EC TREATY art. 81(1)
49. See Vereeniging van Cementhandelaren, 1972 O.J. (L 13) 34 (Cartel which was limited to the Netherlands nonetheless had an effect on trade between Member States).
50. See id. See also Stichting Baksteen, supra note 15, (all members of crisis cartel were in the Netherlands).
51. See Stichting Baksteen, supra note 15, at 19, para. 17; Synthetic Fibres, supra note 14, at 22, para. 27.
53. See Pre-Insulated Pipes Cartel, 1999 O.J. (L 24) 1, at 54, para. 146.
54. EC TREATY art. 81(1)(b).
55. In the amended EC TREATY the language of Article 85 is found in Article 81. 23RD REPORT, supra note 3, at 48, para. 83. See, e.g., Stichting Baksteen, supra note 15, at 18, para. 15; LDPE, supra note 46, at 33, para. 42; Synthetic Fibres, supra note 14, at 22, para. 26; Rolled Zinc Products and Zinc Alloys, 1982 O.J. (L 362) 40, at 48; Italian Cast Glass, supra note 46, at 23. See also Case T-148/89, Tréflunion v. Commission, 1995 E.C.R. II-1063, 1108, para. 109 (Ct. First Instance).
B. Exemption of Crisis Cartels

Since agreements that infringe Article 81(1) are automatically invalid and the participating firms are subject to fines, the question arises whether crisis cartels can be exempted under Article 81(3) of the EC Treaty. This provision allows the Commission to exempt an agreement which infringes Article 81(1) if four conditions are fulfilled: (1) the agreement must "contribute[ ] to improving the production or distribution of goods or to promoting technical or economic progress," (2) consumers must obtain "a fair share of the resulting benefit," (3) the restrictions imposed must be indispensable to the attainment of the beneficial results, and (4) the parties to the agreement must not be afforded "the possibility of eliminating competition in respect of a substantial part of the products in question."

1. Development of Policy

Since crisis cartels clearly infringe Article 81(1) of the EC Treaty, the fundamental policy issue is whether these types of restrictive agreements should be exempted under Article 81(3) of the EC Treaty. Since, as is discussed below, crisis cartels do not technically meet the four requirements of Article 81(3), the Commission's policy decision to permit such arrangements has distorted the legal interpretation of Article 81(3). Like so many other areas in European law, crisis cartels illustrate how the law is shaped to fit the policy.

In the early 1970's, the Commission was first faced with the decision whether to exempt a crisis cartel under Article 81(3). A group of Dutch cement producers had entered into an agreement providing for the allocation of quotas for the Netherlands along with uniform pricing and sales terms. After the Commission objected to the price control arrange-
ments which the cartel had established, the group applied for an exemption. The cement producers argued that the industry was in a crisis situation characterized by excess capacity. The Commission refused to promulgate general rules for exempting crisis cartels but instead stated that it would take a case-by-case analysis:

At the competition policy level it is necessary to know under what conditions these difficulties can be resolved by an agreement between undertakings in a manner compatible with the Treaty's competition rules. This problem is too delicate to afford grounds for hoping that it can be solved by a general approach. The method of case-by-case examination is unavoidable.

The Commission's review in that case revealed that the measures adopted by the cartel participants were not necessary to address the problem. In 1978, however, the Commission actually took an active role in promoting a crisis cartel in the synthetic fibers industry. Faced with prolonged excess capacity in that industry, Viscount Etienne Davignon, who was the Commissioner for Industrial Policy at the time, encouraged the synthetic fibers producers in the Community to cooperate to reduce capacity. This industrial policy decision did not sit well with those within the Commission charged with protecting competition. The Commission was faced with the fundamental question of whether a crisis cartel could be exempted under Article 81(3) of the EC Treaty. The basic problem would be to reconcile the industrial policy with the application of the competition laws. The Commission's Directorate General for Competition initially took the position that the agreement could not be exempted because all of the major European producers were

64. See Vereeniging van Cementhandelaren, supra note 49.
66. See 2ND REPORT, supra note 62, at 37, para. 29.
67. Id. at 26, para. 18.
68. See Commission Decision 72/468, supra note 65, at 7; 2ND REPORT, supra note 62, at 41, para. 31.
70. See Joliet, supra note 31, at 413.
involved. As indicated above, in order to qualify for an exemption, the agreement cannot afford the possibility of eliminating competition in respect of a substantial part of the products in question.

Since the Commission does not have the authority to authorize practices that are contrary to the EC Treaty, the permissibility of crisis cartels requires special legislation. In July 1978, Viscount Davignon met with Raymond Vouel who was then serving as Commissioner for Competition Policy. They agreed to introduce a proposal for drafting a regulation based on Article 83 of the EC Treaty to be submitted to the Council by the Commission which would exempt the crisis cartel. However, these two Commissioners were unable to garner sufficient support from their colleagues within the Commission, and the proposal was abandoned in July of that year. The strict application of the competition laws still held sway over industrial policy. According to the Commission, its policy "regularly confirmed by the Court of Justice, is that it is not permissible for undertakings to use restrictive agreements or concerted practices to determine the way in which their output or their sales will progress."

One year later, the Commission took the same strict approach in response to a cartel of cast glass producers. The firms, representing approximately 75% of the Italian cast glass market, had entered into an agreement involving production quotas. They argued that the cartel was entered into in re-

71. See id.
73. See id. at 413, 439 n.58.
74. According to Article 83, the Council is authorized to adopt regulations or directives to give effect to Article 81 and 82 of the EC Treaty. The general consensus is that it is unlikely that, if challenged, this provision would have allowed the Council to preempt the application of the competition laws to crisis cartels. See Joliet, supra note 31, at 420; Ulrich Immenga, Internationale Selbstbeschränkungsabkommen zwischen staatlicher Handelspolitik und privater Wettbewerbsbeschränkung, 49 RABELS ZEITSCHRIFT FÜR AUSLÄNDISCHES UND INTERNATIONALES PRIVATRECHT 303, 323 (1985); Gabriela Wallenberg, Das Krisenkartell europäischer Chemiefaserhersteller, 1986 RECHT DER INTERNATIONALEN WIRTSCHAFT 755; Sharpe, supra note 69, at 80.
75. See Joliet, supra note 31, at 414.
76. 8TH REPORT, supra note 31, at 50, para. 42.
77. See Italian Cast Glass, supra note 46.
78. See id.
sponse to a structural crisis and therefore should have been exempted under Article 81(3) as a permissible crisis cartel. Since the cartel was not notified to the Commission, the issuance of an exemption under Article 81(3) was precluded. However, the Commission stated that even if the crisis cartel would have been notified, no exemption would have been granted: “At all events, at least one of the requirements under Article 85(3) has not been met, since, through the agreements which are the subject of this decisions, more than half of Italian production of cast glass was shielded from competition, thus eliminating competition in respect of a substantial part.”

In response to the arguments that the crisis situation justified the creation of the cartel, the Commission stated quite directly that Article 81(3) of the EC Treaty “makes no reference to such a situation.” The position held by the Commission up to the beginning of the 1980’s was therefore consistent with the opinion of the competition law scholars.

Within two years, however, economic developments caused the Commission to change its position dramatically. The first formal indication that the Commission was ready to exempt a crisis cartel appeared in its Twelfth Report on Competition Policy:

As the economic recession persists, problems of overcapacity are appearing in increasingly acute form in individual firms and entire industries. The associated employment problems are particularly worrying at a time of high unemployment in all the Member States. In such circumstances, the Commission must offer guidance as to how far it considers the solutions sought by firms as compatible with Article 85 of the EEC Treaty.

Although the Commission had earlier suggested that a crisis cartel may be exempted under Article 81(3), the situation was now ripe for relying on this option. In 1984, the Commis-

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80. Italian Cast Glass, supra note 46, at 24. In the amended EC TREATY the language of Article 85(3) is found in Article 81(3).
81. Id.
82. See Joliet, supra note 31, at 420-21; Immenga, supra note 74, at 323.
83. 12TH REPORT, supra note 4, at 43, para. 38. In the amended EC TREATY, the language of Article 85 is found in Article 81.
sion exempted a crisis cartel for the first time. The agreement was between ten of the largest European synthetic fiber producers to close 18% of their production capacity. As part of its approval, the Commission required the participants to take the following steps: (1) to supply to a trustee all relevant information concerning the capacity to be dismantled and to permit the inspection of their plants by independent experts, (2) to consult each other in the event of important changes on the market, and (3) not to sell the dismantled plants.

Since 1984, the Commission has exempted only one other crisis cartel. Because of the informal procedure which occurs, it is difficult to determine how many proposed crisis cartels the Commission has refused to exempt. Once firms involved in or contemplating a crisis cartel decide to approach the Commission to receive clearance, the contact is made at an informal level. In some cases, it is made via the Commissioner responsible for industrial policy since he or she tends to be more receptive than his or her colleagues to the argument that the other means of addressing excess capacity are inappropriate. Once the blessing of that Commissioner is received, the firms (or even that Commissioner) approaches the Directorate General for Competition (DGIV) informally prior to any formal notification being submitted. If the DGIV responds negatively, the plan is often dropped without ever filing a formal notification. In other words, there is little in the way of public records identifying the attempts to establish a crisis cartel. A formal decision by the Commission is only rendered when it has been determined in advance that the crisis cartel should be approved. Conversely, a formal decision may be reached where the Commission discovers a purported crisis cartel which was never notified to the Commission.

84. See Synthetic Fibres, supra note 14.
85. See 13TH REPORT, supra note 5, at 54, para. 59.
86. See Synthetic Fibres, supra note 14, at 20, art. 18(a)(f).
87. See id. at 20, art. 18(g).
88. See id. at 20, art. 18(a).
89. See Stichting Baksteen, supra note 15.
90. In one case, it prohibited a purported crisis cartel which had been approved under German competition law. See Case C-185/95, Baustahlgewebe GmbH v. Commission, (E.C.J. Dec. 17, 1998) (not yet reported).
2. Requirements for an Exemption

Agreements which infringe Article 81(1) of the EC Treaty are automatically invalid unless they qualify for an exemption under Article 81(3).\textsuperscript{91} Once the Commission made the policy decision in 1984 to exempt a crisis cartel, it was faced with the legal problem of explaining how the cartel met the requirements of an exemption under Article 81(3). There are two legal constraints which make the Commission's task difficult. First, the Commission is obligated by Community law to state the reasons for its decisions. Failure to give a well-reasoned opinion based on sound economic reasoning can lead to the nullity of the decision.\textsuperscript{92} Second, the Court has stated that the Commission must refuse to grant an exemption under Article 81(3) unless all of the requirements are met.\textsuperscript{93} Thus, the Commission is faced with the difficult task of explaining how crisis cartels fulfill each of the requirements of an exemption under Article 81(3). Its reasoning has been less than convincing.

\textbf{a. Improvement in Production, Distribution, Technology or Economic Progress}

The first requirement under Article 81(3) is that the agreement must contribute to improving the production or distribution of goods or promoting technical or economic progress.\textsuperscript{94} The standard which the Commission itself has set forth is that the improvement must entail objective and appreciable advantages such as to compensate for any disadvantages caused by the restraint.\textsuperscript{95} In the context of crisis cartels, the basic bene-

\begin{footnotesize}
\textsuperscript{91} EC TREATY art. 81(1)(3).
\textsuperscript{94} EC TREATY art. 81(3).
\textsuperscript{95} See Stichting Certificatie Kranverhuurbedrijf/Federatie van Nederlandse Kranverhuur, 1994 O.J. (L 117) 30, at 35, para. 29.
\end{footnotesize}
fit identified by the Commission is the restoration of an "econo-
mically healthy structure of supply in the Community" in
that particular industry. The assumption is that the crisis
cartel will allow the industry to close its less efficient plants:

As the capacity closures concern production units that are the
least suitable and least efficient because of obsolescence,
limited size or outdated technology, production will in the
future be concentrated in the more modern plants which will
then be able to operate at higher capacity and productivity
levels; this will lead to a corresponding reduction in the inci-
dence of fixed costs, which form a large proportion of net
costs.

The Commission is well aware of the fact that a cartel
protects its members from market forces which would other-
wise eventually force them to reduce capacity. As a surrogate,
the Commission replaces the market mechanism with the
requirement of a plan to reduce capacity. This plan must
ensure that overcapacity is irreversibly dismantled and no new
capacity is created for the duration of the cartel.

b. Benefits to Consumer

Article 81(3) of the EC Treaty also requires the Commis-
sion to explain how the crisis cartel allows "consumers a fair
share of the resulting benefit." Explaining how this re-
quirement is fulfilled in the context of crisis cartels presents a
significant hurdle for the Commission since crisis cartels are
aimed at increasing the profitability of the incumbent firms
and, as the Commission recognizes, result in increased pric-
es. Moreover, in other cases the Commission has indicated
that a cartel agreement which keeps inefficient firms afloat
does so to the detriment of the public interest.

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96. 23RD REPORT, supra note 3, at 49, para. 85.
98. See id. at 20, para. 33; 23RD REPORT, supra note 3, at 48, para. 84.
99. See 12TH REPORT, supra note 4, at 43, para. 39; 23RD REPORT, supra note
   3, at 49, para. 85.
100. EC TREATY art. 81(3).
101. See Stichting Baksteen, supra note 15, at 20, para. 31; Synthetic Fibres,
   supra note 14, at 23, para. 41.
102. See Fire Insurance, 1985 O.J. (L 35) 20, at 28, para. 44.
The Commission’s basic position in the context of applying this requirement to crisis cartels is that a “healthy” European industry is good for consumers. The Commission overlooks or even rejects the notion that the crisis cartel will lead to higher prices for consumers. The policy reasoning behind the exemption for crisis cartels is that the reduction in capacity will lower the fixed costs for the incumbent firms and, assuming prices remain stable, will generate profits for them. The problem is, however, that the increased profits are economic rent which is paid for by the consumers without any redeeming welfare benefits. In a competitive industry the benefits accruing from a lowering of fixed costs are typically passed on to the consumer in the form of lower prices. Increased profits for the producers resulting from the crisis cartel means that the prices for consumers are higher than they would be in the absence of the cartel.

Assuming, however, that a profitable European industry is indeed a benefit to consumers, there is no guarantee that the ensuing benefits will incur to the benefit of the consumer which is required by Article 81(3). In exemption decisions, the Commission, after identifying a certain benefit, typically relies on the fact that existing competition within the industry in which the agreement takes place will force the parties to the agreement to pass on the benefits to the consumers. In the case of crisis cartels, however, most if not all of the industry needs to be part of the cartel in order for it to have any chance of success. Otherwise, those firms not involved in the cartel would be able to increase their capacity utilization rates, lower their marginal costs and place the cartel members at a severe competitive disadvantage. In fact, since the crisis cartel results in inflated prices, there is an incentive to increase capacity. This is why the Commission requires that the cartel include those firms representing all or a significant percentage of capacity in the relevant sector. However, if a majority of the

105. See Synthetic Fibres, supra note 14, at 22, para. 34.
108. See 13TH REPORT, supra note 5, at 53, para. 56; 23RD REPORT, supra note
competitors are involved in a cartel, it is questionable whether there will be sufficient competition to force the cartel members to pass on the benefits. The protection from competitive forces which is required for the success of the cartel suggests that the cartel members would not be forced to pass on any benefits to the consumers.

c. Indispensability of Restrictions

The third requirement which must be fulfilled before the Commission grants an exemption is that the restrictions imposed by the agreement must be indispensable to attaining the redeeming consumer benefits. The first issue in applying this indispensability test is whether there are other less restrictive means to obtain the identified benefit. If other means of obtaining the objective exist which are less restrictive of competition, an exemption cannot be granted. In the context of crisis cartels this standard poses a significant hurdle for the Commission because the Commission must state why there are no other means of reducing capacity which are less restrictive of competition. As discussed above, cartels are only one method of addressing the problem of structural excess capacity.

Two alternative methods which might be less restrictive of competition are market forces and state intervention. In most instances, market forces are a much more appropriate response (at least from the perspective of consumer welfare) to the economic situation which crisis cartels are ostensibly designed to address. The justification for crisis cartels is the elimination of excess capacity. Generally, excess capacity can only exist in a competitive market for a short period of time. If costs associated with excess capacity are causing the production of the particular product to be unprofitable, the industry will generally

3, at 49, para. 84.

109. See EC TREATY art. 81(3)(a).


reduce excess capacity on its own.112 Although the Commission recognizes this attribute of a market economy,113 it rejects the assumption that the market is an equally efficient means of obtaining the same results as a crisis cartel.114 In its Stichting Baksteen decision, for example, the Commission stated that in the absence of the crisis cartel, "[t]he other parties, as leading manufacturers, would not have decided individually and independently to reduce capacity had they not been certain that competitors would follow their example."115

The Commission has identified two types of subsidies which suggest that the market may not be as efficient as a crisis cartel at restoring market equilibrium. First, cross-subsidization may allow less efficient firms to remain in the market rather than being forced out by their more efficient competitors.116 The Commission has identified two sources of cross-subsidies which could produce this effect.117 According to the Commission, "[u]ndertakings which have failed to make the necessary adjustments may have their losses offset within their groups, to the detriment of healthy undertakings."118 This reasoning rests on the assumption that the profit to be made in the long term exceeds the losses which the group will be forced to absorb in the short term. No reasonable entrepreneur would cross-subsidize a losing affiliate unless there was profit to eventually be made. The assumption upon which the Commission's policy is based, i.e. that there are profits to be made in the particular industry in the long term, exposes the contradiction in the Commission's reasoning. In such an indu-

112. The recent experience of the semiconductor industry provides a prominent example of how market forces operate to achieve equilibrium when faced with excess capacity. See Michiyo Nakamoto, Hitachi Closes Chip Factory, FIN. TIMES, Apr. 19, 1997, at 23; Takahashi & Hardy, supra note 34, at B8; Takahashi, supra note 34, at B7; Deveney, supra note 34, at A12.
113. In its 12th Report, the Commission recognized that "[i]n a predominantly free market economy such as the Community's, it is up to each undertaking to assess for itself whether and at which point such overcapacity becomes economically unsustainable and to take the necessary measures to reduce it." 12TH REPORT, supra note 4, at 43, para. 38.
116. See id. at 19, para. 26.
117. See id.
118. 12TH REPORT, supra note 4, at 21, para. 38.
try, the incumbent firms which do not belong to a larger group willing to subsidize it until profits can be made still have access to the capital markets. If indeed profit is to be had, as the Commission assumes, these independent firms should be able to get access to the requisite capital. However, even if one assumes that there are imperfections in the capital markets, the Commission's reasoning ignores the fact that other firms or groups with significant financial resources could purchase the efficient plants once the independent firm was forced out of the market. These other firms would be attracted by the same long term returns which motivated the cross-subsidization.\footnote{See F.M. Scherer, \textit{Industrial Market Structure and Economic Performance} 214 (2d ed. 1980). This scenario was played out recently in the steel industry. \textit{See Larry Holyoke, et al., \textit{Psst! Wanna Buy a Used Steel Plant?}, BUS. WK., Aug. 22, 1994, at 48; Stephen Baker & Keith L. Alexander, \textit{Niche Work—If You Can Get It}, BUS. WK., Aug. 29, 1994, at 31.}

The other type of subsidy which has been identified by the Commission as the reason why market forces are less efficient than a crisis cartel at reducing excess capacity is state subsidies. According to the Commission, in certain industries, competition often has been "distorted by state aid aimed at creating capacity."\footnote{23RD REPORT, supra note 3, at 47, para. 82.} Inefficient undertakings have been able to remain in the market because Member States have extended them aid. This prevents or at least delays the restoration of a market equilibrium.

While this may be an accurate assessment of the situation in many Member States, it does not explain why the formation of a crisis cartel is indispensable to reducing capacity as required by Article 81(3). In fact, the more appropriate method of addressing industries plagued by excess capacity caused by state aid is to increase enforcement of Article 87 and Article 88 of the EC Treaty. These provisions provide that any aid granted to a Member State in any form which distorts or threatens to distort competition by favoring certain industries or the production of certain goods shall be incompatible with the Common Market.\footnote{EC TREATY arts. 87, 88.} Member States are required to seek the Commission's approval for new aid granted and the Commission has the authority to recover any aid granted illegally.\footnote{See generally Hans-Jochim Priess, \textit{Recovery of Illegal State Aid: An Overview of Recent Developments in the Case Law}, 33 COMMON Mkt. L. REV. 69.}
Stricter enforcement of the rules on state aid is less restrictive of competition than crisis cartels.

C. Absence of Possibility of Foreclosure

The fourth requirement for an exemption under Article 81(3) is that the agreement must not “afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.” This requirement presents a problem for the Commission because on the one hand the Commission, in applying this requirement, generally relies on the collective market position of the parties to the agreement to determine whether substantial competition will be foreclosed. On the other hand, in the context of crisis cartels, the requirement under Article 81(3) that the benefits be passed on to the consumers means that, according to the Commission’s policy, at least a majority of members of the industry participate in the cartel. From a practical perspective, in fact, this is generally the only way the cartel can achieve its objective of capacity reduction. This places the Commission in a difficult position in applying Article 81(3) since it must explain why the cartel does not preclude substantial competition. In the Stichting Baksteen case, 16 of the 25 Dutch firms on the Dutch brick market participated in the cartel. These participants represented 90% of installed capacity in the Netherlands accounting for 85% of total brick sales. In the Synthetic Fibres case, the members of the crisis cartel held about 70% of total synthetic fiber capacity and about 85% of installed capacity in the Community.

The Commission is aware of this inconsistency but argues that since the reduction of capacity is only one element of the competitive strategy of the firms, they will not have surrendered all the freedom of action in the marketplace with the

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123. EC TREATY art. 81(3)(b).
125. See supra notes 101-08 and accompanying text.
126. See 13TH REPORT, supra note 5, at 53, para. 56; 23RD REPORT, supra note 3, at 48, para. 84.
128. Synthetic Fibres, supra note 14, at 18, para. 7.
result that a degree of "internal" competition will be maintained. The Commission also points out that the presence of other firms in the market which are not parties to the cartel, as well as imports from third countries, will usually provide a source of external competition. It is difficult to conjecture where the Commission is going with this line of reasoning. If there is sufficient competition remaining in the industry, the success of the crisis cartel at reducing capacity will be jeopardized. It makes no difference whether this competition is "internal" or "external." In addition, the fact that the firms continue to be competitors does not mitigate the negative impact that the cartel will have on competition and consumer welfare. Needless to say, the Commission's line of reasoning in this context has never been scrutinized by the European Courts.

D. Crisis Cartels and the Application of Article 82

Up to this point, the focus of this article has been on the compatibility of crisis cartels with Article 81 of the EC Treaty and, in particular, the requirements for an exemption under Article 81(3). However, Article 81 constitutes only one part of the European competition law regime. Another important provision is Article 82 of the EC Treaty which prohibits the abuse of a dominant position. In contrast to Article 81, however, Article 82 does not provide for the possibility of an exemption. Thus, the Commission is required to prohibit all abuses of a market dominating position which have an effect on trade within the European Community.

This raises several issues in the context of crisis cartels. The first issue is whether the application of Article 82 to crisis cartels is precluded where the Commission has granted an exemption under Article 81(3). Both the Commission and the European Courts have repeatedly stated that Article 81 and

129. See 12TH REPORT, supra note 4, at 44, para. 39.
130. See Synthetic Fibres, supra note 14, at 24, para. 50; 12TH REPORT, supra note 4, at 44, para. 39.
Article 82 apply to two different types of restraints of competition. Thus, the fact that a particular practice fulfills the requirements of an exemption under Article 81(3) does not preclude the application of Article 86 to that same practice if all the elements of an infringement of Article 82 are fulfilled.

The second issue therefore is whether crisis cartels infringe Article 82 of the EC Treaty. There are essentially three elements to an infringement of Article 82: (1) market dominance, (2) abuse of that dominance, and (3) effect on trade between Member States. Since crisis cartels generally involve undertakings from several Member States, the third element would not be an issue. In European competition law, a dominant position is generally understood as "the ability to act to an appreciable extent independently of competitors, customers and ultimately of the consumers." A market share of at least 50% will generally be indicative of dominance. A market share below 10% usually is sufficient to illustrate that the undertaking is not in a dominant position.

There is nothing inherent about crisis cartels which would suggest that any of the firms involved has a dominant position. To the contrary, the fact that the firms agreed to form a crisis cartel suggests that none of them has a dominant position. However, Article 82 also applies to situations where two or more firms hold a position of collective dominance. The existence of "economic links" between the firms is sufficient for their individual market positions to be considered together.

134. The requirement that there is an effect on trade between Member States is the same as under Article 85 of the EC Treaty. See Joined cases 6 & 7/73, Commercial Solvents v. Commission, 1974 E.C.R. 223, 252, para. 30.
138. Trans-Atlantic Conference Agreement, supra note 133, at 90, para. 521.
139. See Joined cases T-68/89, 77/89 & 78/89, SIV v. Comm'n, 1992 E.C.R. II-1403, 1548, para. 358 (Ct. First Instance); Trans-Atlantic Conference Agreement,
This requirement is fulfilled, for example, where the firms have entered into an agreement or engaged in concerted practices in the sense of Article 81. Thus, a crisis cartel would fulfill the first requirement of Article 82 of the EC Treaty. As discussed above, one of the basic requirements established by the Commission is that the crisis cartel include most, if not all, competitors in a particular market. Since a crisis cartel must be based on an agreement, the members would together occupy a position of collective dominance.

The mere existence of market dominance, however, is not sufficient to establish an infringement of Article 82. There must also be abuse of that dominance. A dominant firm abuses its position when it engages in conduct that would not be possible in a competitive market. The mere fact that crisis cartels infringe Article 81(1) of the EC Treaty is not evidence per se that the conduct infringes Article 82. The abuse of the collective dominant position within the context of a crisis cartel exists when the members agree to limit production, thereby reducing supply and increasing the price the consumer has to pay for the product. Article 82(b) of the EC Treaty expressly identifies, as an example of abuse, the limitation of production to the detriment of customers. When firms in a position of collective dominance use their position to restrict output, there is an infringement of Article 82 of the EC Treaty. In most instances, therefore, a crisis cartel would amount to an infringement of Article 82 even if it has been exempted under Article 81(3).


142. EC TREATY art. 82(b).
This contradictory result of the parallel application of Article 81 and Article 82 to crisis cartels is explained by the fact that the Commission does not apply the elements of Article 81(3) consistently to crisis cartels as to other forms of restrictive practices. Agreements between competitors representing a major portion of the market designed to restrict output and raise prices do not technically fulfill the requirements of Article 81(3). Thus, if the law were applied correctly, there would be no conflict between the application of Article 81 and 82. The crisis cartel would be prohibited by both provisions. For policy reasons, however, the Commission pragmatically applies the rules to crisis cartels. This stretching of the exemption possibility under Article 81(3) to crisis cartels is the source of the conflict with Article 82 of the EC Treaty.

VI. CRISIS CARTELS AND THE TRIUMPH OF INDUSTRIAL POLICY

The authorization of crisis cartels under the European competition laws represents another triumph of industrial policy over competition law in Europe. This has negative consequences for the European legal system and European consumers. From a purely legal perspective, the creative application of the competition rules to crisis cartels undermines the legitimacy of European competition law. Based on the Commission’s decisions in prior cases, it is difficult to argue that the formation of a cartel between most if not all the competitors in a particular industry designed to reduce capacity would fulfill the requirements set forth in Article 81(3) of the EC Treaty. In any event, it would probably be caught by the prohibition of Article 82 which does not allow for an exemption. The Commission gets around this by simply not applying Article 82 to crisis cartels. The fundamental issue whether crisis cartels can be exempted under Article 81(3) of the EC Treaty or whether they infringe Article 82 of the EC Treaty has not been addressed by the European courts. Therefore, the reasoning the Commission uses to exempt such cartels has never been subject to judicial scrutiny. This is largely because those who suffer the injury from crisis cartels, the consumers, do not have standing to contest the decisions.143 The injury to the individual consum-

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143. In order for a natural or legal person to contest a decision of the Commission, the decision must be addressed to him or of direct and individual concern to
er is indirect and outweighed by the costs of contesting the decision. Although the competitors who are not involved in the crisis cartel would arguably be able to contest the decision, they would have no interest in doing so since the cartel results in higher prices from which they can benefit.

Crisis cartels are permitted by the competition rules not because they comport with the competition provisions of the EC Treaty, but rather as a matter of industrial policy. The triumph of industrial policy over competition law is an illegitimate exercise of the Commission’s authority. The European Court of Justice has specifically stated: “In no circumstances does it [the Commission] have the authority to authorize practices which are contrary to the Treaty.” Moreover, the triumph of industrial policy over competition law creates inconsistencies in the application of European competition law. As discussed above, since the Commission is required to issue a formal decision exempting a crisis cartel under Article 81(3) of the EC Treaty, it is forced to adopt reasoning which is questionable and sometimes contradictory. One way to avoid the distortion would be to recognize that the authorization of crisis cartels is a policy decision rather than a result of the objective application of European competition law. In the United States, for example, crisis cartels, when promoted by the state as a matter of industrial policy, are permitted by application of the state action doctrine rather than by creatively applying the antitrust laws.

144. In the most recent crisis cartel case, no one even bothered to respond to the Commission’s invitation for comments. See Stichting Baksteen, 1993 O.J. (C 34) 11.
More important than the legal distortions which the European Commission’s approach to crisis cartels creates is the social costs which the triumph of industrial policy imposes on Europeans. The most direct social cost imposed by crisis cartels is in the form of monopoly prices. The existence of the cartel means that the prices for the products involved in the cartel are higher than they would have been if the cartel did not exist. This economic rent is collected by the incumbent firms which may or may not use the rent to enhance efficiency.

In addition, there is an indirect social cost resulting from the impact which crisis cartels have on the competitiveness of the industry involved in the cartel. As the Commission has expressly recognized, “the competitiveness of European industry as a whole [is promoted] by strict enforcement of the competition rules.” As Schumpeter recognized, the defining characteristic of competition is its ability to force firms to increase efficiency or be forced from the market. By protecting firms from these forces, the authorization of crisis cartels diminishes the incentives of firms to increase their efficiency. If European industry were not exposed to global competition, the impact of this protection would not be extreme. However, since European firms are forced to compete on the global stage, the permissive policy towards crisis cartels places European industry at a distinct competitive disadvantage.

Although the European Commission cites the positive effect on employment as one of the redeeming characteristics of crisis cartels, the harm to the competitiveness of European industry may actually have a negative effect on employment. In the short term, crisis cartels may artificially increase employment by delaying the exit of the inefficient firms. In the long term, however, crisis cartels may have another negative effect on employment. By shielding these firms from the competitive forces that would otherwise require them to enhance their efficiency, the Commission is simply postponing the inevitable. These firms, once exposed to global competition, will be

149. JOSEPH A. SCHUMPETER, CAPITALISM, SOCIALISM AND DEMOCRACY 84 (7th ed. 1994).
150. See 23RD REPORT, supra note 3, at 48, para. 85. Although the Commission has also identified the “impact on employment” as a benefit of such agreements, this benefit is only incidental since it is not identified in Article 81(3).
at a distinct disadvantage. The absence of a competitive advantage in a global industry could result in the long-term in higher unemployment. Take, for example, the case where the excess capacity of a firm is due to the fact that another competitor has introduced a more efficient production technique or a better product which it is able to offer at a lower price. In most cases, this is the result of significant investment and hence risk. Often, this development will force the "obsolete" product or firm from the market and the increased demand for the product of the more efficient firm will increase thereby necessitating an increase in employment.

Finally, there is an element of unfairness in the Commission's policy. For one, the departure from the strict enforcement of competition law in the context of crisis cartels has the effect of penalizing the firms which increase their efficiency as a response to excess capacity. In addition, the policy effectively penalizes those firms which correctly anticipated the development of demand and creates an incentive to expand capacity. As discussed above, the time associated with the expansion of capacity means that capacity is increased in anticipation of demand. This is a risk because an inaccurate assessment of future demand growth can create costly capacity. In a market economy, the market would punish the incorrect firms and reward the correct ones. If the market mechanism is distorted by cartel agreements, the efficiencies of the market are lost.

VII. CONCLUSION

The authorization of crisis cartels under European competition law is a policy decision rather than the result of the objective application of the law. In fact, an objective application of the law based on the Commission's position in other cases would lead to the prohibition of crisis cartels. The same conditions which require the success of the cartel in reducing excess capacity indicate that crisis cartels do not fulfill the requirements of an exemption under Article 81(3) of the EC Treaty. However, the triumph of policy over law requires the creative application of European competition law. Moreover, the basis of the policy are flawed. The creation of crisis cartels imposes significant social costs on European society. The only actors who benefit from the policy are the firms who collect the
rent facilitated by the cartel. This suggests that the triumph of industrial policy over competition law in the context of crisis cartels is a manifestation of the success of private interests to the detriment of the long-term competitiveness of European industry and the European public.