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On Government, Governance and Judicial Review: The Case of European Competition Policy

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ABSTRACT

From a traditional rationalist principal-agent framework, the development of the European Community's competition policy could appear as a straightforward story of agency loss. However, the recent overhaul of competition policy, which the Community presented in terms of decentralisation, appears to have changed the story. We are confronted with the uncommon event of an agent (the European Commission) returning some of its powers to the principals (the member states). This paper resolves the puzzle by highlighting the role of the Commission and of European courts. It has become part of the Commission's strategy to pursue its objectives through legally non-binding instruments such as notices or guidelines or co-operation in networks. These instruments do not need the approval of the Council of Ministers or the European Parliament. With the Commission's promotion of new modes of governance, the link between sectoral governance (in terms of regulation specific to competition policy) and the governmental shadow of hierarchy shifted to an increasing extent to judicial review by European courts. Alongside this shift, the character of judicial review has changed in the direction of judicial control, as European courts no longer restrict themselves to review of the legality of Commission actions, but also engage in assessing the facts themselves.

1 Introduction

In the terminology of principal-agent theory, the development of the European Community's competition policy might be read as a pretty straightforward story of *agency loss or escape* (Wilks 2005a). With the objective of establishing proper control over market-disturbing practices, the founding states of the EC (as the principals) delegated competences in the area of competition policy and law to the European Commission (as the agent). Over time, the principals found that the agent did much more than merely fulfil the expectation of credibly monitoring markets. Rather, the Commission's Directorate General for Competition (DG

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Comp) has developed into a powerful actor in the realm of European – and increasingly international – competition policy. Close observers have described this development as an astonishing transformation of competition policy from a 'sleepy, ineffectual backwater of Community administration' (Wilks and McGowan 1996: 225) into the 'first supranational policy' (McGowan and Wilks 1995). Accordingly, viewed through our principal-agent lens, the story of European competition policy becomes one in which the member state principals see themselves increasingly confronted with a supranational agent, with preferences of its own, which has repeatedly acted against the preferences of at least some member state principals. At the same time, the principals found that their control mechanisms to address agency loss were quite limited.

Without the alternative of reversing the clock, governments have two basic avenues to pursue. They may accept the well-established functional structure of competition policy, and seek to influence the balance in the multilevel structure of European competition policy between the supranational competences of the Commission on the one hand, and national competition authority and courts on the other. The continuous struggle for financial thresholds as criteria for the division of labour between the national and the supranational level illustrates these efforts. Alternatively, governments may seek to maintain control over future developments in European competition policy. The recent debate on the competences of national financial regulators displays the tension between national governments' public support for the consistent application of European competition rules and their attachment to national champions and national control.[1]

Thus far, the story of agency loss is in accordance with traditional applications of rationalist principal-agent frameworks to European competition policy (Bulmer 1994; Pollack 1997, 1998). However, the story becomes somewhat more complicated when we focus on how agent slippage has occurred in practice and how the most recent reform of European policy on mergers and acquisitions fits in. As the latter sails under the flag of decentralisation, it has been interpreted as a quite uncommon event in which an agent (the European Commission) returns some of its powers to the principals (the member states) or at least shares some of its powers with other agents (national competition authorities) of their principals (Wilks 2005a: 435). To understand how the Commission has managed actually to expand its powers in the sectoral governance[2] of European competition policy, we must introduce the European Court of Justice (ECJ) into the equation. The ECJ has frequently backed the Commission's efforts to expand competition provisions beyond their original reach. It has done so not only with respect to Commission decisions in individual cases, but also when commenting on the

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Commission's increasingly common practice of referring to legally non-binding instruments. Today, together with the Court of First Instance (CFI), the ECJ is the most important control mechanism in European competition policy. And yet, as will be shown, it is not a straightforward task to interpret judicial review in principal-agent terminology.

In what follows, I will address both questions – the role of the European Commission and that of European courts – with a focus on this special issue's interest in the linkage between sectoral governance and territorially bound democratic governance. The article starts by presenting some basic information on European competition policy and its development with respect to some important sub-domains: state aids, mergers and antitrust issues. It continues by analysing the Commission's ongoing tactic of referring to legally non-binding instruments and the subsequent approval of this practice by European courts. The article concludes by reviewing the insights on government, governance and judicial review in the area of competition policy in the light of principal-agent theoretical assumptions.

2 *Competition policy in Europe*

2.1. *The rough picture*

With the general objective of ensuring the undistorted operation of the internal market, competition policy encompasses a broad range of targets, including the fight against monopolies, oligopolies, cartels and market-sharing arrangements as well as against subsidies and state protection. The economic justification for addressing these issues is that their resolution will help achieve a more efficient allocation of resources, promote innovation, lower consumer prices and thereby increase societal welfare. As these objectives chime with the purpose of economic integration in Europe as formulated in the Treaties of Paris and Rome, the explicit inclusion of competition policy was coherently reasonable. Although the final wording of the Treaty of Rome did not entail far-reaching competences for the European Commission as had been allocated to the High Authority under the Treaty of Paris, the Commission still enjoyed substantial powers from the very beginning, including the power to decide, implement and enforce policies (Allen 1996; Pinder 1991: 101–4).

Competition policy provisions in the Treaty of the European Economic Community included restrictive practices in Article 85 EEC (in the Treaty of Amsterdam Art. 81 TEC), monopolies and abuse of dominant positions in Article 86 (Art. 82 TEC), monopolies in Article 90

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(Art. 84 TEC) and, finally, state aids in Articles 92–4 (Arts. 87–9 TEC). The procedural regulation to these articles, Regulation 17/1962, not only provided the European Commission with substantial powers, but also protected it from the intergovernmentalist backlash that occurred in the Council in the mid-1960s (Allen 1996: 159). Regulation 17 put the European Commission in a very strong position in relation to companies and provided the it with a monopoly on granting exemptions to behaviour that was otherwise prohibited (Art. 81 (3) TEC).

The formal inclusion of competition policy in the Treaty of Rome did not imply that the actual development of Commission activities in the different dimensions of EC competition policy was linear and even. For instance, before the late 1980s there was no substantial control of state aid, and the liberalisation of utilities and competition policy activities began only in the late 1990s (Wilks 2005b: 117). Concerning the European Commission's control over private companies, antitrust policies – with their two areas of restrictive practice and abuse of dominance – development differently. While in the realm of the former the Commission was able to use its extensive discretion to develop decisions that usually gained approval from the ECJ, it was not until the early 1990s, with the encouragement of the CFI, that the Commission was able to establish a more certain legal grounding (ibid.: 118). Finally, control of mergers and acquisitions, which tends to attract media attention because of the frequent involvement of well-known companies, was omitted from the Treaty of Rome, essentially because it was not thought of as a priority by the member states (Hölzler 1990: 9).

2.2. Linking governance to government, new modes of governance and judicial review

Let us now turn to a quick overview of issues and milestones in European competition policy. Roughly speaking, while the first twenty-five years of European competition policy were characterised by a separation of national and European competition policies, from the mid-1970s onwards there has been greater integration into one functional area. Paradigmatic for the first phase was the 'double-barrier' theory established by the ECJ in the case of Walt Wilhelm (case 14/68), according to which agreements between private parties must satisfy both Article 85 EEC and national law (Goyder 2003: 440). A feature of the later development was the continuous debate on the degree of centralisation or decentralisation and the formal division of competences between the European and the national level within the functional area of European competition policy (Dabbah 2003: 95).

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In what follows, I will present a more fine-grained analysis, which provides more detailed insights into the link between sectoral governance and territorially bound government. A closer look at two areas of competition policy, each with a different history – state aid control and the control of mergers and acquisitions – sheds some light on the dynamics linking government to governance, looking especially at new modes of governance and judicial review by European courts.

Control of state aid

As part of European competition policy, state aid control under Articles 87–9 TEC is not only of practical relevance for national and sub-national activities: what is more, it links the European level and the member states in politically sensitive areas such as industrial subsidisation or regional policy. Whereas Article 87 TEC generally bans direct or indirect state aid that has the potential to distort competition, the same article also permits exemptions in particular circumstances. Paragraph 2 lists conditions that make aid automatically compatible with EC provisions (e.g., aid to make good the damage caused by natural disasters or exceptional occurrences) and enumerates circumstances that may be compatible (such as aid to promote the economic development of areas where the standard of living is abnormally low or where there is serious underemployment). Member states are obliged to notify the Commission, which is at the centre of the EC's state aid control system, of aid schemes. Via the Council, member states may determine the procedural rules under which the Commission operates.

Secondary legislation played, however, only a minor role in the design of rules governing state aid control, and it took until 1998 for the member states to agree to adopt official regulations (Council Regulations 994/98 and 659/99). As a consequence, the Commission had to navigate in very sensitive areas in which support by the member states, as the targets of Commission activities, could not be taken for granted (Wilks 2005b: 123) and in which intra-organisational tensions between different directorates general of the Commission were quite common. Interestingly, there was a shift in the strategy of the Commission or, perhaps more precisely, in that of what was then Directorate General IV: faced with resistance to enacting provisions on state aid control by the member states in the 1960s and 1970s, the Commission was less and less inclined to formalise its powers in the 1980s and 1990s (Cini 2001: 199).

Instead, as early as 1971, the Commission used informal modes of influencing the behaviour of its interlocutors. With its first informal instrument – a letter to the member states in which the Commission laid down the principles of its strategy to deal with state aid in the clothing and textile industries – the Commission established a practice of applying

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legally non-binding instruments. It uses them, for instance, to interpret treaty provisions, to clarify procedural questions, to explain its own case law or that of European courts, and to establish the orientation of its future policy objectives. The instruments include guidelines, notices, communications, recommendations and, as just mentioned, even letters (Aldestam 2004: 14). Of course, many of the objectives could have also been accomplished by regulations. Yet, from the perspective of the Commission, soft law instruments had the advantage of combining time-effectiveness, flexibility, policy stability and credibility, while retaining the most discretion possible (Cini 2001: 199). Sometimes *policy framework* is used as a generic term to describe the function of legally non-binding instruments issued by the Commission (Aldestam 2004).

In the Commission's efforts to accomplish the task of a historic move 'away from state subsidy of industry and, indeed, from traditional industrial policy' (Wilks 2005b: 123), two factors proved important. The launch of the common market programme changed the intra-Commission balance between the competition and the industrial DGs in favour of the former. What is more, the Commission was backed by the ECJ and the CFI. For instance, in the dispute between some member states and the Commission on the question of whether Article 93(2) EEC (86(2) TEC) applied only to existing and new state aid schemes, it was an ECJ judgement (case 173/73, Italy vs Commission) that authoritatively confirmed the Commission's power to apply the provisions also to non-notified cases. An important decision contributing to the 'sea change' in the evolution of the Commission's state aid policy (Allen 1996: 177) is the ECJ's award in the dispute between the Commission and Philip Morris (case 240/82, Philip Morris vs Commission). The subject of the case was the subsidies granted to Philip Morris by the Dutch government, which were considered by the Commission to be incompatible with EC provisions. Reacting to the appeal, the ECJ established the principle that, in applying Article 93(3) TEC, the Commission may assess the economic and social implications of a state aid in a Community context.

European courts were not only involved in judicial review of the Commission case decisions, but also in its practice of referring to legally non-binding instruments. While the ECJ generally acknowledged the Commission's competence to use its discretion to ensure the smooth and proper implementation of Community policies, certain judgements were more restrictive. Some examples may illustrate this point. In France vs Commission (case C-325/91), the ECJ stated that the Commission's policy frameworks must clearly set out their legal basis in order to become binding. In the context of the Commission's policy framework dealing with state aid to the motor vehicle industry, the ECJ had to decide in a series of cases between the Commission and Spain. The ECJ

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acknowledged the Commission's competence to establish rules – under exceptional circumstances – without the agreement of the member states (C-135/93).[3] A couple of years later, however, the ECJ emphasised the conditionality of this Commission competence and annulled a Commission decision because the exceptional requirements were not given at the time of the action (C-295/95). Yet in another case the ECJ emphasised that, for reasons of legal certainty, the policy frameworks in state aid policy are binding on the Commission. In the case CIFRS vs Commission (C-131/90), the ECJ stated that the Commission had to abide by a policy framework established in 1984, and that any departure from this policy required the agreement of the member states.

Merger and antitrust policy

The control of mergers aims to outlaw those mergers and acquisitions that have the potential to distort competition. European regulation on mergers and, more generally, antitrust issues brings the Commission in direct contact with business in the member states, and cases frequently gain a substantial degree of public attention (e.g. the cases of Pfizer/Pharmacia, General Electronics/Honeywell and Vodafone/Mannesmann). Although the Treaty of Rome lacked any relevant provisions, the Commission conceived mergers, acquisitions and joint ventures as a potential source for anti-competitive behaviour from the very beginning. Given the omission of provisions in the Treaty and faced with continued resistance from key member states (France, the UK, Germany) to the delegation of further competences to the European level, the Commission has repeatedly tried to use Articles 85 and 86 EEC (Arts. 81 and 82 TEC) to achieve control over mergers. In so doing, it was on several occasions backed by judgements of the ECJ (Hölzler 1990: 10; McGowan and Cini 1999: 179). For instance, in the Continental Can judgement (case 6/72), the ECJ approved the Commission's action to regulate the concentration of the industry with Article 86 EEC on abuse of dominant position. Also, in the tobacco industry judgement on Philip Morris (cases 142 and 156/84),[4] the ECJ stated that Article 85 EEC not only refers to restrictive market practices but also may be applied to mergers.

While disagreement within the Council repeatedly blocked the Commission from formally delegating competences in the area of merger control, the Commission's substitute strategy of stealthily extending its competences led to a substantial degree of legal uncertainty. By the mid-1980s both its conceptual approach and its practice faced considerable criticism from industry as well as from some member states.

Germany and the UK in particular criticised merger control policy as too lax and too politicised; in the 1990s they called for an independent

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European merger control agency (McGowan and Wilks 1995). At the same time, the Commission faced additional difficulties. While its move to address state monopolies in public utilities was not especially welcomed by the member states, a lack of precision and stringency in the interpretation of the concept of market position led both the ECJ and the CFI to override Commission decisions on several occasions (McGowan and Cini 1999: 181; McGowan and Wilks 1995: 150; Morgan 1998). Finally, the steady increase in the number of cartel, antitrust and merger activities since the mid-1980s and the increasingly extraterritorial dimension of merger control activities – with the Commission's interventions in the case of Boeing/McDonnell Douglas and General Electronic/Honeywell being only the most visible cases (Morgan and McGuire 2004) – made existing problems in the established regulatory framework only too apparent.

Because of the continuing resistance of some member states, the first European merger control regulation became effective only in 1990 (Council Regulation 4064/89). A critical point in the debate was the relationship between the European Commission's competences in addressing merger cases and those at the national level. In particular, those countries with well-established control agencies, such as Germany and the UK, opposed what they saw as the excessive dominance of the European Commission. The compromise established absolute turnover thresholds allowing for a 'necessarily arbitrary' determinant of jurisdiction – either the Commission's or a member state's – on a case-by-case basis (Morgan 2001: 456). A second important conflict revolved around the balancing of conflicting criteria, with Germany and the UK favouring a strict competition policy and France wanting to include social and industrial policies in merger control (Pollack 1998: 233).

Notwithstanding the fact that the 1989 merger control regulation granted the European Commission, for the first time, proper control competences in the realm of mergers and acquisitions, the reality of an increasing workload made the situation precarious again shortly after its enactment. The Commission continued its practice of using bloc exemptions (granting approval to an entire class of cases according to Article 81(3) TEC) and so-called comfort letters (interim measures relieving companies from future fines in the case of a negative decision by the Commission) to meet the deadlines of its control regime. However, actual economic developments soon rendered the new regulatory framework unsatisfactory. The more the single European market took shape, the more strained were the Commission's resources; as a consequence, the enforcement of Articles 81 and 82 TEC became more and more critical. In this situation, decentralisation became an ever more appealing option for the Commission (McGowan and Wilks 1995: 168 n. 43), and it

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launched a fundamental overhaul of its merger control and antitrust policy. Following the issuing of green and white papers on merger control and an interim amendment of the 1989 merger regulation in 1997, the Council of Ministers adopted a new legal framework for the enforcement of Articles 81 and 82 TEC in 2002 (European Commission 1996; European Commission 1999; Council of the European Union 2002).

Entering into force in May 2004, the new legal framework of Regulation 1/2003 replaced the forty-year-old system of Regulation 17/1962. Most importantly, the regulation implies a new approach to the implementation and enforcement of the antitrust and merger control policy of Articles 81 and 82 TEC, with the key words being 'decentralisation' and 'modernisation'. *Decentralisation* refers to the devolution of the policing of anti-competitive behaviour and of complaint-handling to the European family of competition authorities: the national competition authorities and the European Commission, linked through the European competition network. The concept of *modernisation* captures the new priorities of the Commission's enforcement agenda, such as private enforcement of company activities in national courts.

While the new regulation provides the skeleton of the new regulatory regime, some important questions have been left open, including: the scope of exemption provisions according to Article 81(3) TEC; the clarification of criteria for case allocation; and measures to ensure a harmonised application of European provision by national competition authorities (e.g. leniency provisions). The Commission has put flesh on the bones of the new regulation by adopting an implementation regulation plus (by the time of writing) more than twenty notices and guidelines to address the questions and to provide guidance on various aspects of the enforcement of the Articles 81 and 82 TEC.[5]

These activities indicate that, as with state aid control, the Commission has established a practice of referring to legally non-binding measures in the area of antitrust policy. For instance, the Commission's first notice on agreements of minor importance which are expected not to restrict competition under Article 81(1) TEC ('de minimis Notice') was published in 1986 and has since been revised several times. In addition, comfort letters, as quick and informal means, allowed the Commission to decide on cases by communicating to companies that their agreement does not infringe Article 81(1) TEC.

With respect to the judicial review of legally non-binding instruments, the ECJ's practice has been quite permissive. It granted the Commission the competence to use guidelines to indicate the directions of its policies (ECJ in Agranda Zucker und Stärke vs Commission (2001)) or to use administrative guidelines to lay down 'policy rules' for the exercise of its discretion (ECJ in Netherlands vs Commission (2002)). At the same time,

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European courts confirmed their position that administrative guidelines, which have an abstract-general scope of application, may not be implicitly amended by decisions in individual cases. Although both the ECJ and later the CFI frequently allowed the creeping extension of supranational competences through Commission decisions, they maintained a strict review policy. In particular the CFI reached a number of judgements (Airtours/First Choice (T-5/02 and T-80/02), Schneider Electric (T-48/03) and Tetra Laval (T-5/02 and T-80/02)) in which it not only overturned Commission decisions, but also explicitly criticised the Commission's economic expertise, its use of evidence and its procedures (OECD 2005: 43; Wilks 2005b: 122).

3 Assessing links, actors and impacts

Thus far, I have presented information about fundamental developments in almost fifty years of history of competition policy in Europe as well as about basic factors that have influenced these developments. Recalling occasionally tough Commission decisions, in particular in the area of state aid, member states were reluctant to provide the Commission with more explicit and detailed competences to fight effectively against any restriction or distortion of market competition. The Commission's strategy of expanding its competences involved both the creeping exploration of new jurisdictions and the increasing reference to legally non-binding instruments. Both strategies were frequently encouraged by European courts which became, over time, the most important control mechanism over Commission actions and decisions. In what follows, I will address each of these aspects with attention to the link between sectoral governance and territorially bound democratic government.

3.1 Member states as principals

In outlining the analytical framework of this special issue, Héritier and I introduced some basic assumptions about the properties of principals and the relationship between principal and agent. In accordance with the theoretical principal-agent literature, important properties are preference constellations in the case of multiple principals, the distribution of information between principals and agents, and the organisational arrangements and decision rules within which the principals might exercise their control powers (see also Pollack 1997).

The first important aspect that needs to be taken into account is related to the fact that, in the context of European integration, we deal with multiple principals. This necessarily implies a multiplicity of national preferences that have to be accommodated before a unified voice of the

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principals can be heard. This is not to say that individual government actors had no impact on the history of European competition policy. For instance, during the depression in the mid-1970s the member states exercised significant pressure on the Commission to relax its control of governmental industrial policy interventions (Allen 1996: 177).

Later, in the mid-1980s, discontent with the Commission's policy and control practice led some governments to call for a recontracting, i.e. structural change involving the attribution of control competences to an independent European agency. The concern about the Commission's exercise of European competition policy arose from different sources: France, which had just successfully defeated the Commission on state aid and mergers, basically supported a maintenance of the status quo in the pursuit of competition policy and the distribution of competences between the national and the European level; Germany's position, apart from the question of the politicisation of Commission decisions, was dominated by a concern about the creeping centralisation of competences in merger control – the most important field of activity for the resource-rich German national competition authority; finally, the UK shared concerns about the politicisation, transparency and consistency of Commission decisions and supported a greater recourse to national competition authorities (Wilks and McGowan 1995: 263).

This brief summary of positions of key national governments underscores that there was some discontent with the operation of the agent. At the same time, the positions of the principals were still too heterogeneous to be consolidated within the voting procedures in the Council. Rather, different perspectives on the institutional design of a European cartel office and different preferences of the individual principals prevented the disempowerment of the agent. In a similar vein, member states were not able to take the opportunities provided by intergovernmental conferences to significantly 'clip the wings' of European competition policy (McGowan and Cini 1998: 123).

In sum, both 'inability or unwillingness' of the member states and the 'weight of the original treaty provisions' (ibid.) limited the ability of member state principals to constrain the agent's behaviour. Instead, these factors enabled the Commission to pursue its policy path almost undisturbed by democratically legitimated actors, including the Council and the European Parliament. Put differently, the influence of the shadow of hierarchy by territorially bound democratic government on the efficiency of sectoral governance was quite limited. In turn, it was the Commission's strategy to increase the efficiency of its policies by resorting to new modes of governance that bypassed both the member states and the European Parliament. Next, I will address the operational mode of sectoral governance.

New modes of governance

Apart from its case decisions, legally non-binding instruments are of the utmost importance for the Commission as modes of governance in competition policy. The Commission's mandate to apply instruments outside the provisions of Article 249 TEC derives from Article 211 TEC, which states that 'to ensure the proper functioning and development of the common market' the Commission has to 'ensure that the provisions of this Treaty and the measures taken by the institutions pursuant thereto are applied' and may 'formulate recommendations or deliver opinions on matters dealt with in this Treaty, if it expressly so provides or if the Commission considers it necessary' (Article 211 TEC, points 1 and 2). Under changing labels such as *soft law*, *quasi-legislation*, *informal regulation* and *policy frameworks*, these measures include guidelines, declarations, codes of conduct, notices, communications, letters and interpretations.

These measures are not new nor are they restricted to Commission activities. Since the early 1990s, there has been an intense scholarly debate focusing primarily on issues such as proper definitions and the legal quality of soft law instruments (e.g. Beveridge and Nott 1998; Mörth 2004; Snyder 1994). Criteria for the classification of soft law instruments referred *inter alia* to their origin, their content or their resemblance to either national measures or international private law. For instance, with a focus on the function of non-binding measures, one classification distinguishes between *informative or preparatory* instruments such as papers (green, white or action) and informative communications, *steering* instruments with pre-regulatory functions such as recommendations, and *interpretative or decisional* instruments such as guidelines and notices that spell out ways in which the Commission judges a specific behaviour (e.g. Brammer 2005; Cosma and Wish 2003; Hoffmann 2006).

Among the specific features of these instruments not included in Article 249 TEC is that none of these measures requires Council or Parliament approval. Not only does administrative policymaking occur outside the Council and Parliament, but – given the Commission's information advantage deriving from the incorporation of input from experts and interest groups via hearings and comments in the drafting of papers, notices and guidelines – governance by non-binding rules also strengthens the position of the European Commission in procedural and substantial terms vis-à-vis national competition authorities and national courts. For instance, in a frequently cited case from the arena of social policy (occupational diseases), the ECJ stated that 'national courts are bound to take recommendations into consideration in order to decide disputes submitted to them, in particular where they cast light on the interpretation of national measures adopted in order to implement

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them or where they are designed to supplement binding Community provisions' (case C-322/88: 18).

Also, in times of uncertainty about the interpretation of specific provisions via Commission notices, guidelines and the like may gain a much more binding character in practice. Two examples underline this point. To start with, take the European Competition Network, comprising the Commission and national competition authorities: given the economic and legal complexity of cases, there is some truth in the observation that being a fully fledged member of the European family of competition authorities largely depends on endowment with the appropriate powers of surveillance, investigation and enforcement. At the moment, however, there seem to be different classes of family membership, with some members – the British, French, German and Italian agencies in addition to DG Comp – being in the top tier in terms of budget and case load, while the majority of others lag behind (Riley 2003: 658; Wilks 2007: 5). Also, the knowledge and experience of the national competition authorities are highly unequal in the member states. On the one hand, it is only since 1990 that all member states have had a national competition law. On the other, frequently either the national provisions differed from the Europe approach in their underlying philosophy or there was very little contact between national authorities and European provisions (Riley 2003: 659). Both factors tend to favour the position of the Commission and its efforts to influence the operation of competition enforcement via legally non-binding instruments. The actual relevance of this observation is underlined by a practitioner's view according to which member states might well have felt 'neglected and ploughed over' by the Commission's practice of governing by legally non-binding instruments (Aldestam 2004: 14).

Looking at the sector level – and more and more often Commission interventions based on competition law are sector interventions in cases of either mergers and acquisitions (e.g. in telecommunications) or abuse of dominant position (e.g. in energy) – there is some plausibility in the statement that companies are well advised to follow Commission guidelines on pain of being subject to antitrust law investigations (see Geradin and Sidak 2003: 19). In conjunction with the importance of precedents set by Commission decisions, soft means strengthen the Commission's role in procedural and substantial terms in relation not only to national competition authorities, but also to national courts.

At the same time, legally non-binding instruments are neither neutral nor static. Rather, they must be interpreted with respect both to the interinstitutional politics in the multilevel European polity and to their change over time. On the institutional politics dimension, Cini has convincingly argued that the Commission makes strategic choices for

either hard or soft law. For instance, after repeated unsuccessful efforts to persuade the principal to enact a regulation on merger control, the Commission has learned that its soft laws – which need neither Council nor Parliament approval – are a vital alternative to help exercise control in all areas of competition policy. The Commission even resisted Council pressure to draft Council regulation under Article 89 TEC (Cini 2001: 202).

A second interesting point relates to the observation that soft law instruments develop over time. On the one hand, they may harden as legally non-binding instruments of the Commission are replaced by legally binding Council regulations. For the state aid regime, Aldestam and Cini have identified such transformations. They distinguish between substantial matters, in which soft law complements hard law, and procedural matters, in which hard law replaces soft law (Aldestam 2004: 31; Cini 2001: 203). The transformation from hard to soft law may aim at ensuring compliance where voluntaristic approaches have failed. An important force in this hardening is the judgements of European courts, with the stance of the CFI being firmer than that of the ECJ. Accordingly, Cini interprets the ultimate willingness of the Commission to draft state aid regulations 'as a way of pre-empting further more restrictive procedural judgements by the courts' (2001: 203). Along similar lines, court judgements have added specific impetus to legally non-binding instruments. For reasons of legal certainty, legitimate expectation and equal treatment, legally non-binding modes of governance may produce a legal effect not on the addressees but on the Commission (joint cases C-189, 202, 205, 208, 213/02 P, Dansk Rørindustri and others vs Commission) (e.g. Aldestam 2004: 27; Hoffmann 2006: 159). But neither of these tendencies implies that the soft law of sectoral governance prepares the ground for government. Rather, the rules of the sectoral governance may harden and may contribute to its centralisation over time.

Judicial review

The debate about the contribution of European courts to the development of sectoral governance in European competition policy now leads us on to the issue of judicial review. Indeed, as frequently mentioned, judicial review by European courts has gained the utmost importance in the making of competition policy. So far, European integration theory has established that the interplay of the Commission and the ECJ – rather than the conventional policymaking triangle of Council, Commission and European Parliament – fuels a supranational pull (Burley and Mattli 1993; Weiler 1994). This observation is based on the pattern of court decisions that have later been exploited by the

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Commission, with the Van Gend en Loos and Cassis de Dijon cases being the most prominent (Alter and Meunier-Aitsahalia 1994). With few exceptions, the European political science literature has given much less attention to judicial review as a means of controlling the Commission's policymaking via case decisions and soft modes of governance.

In particular, a body of literature similar to that on the US judicial oversight of administrative agencies is largely missing at the European level. It is, however, possible to extract some insights from findings on constitutional review and research in the realm of social-legal and administrative studies (Hertogh and Halliday 2004). While the constitutional review literature addresses the validity of norms enacted by the traditional legislative process, that on social-legal and administrative studies is more concerned with the scrutiny of the executive branch's compliance with public law. The latter aspect, especially, points to differences between national traditions of judicial review and control. For instance, the English model may be characterised as rights-based approach, in which the rule-of-law focus of review is at odds with a review of policy substance of administrative rule-making. This is in stark contrast to the US 'separation of powers'-focused, institutional design model, in which we find a strong inclination towards control over administrative rule-making not only in procedural but also in substantial terms (Cane 2004).

Following this observation, it would be interesting to know whether – following the European emulation of the US-style regulatory state model – judicial review at the European level will again experience a development similar to that of the United States. In the American case, Shapiro has identified that, alongside an extension of the delegation of rule-making competences to administrative bodies and independent agencies, courts established demanding judicial review policies and struck down administrative rules themselves (and not merely their individual application) on both procedural and substantial grounds (Shapiro 2004).

For a long time, the situation in the EU was different. European courts were relatively reserved in exercising the powers of Article 230 TEC to review legally non-binding measures of the Commission. If they did so, the focus was either on the individual application (as in the annulment of the policy framework of state aid for the motor vehicle industry) or on general features, such as the Commission's competence to provide guidance by administrative rather than legislative means. The same was true also for court review of Commission decisions.

As a long-time CFI judge explains, the court defines its role in terms of judicial review rather than full judicial control: 'Our task is to review the legality of what has been done. But this is a very different thing from a judge trying a case himself' (Bellamy 1999: 18). In a similar vein, the current president of the CFI, Bo Vesterdorf, states that the 'CFI simply

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checks whether or not the Commission correctly applied the law as interpreted by the Community Courts'; in addition, it controls the facts. While in neither of these two arenas is there 'room for discretion on part of the Commission' (Vesterdorf 2005: 13), it does have discretion when assessing the facts. Yet, in practice, the analytical distinction between law and facts with unlimited judicial review on the one hand and the assessment of facts with limited judicial review on the other is not as clear. As another former CFI judge has described, the procedure of review of the Commission's discretionary decisions necessarily has to test the soundness of the Commission's appraisals. By so doing, however, 'judges are obliged to examine the administrative file, thereby inevitably bringing themselves intellectually close to building their own bridge from the facts, via the legal framework of the case, to a legal outcome in casu' (Tiili and Vanhamme 1999: 888).

The question of whether or not the CFI exceeds its competences under Article 230 TEC by assessing the facts rather than limiting its review to the control of the law and of the facts was the subject of a Commission appeal to the ECJ. In 2002, the Commission prohibited a merger between Tetra Laval and Sidel, two companies active in the industry for liquid food packaging, on the grounds of risk of the abuse of dominant market position.[6] Redefining core economic concepts such as *conglomerate*, the CFI came to the conclusion that the Commission had failed to produce convincing evidence; it therefore annulled the Commission's decision due to a manifest error of assessment of facts. In turn, the Commission filed an appeal to the ECJ firstly on substantial grounds (contesting the standard-of-proof criteria) and secondly on the grounds that the CFI had exceeded its jurisdiction under Article 230 TEC by not restricting its review to the question of whether or not the Commission had made a 'manifest error of assessment'. With respect to the second point, the ECJ confirmed that the Commission has a certain degree of discretion in the economic assessment of facts. At the same time, European courts act in accordance with their competences when reviewing the Commission's assessment of information and economic implication of a specific activity.

Overall, it can be said that the ECJ and the CFI have intensified their examination of Commission practices over time. The interpretation of the scope and depth of judicial scrutiny has been significantly extended. The more the CFI has stretched the limits of its judicial scrutiny, the more the margins of the Commission's discretion have diminished (Bailey 2004: 1358). The European courts' changing interpretation of their role indicates that judicial review is not a static concept. It also implies that the differentiation between judicial review and judicial control may and, in the present case, has diminished. The increasing relevance of the CFI

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finds also expression in numerical terms. As of September 2007, the CFI has issued thirty-one judgments under the EC merger regulation and it has annulled nine Commission decisions (Bailey 2007: 103). In sum, it seems legitimate to argue that the European model of judicial review is indeed moving in the direction of the American model, with its stronger substantial impetus.

Conclusion

One might start the conclusion by characterising the role of the European Commission. The literature suggests a number of portrayals: it is the 'first among equals' in the European competition network (Maher 2006: 12); it is 'more than an agent in state aid' and, even more in line with Majone (2001), it 'has become as a trustee of the competition rules' (Wilks 2005b: 123, 127). These portrayals indicate that applying a principal-agent perspective not only can provide interesting insights into the relationship between territorially bound government and sectoral governance in the realm of EU competition policy, but also, what is more, it can take us very close to the limits at which the approach is applicable.

The starting point was the limited willingness of the member states to delegate proper competences to the Commission in the functional area of competition policy. Viewed positively, over time the Commission, as the agent of the national governments, managed to cope quite successfully with this incomplete vertical integration (see Eberlein, in this issue). Backed by the European Court of Justice in its strategy of expanding its jurisdiction, the Commission established itself at the heart of a quite powerful competition policy regime in the EU. Given the heterogeneity of the principals and their disagreement about central issues, the shadow of hierarchy remained relatively pale.

More negatively, such an interpretation tends to underrate the complexities of modern administrative processes in the EU's multilevel setting. Instead, it seems necessary to acknowledge a dynamic and an interdependence that make modern administrative patterns two-way streets, rather than one-way efforts of principals seeking to control agents (Krause 1999). Especially in the European multilevel constellation, the changes over time have become akin to in-built institutional features. The actual patterns of change are related not so much to the behaviour of single actors but instead to two-way signalling processes of the actors in the system. In the case of competition policy, the interdependence of member states and the Commission (and the courts) can frequently be traced. On the one hand, the shadow of governmental hierarchy became visible not only through the budget, but also through the threat of recontracting, i.e. by reallocating regulatory competences from the

Commission to a European central competition agency. A more recent example is the new French president's intervention about the role of competition policy in Europe's Reform Treaty at the 2007 EU summit in Berlin. On the other hand, the Commission sent both accommodating and threatening signals to the member states. For instance, its relatively lackadaisical control regime in the period of institutional crisis ('Eurosclerosis') signalled an awareness of the strain put on the member states' capacity for collective action. At the same time, the Commission did not hesitate to take a firm stand against the resistance of large member states as well (Büthe and Swank 2005). The recent annual Report on Competition Policy documents the Commission's practice of combining different instruments, including advocacy and fines, to achieve its objectives (European Commission 2007).

Notwithstanding the foregoing ambiguous assessment, the principal-agent perspective has helped us gain insights into the relationship between government and governance. As has been shown, it was the Commission's strategic behaviour rather than the shadow of hierarchy that has in large part spurred efficiency gains. In recent years, part and parcel of its strategy has been the increasing use of legally non-binding instruments such as notices or guidelines. For the Commission, these instruments have the advantage that they need approval neither of the Council of Ministers nor of the European Parliament. With the Commission's promotion of new modes of governance in the area of competition policy, the link between sectoral governance in terms of regulation specific to competition policy and the governmental shadow of hierarchy shifted, to an ever larger extent, on to the mechanism of judicial review by European courts.

The role of European courts in general and the relationship between the courts and the Commission in particular are disputed in the literature that takes a principal-agent perspective. For the present topic – interaction between territorially bound government and sectoral governance – it is necessary neither to define the status of European courts nor to address the reason for the delegation of dispute resolution to a third party by the member states.[7] Rather, even when displaying their teleological vision on the integration process in general and on the goal of the single market programme in particular, the decisions of European courts have been based on the legal framework established by the member states. Within this framework, judicial review of Commission decisions by the ECJ and the CFI has certainly been the most important control mechanism for member state governments (as well as for individual companies) in the area of competition policy.

The effect of judicial review both on administrative decisionmaking by cases and soft modes of governance and, more generally, on institutional

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development in the EU is twofold. For one, we might expect a positive impact on the overall efficiency of European competition policy, which may find expression in a higher degree of legal certainty, in more coherence in the Commission's application of new modes of governance, and in a less disputed distribution of cases between national and supranational jurisdictions. Also, the increasing backing of Commission decisions and instruments on economic reasoning might be related to the criticism of Commission decisions by European courts.

At the same time, judicial review tends to contribute to a creeping supranationalisation of both de facto and de jure competences. On the one hand, we have a supranational rather than an intergovernmental actor supervising a supranational agent. On the other, it is not too far-fetched to argue that the focal point of this supranational judicial review will be European rather than national. A good case in point is the CIF case,[8] in which the ECJ emphasised the 'European role' of national competition authorities as well as national courts in competition cases. And, finally, as judicial review establishes a legal rather than a political discourse, the emergence of new modes of governance does not necessarily break the spell of integration through – supranational – law as is sometimes assumed in the literature on legally non-binding instruments. It remains to be seen whether a bureaucratic-judicially dominated character will restrict the politicisation that has long been present in European competition policy.

NOTES

1. 'Financial Regulators Oppose EU Reform', *Financial Times*, 2 Oct. 2006, p. 2.
2. Governance of competition policy is cross-sectoral rather than sectoral.
3. 'Exceptional circumstances' occurred when there was shown to be an 'overriding need to maintain undistorted competition in the motor vehicle industry'.
4. The cases are not linked to the aforementioned Philip Morris case in state aid matters.
5. See ec.europa.eu/comm/competition/mergers/legislation/legislation.html (last visited 17 June 2007).
6. For the following, see cases T-5/02, Tetra Laval vs Commission (Tetra Laval I) [2002] ECR II-4381 and C-12/03 P, Commission vs Tetra Laval (Tetra Lava II) [2005] ECR I-987.
7. For the controversial debate, see e.g. Alter 2004; Alter and Meunier-Aitsahalia 1994; Burley and Mattli 1993; Pollack 1997; Garrett 1995.
8. Case C-198/01 Consorzio Industrie Fiammiferi (CIF) vs Autorità Garante della Concorrenza e del Mercato, Judgement of 09.09.2003; see Nascimbene 2004.

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