

## Maritime pilots services in seaports and the four fundamental freedoms of the EC-Treaty

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*Zwei Mal hat die EU-Kommission versucht, die Hafendienstleistungen zu liberalisieren. Dazu gehören auch die Seelotsendienste. Der auf einem Vortrag im Rahmen der Jahrestagung der Europäischen Seelotsenvereinigung (EMPA) in Bremen basierende Text untersucht die Vereinbarkeit der Monopolstellung der Seelotsen mit dem Europäischen Wettbewerbsrecht.*

### I. Introduction

#### 1. The liberty principle of the European Union's fundamental freedoms

The freedom of *each and every* citizen is limited by the freedom of other citizens.

This – at the same time simple and plausible – statement puts the limitations of liberty rights in concrete terms. It derives from the French Declaration of the Rights of Man and Citizen of 1789 and has continued to have an effect until nowadays. The wording of Article 2 paragraph 1 of the German Basic Constitutional Law provides evidence for this. This provision declares the basic constitutional rights and, therewith, also the freedom of another person as a constitutional limitation of the general basic freedom of action, which also comprises the so-called freedom of competition.

In the area of competition, these days containing not only the economic, but also the legislative area (for instance, in the shape of a competition of location), the limitation formula of the French Declaration of the Rights of Man and Citizen appears to be both, helpful and pointing the way to the future. At this point, it

may be interpreted to the effect that *all market participants* with their efforts towards customers, sales and turnover have to respect the *legitimate rights of other market participants*. This fundamental principle determines, for example, the regulations as set out in the Unfair Competition Act (Gesetz gegen unlauteren Wettbewerb – UWG).

However, before this background *one* important issue arises: *How* does a situation have to be assessed in which the participation in competition is restricted to a limited group of suppliers in advance; be this on the basis of cartel agreements or factual access restrictions – such as they may evolve from Mafia-type structures – or through statutory barriers such as the introduction of local monopolies?

In *each* of these just mentioned cases the principle of liberty *rebels*. It sides with those people whose free access to the market is restricted and calls for a *justification*.

It stems from this – just as simple as consistent – line of thought if during the past few years the European Commission has repeatedly undertaken the attempt to liberalise access to seaport services.

*Yet*, the European Commission was not only able to found its actions on the basis of the general principle of liberty. In addition, it could *also* rely on this principle's legal illustration in the fundamental freedoms of the EC-Treaty. These form the basis of the European internal market, which *still* needs to be regarded as

being the *centre* of the institutional arrangements of the European Union.

The *freedom of market entry* constitutes the central condition for competition within the internal market. It requires that access to all markets within the European Union will be ensured to every individual and each enterprise that wishes to offer services. Thereby, durable stays are protected by the freedom of establishment and temporary stays are safeguarded by the freedom to provide services.

Restrictions of free access to a market – as they are primarily erected by monopolies and numerical restrictions of another kind – are *generally* prohibited but *at least* subject to a special duty of justification.

## 2. Maritime pilots services as monopolised port services

Simple provisions and also the liberty principle as embodied in the fundamental freedoms do *not always* reach reasonable solutions. With regard to economic activities, this is in particular true where *either* the provision of services requires the fulfilment of special demands *or* the respective market is characterised by certain general set-ups. *Therefore*, in the economy *as well as* in competition law, it is an ever-accepted circumstance that monopolies may not only be justified under certain prerequisites, but may from the perspective of the economic principle *even be* sensible and necessary.

*This insight* is only hard to accept for some supporters of the principle of free competition. Despite of this, it has legitimately found its expression also in European law, *namely* in Article 86 paragraph 2 of the EC-Treaty. At the same time, this provision illustrates under which conditions the freedom of competition may be restricted. The formulation of the provision is as follows:

“Undertakings entrusted with the operation of services of general economic interest or having the character of a revenue producing monopoly shall be subject to the rules contained in this Treaty, in particular to the rules on compe-

tion, insofar as the application of such rules does not obstruct the performance, in law or in fact, of the particular tasks assigned to them. The development of trade must not be affected to such an extent as would be contrary to the interests of the Community.”

In the following paragraph of Article 86 EC, the European Commission is furthermore authorised to address appropriate directives or decisions to Member States in order to ensure the application of this provision.

European law acknowledges – and this is absolutely in line with the economic theory – the principle of liberty and competition as the *determining* basis of the internal market. *Nevertheless*, at the same time, it allows deviations and restrictions under certain prerequisites, which are subject to a specific justification duty.

*In addition*, for this justification *clear* criteria are established:

- First of all, services of *general economic interest* need to be at stake.
- Moreover, it has to be explained that *without the introduction of a monopoly* or another restriction of free access to the market *the respective service* may legally or factually not be delivered.

## 3. The European Commission's point of view concerning the liberalisation of port services

I assume that it sounds just *too* familiar to *all* of you that during the past few years the European Commission, based also on opinions expressed by Member States, has repeatedly attempted to liberalise port services including maritime pilots services, *namely* to abolish the monopoly of pilots in seaports.

Given the *fact* that the European Commission has withdrawn its proposal concerning the port package II directive as a consequence of the distinct disapproval of the European Parliament, one *might* think that it is currently inopportune to reflect on this topic any longer. From a perspective *solely* orientating itself by daily politics this evaluation might be right.

*However, from an academic standpoint as well as from a viewpoint taking into consideration also medium-term and long-term professional politics it is indicated to furthermore deal intensively with this subject in order to deepen and illustrate the arguments in favour of a *continued existence* of the monopoly for maritime pilot services in seaports. This will be a central concern of my speech.*

I would like to show that for the services offered by maritime pilots the *conditions* set out in Article 86 paragraph 2 EC for a restriction of free access to the market are *fulfilled*.

Having said this, I would like to emphasise that this outcome will *not* only be the result of an approach characterised by a purely defensive basic attitude. *On the contrary*, I would like to illustrate that the aims pursued by the competition principle may be implemented *adequately and equally good* by means of the liberal professional's principle of self-regulation as attained in the German law dealing with maritime pilots *so that* it would be absolutely wrong to talk of a "necessary evil" in this context.

On the one hand, I will orientate my reflections on the structure of the Act in classical juristic manner. *At the same time*, I will also consider the arguments put across by the European Commission in its proposal for a directive on market access to port services.

## **II. Maritime pilots services as services of general economic interest**

In the second part of my speech, I will, *first of all*, reflect on the definition of "services of a general economic interest" *and*, thereafter, I will show that the services provided by maritime pilots fall under this definition.

### *1. Services of a general economic interest*

Every reference to the exceptional provision of Article 86 paragraph 2 of the EC-Treaty *initially* requires proof that the privileged activity constitutes a service of general economic interest.

The expression „general economic interest“ is the *decisive* criteria to define what kind of undertakings entrusted with the operation of ser-

vices Article 86 paragraph 2 EC comprises. The included activities of undertakings are *not limited* to services in the sense of Article 50 EC. *Rather*, all economic activities to ensure infrastructure and services for the public are enfolded by the term; according to recent case law also activities in the interest of public security should be covered. Besides classical services, the mentioned economic activities include the supply of goods and other contribution in kind, too, especially the supply of energy.

The national courts within the European Union circumscribe the term as "... services in favour of all users in the entire sovereign territory of the respective Member State regardless of special cases and the efficiency of each single process".

The deciding factor is that the undertakings in question act in the general economic interest. An exact definition of what this actually means does not exist at European level. *Yet*, Article 86 paragraph 2 EC says that the undertakings entrusted with the operation of services of general economic interest are those, onto which a special task was delegated.

In spite of opposite initiatives during the consultations concerning the Treaty establishing a constitution for Europe, responsibility is *still* incumbent on *national* governments to define these special tasks. In this regard, these should rest on an as widely as possible spread spectrum of opinions under particular consideration of the users of services. Their decision may be scrutinised by Community institutions only insofar as "evident mistakes" are concerned. Consequently, a conceivably *broad* scope exists when arrangements are set up. "General economic interests" may, *therefore*, have a different content in the different Member States.

*Nevertheless*, the overriding definition criteria have to be taken homogenously from Community law, because the term laid down in Articles 86 and 16 of the EC Treaty is a European expression.

The case law of both, the European Commission and European Court of Justice limits the term from two sides:

On the one side, it needs to be differentiated from sheer individual or group interests. Services are only “general” if they are *at least also* provided in the public interest. For this, the interest of a part of the population or of a single municipality is sufficient. A *strong* indication for action in favour of the general public constitutes a situation in which undertakings also unfold activities contradictory to their *own* economic interests. This is especially the case with partly unprofitable services, which for reasons of a steady supply of the population still need to be available exhaustively.

On the other side, it has to be differentiated from public interests of a *non-economic* kind.

A *further* prerequisite is an entrusting act. In this respect, “*to entrust*” means that a task in the abovementioned sense needs to be transferred by means of an Act of state to the undertaking. *For this reason*, the entrusting act requires the passing of *one* or *more* law-making or administrative acts. With regard to its content, the entrusting act has at least to indicate the selected undertaking to the extent that enables others to individualise it. Furthermore, the entrusting act needs to contain certain commitments concerning the special task and the entrusted undertaking. For example, the entrusting act has to describe especially the kind and duration of the public interest duty, to state the entrusted undertaking/s, the geographical area of applicability as well as kind and duration of possibly granted exclusionary rights.

Besides, in the entrusting act *parameters* for the calculation, supervision and possible change of the equalization payment as well as the precautions have to be described, which ensure that no *over-compensation* arises *or rather* excessive equalization payment is granted back. According to this, the active sovereign conferment of responsibilities and

competences for a task of general economic interest in an *act of law* fulfilling the described conditions is necessary. According to recent adjudication, this may also happen by means of actively conferring concessions of public law. Passively allowing permissions, the opening of a legal frame for a supplying activity entitling basically everybody or putting one economic sector under state supervision are insufficient instruments.

Whether such an entrusting act has to be demanded also from undertakings in the sense of Article 86 paragraph 1 EC, has not been definitely decided yet. For reasons of equal treatment of private and public undertakings it has to be considered as being also necessary to entrust public undertakings. As a rule, this will already be included in the granting of special or exclusionary rights. Whether a suitable entrusting act exists, falls within the competence of national courts to decide.

In Article 16 of the EC-Treaty, which was newly created by the Treaty of Amsterdam, “services of a general economic interest” have – *for the first time* – received recognition as an *independent* economic model at the level of European Community primary legislation for the first time. The special emphasize of its importance for the European Community strengthens the rating of such services. Furthermore, from the respective Declaration to the Final Act it becomes clear that the parties of the Amsterdam Treaty considered an implementation of Article 16 EC (functioning of common economic services) according to certain criteria (“equal treatment”, “quality”, “durability”) as being significantly important.

Article 86 paragraph 2 EC states as a rule that *all* enterprise-related treaty provisions, especially Articles 81 and 82 EC, are applicable also to the undertakings mentioned in this paragraph. The provision permits only in second line exceptions to *this* principle considering the special duty of some undertakings towards the general public. For this, two levels of examination need to be passed: the obser-

vance of treaty provisions has to obstruct the performance of the particular tasks assigned (1); moreover, the development of trade must not be impeded contrary to the interests of the Community. It requires the fulfilment of strict conditions in order to assume that there is an element of "obstruction" in the sense Article 86 paragraph 2, last part of the sentence.

Necessary is the existence of a concrete conflict between the fulfilment of tasks by the undertaking acting in the public interest and the observance of its treaty duties as established by Community law. Article 86 paragraph 2 sentence 1 EC uses the formulation "obstruct". Therefore, it is *insufficient* if provisions of the EC-Treaty only *complicate or hinder* the fulfilment of the delegated task. It has to be *impossible* to provide the respective service under these circumstances. Hence, logical impossibility is irrelevant; otherwise for Article 86 paragraph 2 EC no scope of applicability would remain any longer. Impossibility rather has to be understood in the sense of unreasonableness. The European Court of Justice, European Commission and prevailing academic opinion ask whether there is *another* technically possible and economically as well as legally reasonable way to fulfil the respectively delegated task *without* a breach of the EC-Treaty. According to recent case law of the ECJ, it is decisive to examine whether there is a threat for the public interest tasks "under economically well-balanced conditions".

The conflict between task fulfilment and the observance of treaty provisions has to be proven concretely. The onus for this is on the Member State, which "entrusts" this undertaking.

## 2. *Applying the definition criteria to maritime pilots services*

The conditions for applying Article 86 paragraph 2 EC described therewith *now* need to be applied to maritime pilots services. As far as this point is concerned, it may without difficulties be assumed that *their services are offered at least also in the public interest*, since ensur-

ing the usage of important parts of the traffic and transportation network without risks is the target at stake. Eventually, the required state *entrusting act* unequivocally exists in the shape of *Maritime Pilots Act*, too.

Consequently, there remains the difficult task to clarify whether the introduction of a monopoly and the there from following intensive regulation of professional exercise of maritime pilots for an optimal task fulfilment are indispensably necessary. This question may only be answered taking into account the complete spectrum of tasks and economic as well as legal set-ups governing the exercise of the profession.

For the time being, the following aspects may be enumerated as *significant features of maritime pilots services*:

- availability and readiness at 365 days,
- non-discriminatory obligation to contract,
- high professional standards due to continuing professional education,
- economic and professional independence,
- excellent knowledge of localities and infrastructure,
- comparatively low pilot charges per nautical mile.

These features - without doubt - constitute indications for an especially high operating effectiveness. Yet, this alone does *not* suffice for justifying the elimination of competition. *Rather*, it has to be shown that these standards are *indispensable* and that they may *not be realised without erecting a monopoly*.

### III. **Indispensability of performance standards**

The indispensability of the described standards reveals from different viewpoints:

Firstly, the full-time service is owed to the flow of work in modern seaports and, therewith, externally stipulated.

Secondly, the obligation to contract is a consequence of the ships' dependence upon mari-

time pilots services, which itself is laid down by statute.

Thirdly, high professional standards, which are safeguarded through continuing professional education, have always constituted an integrated part of the professional law of maritime pilots. They are required because of the risks that are combined with this demanding profession.

Additionally, the economic and professional independence of maritime pilots primarily aims to protect from dumping and the risks of neglect of security and quality standards linked to this. It should be excluded that the quality of work is neglected because of *too* low prices or that customers are *discriminated against*. This is a general feature of the liberal professions that – unlike other characteristics – is still unreservedly accepted today.

Finally, likewise proverbial is the excellent knowledge of localities and infrastructure of the waters and ports that each maritime pilot has to have.

Concerning this aspect, already Mark Twain in his book “Life on the Mississippi” explains:

„First of all, there is one faculty which a pilot must incessantly cultivate until he has brought it to absolute perfection. Nothing short of perfection will do. That faculty is memory. He cannot stop with merely thinking a thing is so and so; he must know it; for this is eminently one of the 'exact' sciences.“

This is one aspect of the high professional standards. But, – from the perspective of locality knowledge – this aspect is also linked to the additional aspect that only a continuous activity in a sector guarantees the realization of high professional standards. Consequently, this aspect argues in particular for the erection of a local monopoly.

If maritime pilots services should be provided around the clock without danger and discrimination, the requirements laid down in the statute are indispensable.

For this reason, the issue arises *whether the pursued targets may be reached also without a monopoly* and, hence, without competition restrictions. This is the determining test, which – applying the standards as set out by Article 86 paragraph 2 of the EC-Treaty – the provisions of the Maritime Pilots Act have to pass.

#### IV. Existence of a market failure

##### 1. Theoretical reflections

The economic theory is very keen on justifying derogations from the competition principle with the argument of *market failure*. This is based on the consideration that market processes characterised by free competition are normally in the best position to provide optimal services for good tariffs.

Derogations from the competition principle are primarily accepted if a so-called *natural monopoly* exists or the *provision of public goods* is at stake. In the latter case the state has a legitimate interest to establish the conditions for the provision of services for social or democratic reasons.

A natural monopoly is considered to exist if the provision of a service by *only one* supplier is cheaper. For example, this is the case with train, street and energy or even other networks.

For a long time the infrastructure in seaports and airports has predominantly been regarded to constitute a natural monopoly.

*However*, the developments in connection with airports has illustrated that at least with some of these services a *cautious* loosening is possible. Nowadays, due to the influences of European law one mostly comes across two competing providers for several ground services at airports.

Another model of the European Commission, which has also been incorporated into the port package II directive, planned the *introduction of a regular tender of monopolised services*. In this way, at least a durable control by only one provider is prevented.

Hence, the question arises *whether maritime pilots services* have to be qualified as a *natural monopoly* or whether the introduction of a *tender and concession model* needs to be taken into account for them, too.

Many arguments are put forward against a more or less far-reaching liberalisation in the case of maritime pilots services. These do not concern ownership protection, but the safeguarding of quality and efficiency standards. In the following part of my speech, I would like to show this. I apologise that because of the limited time I cannot possibly take into consideration all arguments.

## 2. *Disadvantages of the tender model*

A minimum model for the introduction of competition with maritime pilots services in seaports could be introduced insofar that the provision of maritime pilots services is tendered for a period of time, for example, let us say for five years. What would be the consequences of such a measure?

The *primary aim* of a tender would be to *reduce costs*.

The costs of the German maritime pilots services system are at a comparably *moderate* level.

A tender would require a privatization. *For this*, a new state regulatory and control system would have to be established. The extensive regulatory administration in the sectors of post, telecommunication and energy illustrates the enormous costs that this would necessitate and the difficulties that would arise in connection with the control process. These costs would have to be added to the pure service costs.

*In the first place*, the issue of professional education would occur to service providers. Maritime pilots, who so far have been organised as liberal profession in their professional organisations (Lotsenbrüderschaften), would have to re-organise themselves. This requires certain incentives, which would be combined with considerable capital expenditures. *As a con-*

*sequence*, the incentive would grow to educate cheaper professionals from other sectors.

Presumably, supra-regional organisational forms would evolve. The attachment to the area – so important for maritime pilots – would be loosened or even get lost. Therewith, *quality losses* would occur.

Because of the parallel availability of capacities, which would be indispensable for applications, problematic *economic constraints* would have to be expected, which would affect professional standards and economic independence of pilots.

*Altogether*, considerable cut backs on central quality features would be combined with the transition to a tender model. *Moreover*, a higher financial burden seems to be likely in this case, whereby the shifting of costs for the control tasks in the tax-financed area must not be forgotten in the overall consideration. In comparison with the currently approached solution a loss in financial fairness would be the consequence.

## 3. *Endangering of task fulfilment?*

Let us return to the justification reasons of Article 86 paragraph 2 EC and clarify whether it is necessary to monopolise maritime pilots services in order to perform the public interest functions combined with these.

As the analysis of the alternative models has shown, the transition from a normal competition of services with many competing providers is excluded already in advance. *To this extent*, the assumption of the existence of a natural monopoly still proves to be correct. This is at least the case *as long as* one qualifies the high professional standards as indispensable for safe sea traffic. This needs to be regarded as being the case because, despite of all technical progress, the considerable competition between shipping companies makes a drop of quality and security standards obvious again and again. For this reason, the model of self-dispatch is *not* applicable at all.

What is more, even a concession model on the basis of a regular tender would bring along organisational additional strains, which would not lead to lower costs without quality losses. The public interest in high security standards argues for the maintenance of our current public-law self-administration model.

Eventually, considerable changes for the maritime pilots professions would be required under the alternative model, which would *not* set *any* incentives to enhance quality and efficiency at all.

*Altogether*, therefore, the decision of a Member State for a public-law control and monopolisation of maritime pilots services in seaports has to be regarded as *compatible* with Article 86 paragraph 2 EC.

#### **V. Summary and conclusions: professional law and self-regulation of maritime pilots as guarantee of high professional standards**

Before the background of these findings, in the concluding part of my speech I would like to draw your attention *once again* to the German regulatory model for maritime pilots services and highlight the *advantages* combined with this.

The organisational form orientated towards the model of functional self-regulation of the German maritime pilots *combines* independent organisational responsibility with state-relieving effects. Among other things, it is based on the idea of honorary posts. This notion has a long and fruitful tradition in Germany.

Being a liberal profession, maritime pilots – due to the profession's self-image – aim at ensuring high professional and ethical standards by means of manifold legal and professional ethical instruments. For many years, this combination of a formal *legal* and an informal *ethical* control in other sectors (concerning undertakings and state alike) has been assessed as exemplarily and striven for. *Here*, although not under an English-named role model of "governance", it has been realised under the roof of old German expressions.

At the same time, the Maritime Pilots Act realises a modern concept of being *closely linked to the citizens* like the European Union is continuously demanding it. *Now*, it is time that also the arms of the competition approach the specific combination of public-law organisational form and self-administration from the perspective of efficiency and do *not only* endeavour to promote competition *whatever happens* in all areas of life.

*In addition*, the German model combines professional exercise with solidarity elements of supply in the professional group and, in this way, makes the basic ideas of the social constitutional principles perceptible in a way that has *not* been the case at the entire state level of social security systems for a long time.

*Eventually*, the thin organisational structures have to be mentioned, which bears *every* comparison with economic undertakings and embarrasses every state administration.

Finally, the *moderate* pilot charges per nautical mile prove that here a high degree of operating effectiveness is reached.

The conclusions of my reflections are, therefore, clear and unequivocally: In view of performance standards as well as with efficiency in mind, there is *no* reason to fundamentally change the legal and economic framework for maritime pilots services in German and European seaports. Profession and professional organisation possess a high degree of operating effectiveness. Whoever criticises these findings as being just an attempt to protect ownership is *sincerely* invited to a more detailed consideration and evaluation.