

Northwestern Journal of International Law & Business

Volume 24

Issue 3 *Spring*

Spring 2004

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Recommended Citation

Alessandra Fratini, Andrea Carta, Chronopost v. Ufex: The Paradox of the Competing Monopolist Symposium on European Competition Law, 24 Nw. J. Int'l L. & Bus. 773 (2003-2004)

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Chronopost v. Ufex: The Paradox of the Competing Monopolist

Alessandra Fratini & Andrea Carta*

I. INTRODUCTION

On July 3, 2003, in the *Chronopost* judgment,¹ the European Court of Justice (“ECJ” or “the Court”) defined the conditions under which a public undertaking, enjoying a legal monopoly for the provision of services of general interest, can provide services to its subsidiaries without infringing Article 87(1) of the EC Treaty.² The impact of this judgment on European Community (“EC”) state aid policy and public services is potentially large, in both legal and practical terms. The ruling casts light on the real dilemma underlying the application of state aid rules to the circumstances of the case: how to allow public companies, entrusted with a network enabling them to provide a given service to all users, to operate in competitive markets while, at the same time, preventing these public operators from unduly exploiting the specific advantages of their position as network operators, in terms of economies of scale/scope, on the downstream competitive markets.

This article deals with the principles defined by the ECJ in the *Chronopost* ruling. The Part II presents the history and background of the judgment, with a short overview of the various aspects of the legal dispute, which the July 2003 ruling brought to an end. The Part III includes some comments on the judgment, and tries to assess the potential consequences

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¹ Joined Cases 83/01, 93/01 & 94/01 P, *Chronopost v. Ufex* (July 3, 2003) at <http://curia.eu.int/en/index.htm>.

² Article 87 (1) of the EC Treaty states: “Save as otherwise provided in this Treaty, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the common market.” CONSOLIDATED VERSION OF THE TREATY ESTABLISHING THE EUROPEAN COMMUNITY, Dec. 24, 2002, O.J. (C 325) 67 (2002) [hereinafter EC TREATY].

of the Court's reasoning in legal terms. Finally, the *Chronopost* ruling is read in the context of the broader political debate taking place across the European Community regarding services of general economic interest ("SGEIs").³

II. HISTORY AND BACKGROUND: FROM *SFEI* TO *CHRONOPOST*

A. The *SFEI* Judgment

The ruling of the ECJ in *Chronopost* represents the final outcome of a lengthy dispute that started as early as December 1990. Litigation began when the French association of international express couriers ("SFEI") filed a complaint with the Commission claiming, essentially, that the logistical and commercial assistance afforded by the French Post Office ("La Poste") to its affiliated company providing express courier services (at the time "SFMI," subsequently renamed "SFMI-Chronopost") constituted illegal state aid within the meaning of Article 87 (1) of the EC Treaty, as access to La Poste's network was granted at more advantageous terms than those available on the market.

The Commission decided to take no action on the complaint under Article 87 of the EC Treaty.⁴ On June 16, 1993, SFEI filed suit against La Poste and Chronopost before the national judge, claiming that La Poste's assistance to Chronopost was in breach of Article 87 (1) of the EC Treaty and any unlawful state aid was to be repaid to La Poste. The Paris Commercial Court (*Tribunal de Commerce*) referred a number of questions on the interpretation of Articles 87 and 88 of the EC Treaty to the ECJ for a preliminary ruling, pursuant to Article 234 of the EC Treaty. It asked, *inter alia*, whether measures adopted by the French Post Office, consisting of the

³ While the E.C. institutions have repeatedly highlighted the importance of SGEIs (*See, e.g.*, Communication from the Commission on Services of General Interest in Europe, 2001 O.J. (C 17) 4; Report to the Laeken European Council on Services of General Interest, COM(01)598 final; Communication from the Commission on Services of General Interest in Europe, 1996 O.J. (C 281) 3), the underlying concept is yet to be clarified. In general, it corresponds to the more generic concept of public service and encompasses the notion of universal service. In this regard, the case law itself is not very precise and indistinctly refers to services of general interest, universal services, public services or services of public interest. However, the exact scope of these notions is not relevant for the purpose of this article. We will indistinctly refer to SGEIs, public services, etc. For a more accurate definition of those concepts, see Green Paper on Services of General Interest, COM(03)270 final, at 6-7, available at <http://europa.eu.int/eur-lex/en/com/gpr/2003/com20030270en01.pdf>.

⁴ The Commission notified SFEI of its decision by letter of March 10, 1992. SFEI lodged an action with the ECJ for annulment of that decision. *See* Case 222/92, *SFEI v. Commission* (1992) (unreported). By its order of November 18, 1992, the Court ruled that it was not necessary to proceed to judgment, in the light of the subsequent Commission Decision of July 9, 1992, to withdraw the decision of March 10, 1992. *See infra* Part 2.2.

grant of logistical and commercial assistance to its controlled express courier operator, were to be regarded as state aid within the meaning of Article 87 (1) of the EC Treaty, where no normal payment was fixed in return.⁵

In its ruling given on July 11, 1996, the ECJ defined the fundamental principle that has given rise to a great deal of debate, both in jurisprudence and legal literature.⁶ The ECJ held that, “[i]n order to determine whether a State measure constitutes aid, it is necessary to establish whether the recipient undertaking receives an economic advantage which it would not have obtained under normal market conditions.”⁷ However, the Court left it up to the national court to decide what was to be considered the “normal” remuneration for the services in question.

In essence, the ECJ established the principle by affirming that “[s]uch a determination presupposes an economic analysis taking into account all the factors which an undertaking acting under normal market conditions should have taken into consideration when fixing the remuneration for the services provided,”⁸ but it did not enumerate the factors.⁹ Shaping the economic content of this principle was meant to be the task of the Commission, the Court of First Instance, and finally, the ECJ in the following episodes of the *Chronopost* saga.

B. The Commission Decision 98/365/EC

After the action against La Poste and Chronopost was lodged before the French judge, the Commission decided to withdraw its earlier decision of March 10, 1992, and reopen the case, pursuant to Article 88 (2) of the EC Treaty. The Commission adopted its Decision on October 1, 1997 with respect to the assistance provided by the French Post Office to Chronopost over the period 1986-91.¹⁰

⁵ Case 39/94, *SFEI v. La Poste*, 1996 E.C.R. I-3547, I-3583-84.

⁶ For comments on the SFEI judgment see Giuseppe B. Abbamonte, *Competitors' Rights to Challenge Illegally Granted Aid and the Problem of Conflicting Decisions in the Field of Competition Law*, 18 EUR. COMPETITION L. REV. 87 (1997); Marie-Angèle Hermitte et al., *Chronique de Jurisprudence du Tribunal et de la Cour de Justice des Communautés Européennes* [*Chronicle of the Tribunal and the Court of the European Communities*], 124 J. DU DROIT INT'L 479, 609 (1997); Michel L. Struys, *SFEI—A Missed Opportunity*, 6 IRIS J. EUR. L. 181, 181-89 (1997).

⁷ *SFEI*, 1996 E.C.R. at I-3596 (emphasis added).

⁸ *Id.*

⁹ It is worth noting that, in his Opinion, the Advocate General suggested that the following were to be taken into consideration: “the cost of providing the assistance, the size of its investment in the undertaking and its return from it, the importance of the activity of the undertaking to the investing group as a whole, conditions on the market in question and the period for which the assistance is granted.” *Id.* at I-3568.

¹⁰ See Commission Decision 98/365/EC of 1 October 1997 Concerning Alleged State Aid

In the framework of these proceedings, the parties advanced two different approaches to the criteria to be used for the purpose of identifying “normal market conditions” within the meaning of the *SFEI* ruling.

According to SFEI, in defining the normal price for the logistic and commercial assistance provided to Chronopost, the economies of scale enjoyed by La Poste by virtue of its monopolistic position should have been taken into account, “since those economies were precisely the root-cause of the distortion in competition.”¹¹ SFEI maintained that the costs that an undertaking would have incurred, in setting up and operating a network similar to that used by La Poste, should have been considered in order to calculate the costs of the main components of the logistical assistance. It also submitted that the Commission should have examined whether, for the logistical and commercial services provided by the French Post Office, Chronopost had paid the “normal market price,” i.e., “the price at which a comparable private company would provide the same services to an unrelated company.”¹² That price should have included a fee for access to the postal network. The complainants also suggested that, in order to comply with the principle defined by the ECJ, “the Commission should [have] disregard[ed] the group’s strategic interests and the economies of scale arising from the privileged access of [Chronopost] to [La Poste’s] network and infrastructure.”¹³ According to SFEI, such considerations were not “taken into account . . . because the Post Office ha[d] a monopoly.”¹⁴ Chronopost should have borne “the costs that a private undertaking would [have incurred] in creating a network equivalent to that of the Post Office.”¹⁵

The Commission carried out its own analysis on the economics of the provision of logistical and commercial services, and acknowledged that the price paid by Chronopost to La Poste was higher than the total operating costs incurred by the latter for the provision of logistical assistance.¹⁶ Further, it recognized that fixed costs were allocated in proportion to the business carried out by La Poste on behalf of the subsidiary, and thus agreed with the French authorities that the remuneration paid by Chronopost was sufficient to cover the marketing cost incurred by the incumbent.¹⁷ The Commission also rejected the complainants’ argument

Granted by France to SFMI-Chronopost, 1998 O.J. (L 164) 37.

¹¹ *Id.* at 41.

¹² *Id.* at 44-45 (emphasis added).

¹³ *Id.* at 45.

¹⁴ *Id.*

¹⁵ *Id.*

¹⁶ *Id.* at 43.

¹⁷ *Id.* (arguing that “[m]arketing and commercial costs are included among the operating costs”).

that the costs of setting up the network should have been taken into account.¹⁸ In this respect, it underlined that, in making any comparison between the French Post Office and other express courier operators, it is necessary to consider the different cost structure of the publicly owned company.¹⁹

Next, and more importantly, the Commission dismissed the complainants' interpretation of the ECJ ruling in *SFEI* and stated its view on the definition of "normal market conditions." It read the judgment as saying that, in order to establish whether state aid was involved in a transaction between two undertakings of a state-owned group, it is necessary to verify whether the parent company had received the normal consideration in return for the services provided to the subsidiary.²⁰ Accordingly, it considered that "internal prices at which products and services are transacted between companies belonging to the same group do not involve any financial advantage whatsoever if they are full-cost prices (total costs plus a mark-up to remunerate equity capital investment)."²¹

After examining the economic relationship between La Poste and Chronopost, the Commission concluded that logistical and commercial assistance had been provided against full-cost coverage, thus under "normal market conditions."²² The Commission concluded that such assistance did not constitute state aid.²³

C. The Annulment Action before the Court of First Instance

SFEI, which had in the meantime become Union Francaise de l'Express ("UFEX"), responded by bringing an action for the annulment of the Commission's decision before the Court of First Instance ("CFI").²⁴ Chronopost, La Poste, and the French Republic intervened in support of the Commission.

The applicants claimed that the Commission had misinterpreted the *SFEI* judgment and assessed the existence of state aid on the basis of incorrect methods. They argued that the Commission should have taken into account the fact that the monopoly holder operates outside "normal market conditions" and thus would not necessarily pass all the costs incurred for services rendered on to its subsidiary. More specifically, according to UFEX, an undertaking operating in "normal market

¹⁸ *Id.* at 43-44.

¹⁹ *Id.* at 44.

²⁰ *Id.* at 45.

²¹ *Id.*

²² *Id.*

²³ *Id.*

²⁴ Case T-613/97, *Ufex and Others v. Commission*, 2000 E.C.R. II-4055. [hereinafter *Ufex*]

conditions” would have had to bear, and pass onto its subsidiary, the network costs and include these in the price for assistance provided.²⁵ The applicants further observed that the normal remuneration for the services provided by La Poste to Chronopost should have included the long-term marginal costs as well as the fixed costs of acquiring and maintaining infrastructure in the form of buildings, equipment, and staff.²⁶ The long-term marginal costs borne by La Poste thus allegedly constituted cross-subsidies to the benefit of Chronopost. Under this line of reasoning, the remuneration that La Poste was to claim from its subsidiary should have been calculated on the basis of the price that a private company would have had to pay, in normal competitive conditions, for equivalent logistical and commercial support.²⁷

The Commission replied that cross-subsidization within a public group does not always constitute state aid.²⁸ On the contrary, it may be part of a long-term strategy which will benefit the group as a whole. The Commission also stated that a monopoly undertaking could always conclude “balanced bilateral contracts,”²⁹ and that no prejudice should have derived from the particular nature of the parent company’s activities. In this respect, the analysis carried out by the Commission showed that the subsidiary paid more than the coverage of full costs. As for the critical issue regarding the economies of scale and scope connected with the management of a monopolistic network, the Commission stated that synergies and strategic considerations within a group could not, as such, be considered as incompatible with Article 87 (1) of the EC Treaty, provided that all costs were taken into account when calculating the remuneration for services rendered. The Commission recalled the EC law principle of neutrality with regards to systems of property ownership in the member states and the principle of equal treatment of publicly owned and private undertakings (Article 295 of the EC Treaty).³⁰ These principles imply that member states are allowed to carry out economic activities and to make investments according to a strategy corresponding to that of a private investor. Such activities would not, per se, entail state aid.³¹

With its judgment on January 14, 2000, the CFI endorsed the

²⁵ *Id.* at para. 44.

²⁶ *Id.* at para. 42. The applicants contended that the Commission’s guidelines on the application of the EEC competition rules in the telecommunications sector, 1991 O.J. (C 233) 2, set out the Commission’s position with regard to cross-subsidies.

²⁷ *Id.* at para. 44.

²⁸ *Id.* at para. 51.

²⁹ *Id.* at para. 52.

³⁰ According to Article 295 of the EC Treaty, the Treaty “shall in no way prejudice the rules in Member States governing the system of property ownership.” EC TREATY, *supra* note 2, art. 295.

³¹ *Ufex*, *supra* note 24.

applicants' arguments and annulled the Commission's Decision. First, the CFI pointed out that the mere fact that the subsidiary paid the full costs incurred by French Post Office was not in itself sufficient to show that no aid, within the meaning of Article 87 (1) of the EC Treaty, had been granted.³² Instead, the CFI took the view that the Commission "should at least have checked that the payment received in return by La Poste was comparable to that demanded by a private holding company or a private group of undertakings not operating in a reserved sector, pursuing a structural policy—whether general or sectorial—and guided by long-term prospects," and that

by ruling out the very existence of state aid without checking whether the remuneration received by La Poste for the provision of commercial and logistical assistance to SFMI-Chronopost corresponded to the price that would have been asked under normal market conditions, the Commission based its decision on an incorrect interpretation of Article 92 [now 87] of the EC Treaty.³³

The case before the CFI presented two possible approaches to defining "normal market conditions." The Commission's first approach interprets the ECJ ruling in *SFEI* as saying that, in order to be compatible with Article 87 (1) of the EC Treaty, the price of services provided by a public undertaking operating a monopoly must cover the total costs that are incurred by the holding company when providing the services (the "*cost-based approach*").³⁴ According to the second approach, endorsed by the CFI, "normal market conditions" should be established with regard to the price that a firm not operating a public network would have charged for the provision of the services in question (the "*market-price approach*").³⁵ While in the first case "normal market conditions" are defined from the provider's perspective, in the second case these are defined from the point of view of the recipient.³⁶

³² *Id.* at para. 74.

³³ *Id.* at para. 75.

³⁴ *Id.* at para. 72.

³⁵ *Id.* at para. 75. (*emphasis added*).

³⁶ It is settled case law that the existence of state aid should be assessed taking into consideration the effects of the transfer of resources might have on the market. See Case 173/73, *Italy v. Commission*, 1974 E.C.R. 709, ¶ 13. Consistent with this approach, the recipient's point of view is crucial because it can verify the existence of an advantage can be verified. For a general overview of E.C. state aid law, see, *generally*, ANDREA BIONDI, PIET ECKHOUT & JAMES FLYNN, *THE LAW OF STATE IN THE EUROPEAN UNION* (Oxford University Press 2003); CONOR QUIGLEY & ANTHONY M. COLLINS, *EC STATE AID LAW AND POLICY* (Hart Publishing 2003); LEIGH HANCHER, TOM OTTENVANGER & PIETER J. SLOT, *EC STATE AIDS* (Sweet & Maxwell 1999); ANDREW EVANS, *EUROPEAN COMMUNITY LAW OF STATE AID* (Oxford European Community Law Series 1997).

D. The ECJ's Consideration of *Chronopost*

Chronopost, La Poste, and the French Republic brought an appeal against the judgment of the CFI before the ECJ.³⁷ Once more the Community judge was called upon to give an opinion on the facts that had been at the root of the *SFEI* case. This time, however, the Court simply could not reiterate a statement of principle. It was obliged to explain—in more precise terms - how the notion of “normal market conditions” was to be applied to the provision of services from a public undertaking, operating a public network for the provision of the universal postal service, to a subsidiary operating in the competitive market of express delivery services.

The Court was faced with the choice between the Commission's cost-based approach and the market-price approach supported by the CFI, which required showing, for state aid to be excluded, that the transactions concerned would be comparable to those taking place between undertakings operating in “normal market conditions.” Following the conclusions of the Advocate General,³⁸ which particularly focused on the status of public firms entrusted with the provision of services of general interest, the ECJ endorsed the Commission's approach.

The Court's reasoning was that the CFI unduly failed to take account of the fact that an undertaking such as a public postal operator is in a situation “that is very different from that of a private undertaking acting under normal market conditions.”³⁹ In order to provide the universal postal service, the ECJ explained, the French post office had to create and maintain a network whose characteristics “are not in line with a purely commercial approach” and that, therefore, “would have never been created by a private undertaking.”⁴⁰ The ECJ went further and recognized that the public postal network had no equivalent on the market and none of Chronopost's competitors had ever requested access to La Poste's network. Hence, the solution to the point at issue was to assess “normal market conditions,” “which are necessarily hypothetical,” by reference to “the objective and verifiable elements which are available.”⁴¹ In the absence of a benchmark, which would allow for the amount charged to Chronopost being checked against the price this undertaking would have paid on the market for the same services, the Court concluded that the cost borne by the public operator represented such objective and verifiable elements. By so

³⁷ See *Chronopost*, at <http://curia.eu.int/en/index.htm>.

³⁸ Joined Cases 83/01, 93/01 & 94/01 P, *Chronopost v. Ufex* (Dec. 12, 2002), at <http://curia.eu.int/jurisp/cgi-bin/form.pl?lang=en&Submit=Submit&docrequire=alldocs&numaff=C-83%2F01+P&datefs=&datefe=&nomusuel=&domaine=&mts=&resmax=100> (Opinion of Advocate General Tizzano).

³⁹ *Chronopost*, at <http://curia.eu.int/en/index.htm>.

⁴⁰ *Id.* at para. 36.

⁴¹ *Id.* at para. 38.

doing, the ECJ espoused the provider's perspective endorsed by the Commission.

On this point, the Opinion of the Advocate General played a crucial role in the Court's decision. In fact, the Advocate General argued that the market did not offer specific and objective references and therefore the assessment of La Poste's behavior ran the risk of being excessively hypothetical and abstract.⁴² Consequently, the Advocate General suggested considering the costs borne by La Poste as the only parameter necessary to assess the existence of state aid.⁴³ The Advocate General accepted that, alternatively, reference could have been made to the market economy investor principle ("M.E.I.P."); however, the cost coverage test offered more guarantees.⁴⁴ The Advocate General pointed out that reference to the M.E.I.P. would not have been sufficient to exclude elements of state aid in the remuneration required to Chronopost. In fact, a private holding company in the same position as La Poste could decide, pursuing a long term commercial strategy, not to pass all costs onto its subsidiary in order to enhance its ability to compete and to maximize the profits.⁴⁵ If authorized to allocate the costs in this way, La Poste "could give the subsidiary the exclusive advantage of all the economies of scale arising from the use of a postal network already established for the provision of a universal service, in order to increase its profits and thus the profits of the group as a whole,"

⁴² The Advocate General concluded that the prices charged by La Poste could not be compared with those of other companies, taking into account the universal service obligation to which La Poste has to comply. Furthermore, none of Chronopost's competitors had ever sought to have access to La Poste's network (this made it impossible to verify whether they would have been ready to pay the price required by the French Post Office for logistical and commercial assistance).

⁴³ It should be noted, however, that the Commission, in its state aid practice, has frequently referred to experts' studies and simulations in order to assess the behavior of state owned companies, especially in cases where the market economy investor principle was a core issue.

⁴⁴ The M.E.I.P. refers to the behavior of a private market investor as a benchmark for the assessment of the behavior of the state in the market. The application of the M.E.I.P. to the transaction between La Poste and Chronopost would have implied checking "whether a commercial investor would be satisfied with the level of consideration received" for the provision of services. See Joined Cases 83/01, 93/01 & 94/01 P, *Chronopost v. Ufex*, para. 52 (Dec. 12, 2002) at <http://curia.eu.int./jurisp/cgi-bin/form.pl?lang=en&Submit=Submit&docrequire=alldocs&numaff=C-83%2F01+P&datefs=&datefe=&nomusuel=&domaine=&mots=&resmax=100> (Opinion of Advocate General Tizzano)..

⁴⁵ *Id.* at para. 52. He explained that:

[A] private undertaking in the same position as La Poste would have to fix the amount of the remuneration so as to maximize the profits for the group as a whole, allowing naturally for the profits distributed by the subsidiary operating in the express delivery sector. Such an undertaking might therefore be satisfied with a lower return in pursuit of a general strategy designed to strengthen the subsidiary's competitive position in the express delivery market.

thus gaining a relevant competitive advantage over other express courier operators that had no access to a public postal network.⁴⁶

The Court, however, defined more accurately the conditions under which pricing for the services of a public network operator constitute "normal market conditions."⁴⁷ In particular, it explicitly included the costs of the network among those to be allocated to the subsidiary for fixing the price in return for the services rendered. It follows, in the Court's view, that the existence of unlawful subsidies can be excluded once it is verified that the undertaking operating on a competitive market has paid an appropriate price. Such a price must be sufficient to cover: (1) all the additional variable costs in which the public holding company incurs in providing the logistical and commercial assistance; (2) an appropriate contribution to the fixed costs arising from the use of the postal network, and (3) an adequate return on the capital investment insofar as it is used to finance the competitive activity.⁴⁸ These three conditions are sufficient to exclude the existence of any state aid as long as the costs have not been underestimated or fixed in an arbitrary fashion.⁴⁹ Accordingly, the ECJ annulled the ruling of the CFI and affirmed the Commission's 1997 decision.

III. COMMENTS ON THE *CHRONOPOST* RULING

A. One Step Forward: A Clearer Legal Framework for Public Intervention on the Market

With *Chronopost*, the ECJ had the final say on a very critical issue, the importance of which goes well beyond the specific facts raised in the case. The judgment confers greater legal certainty in applying state aid rules to companies operating in both reserved and competitive sectors.

The EC's process of gradual liberalization of public utility sectors, together with the need to ensure the provision of SGEIs, resulted in a dichotomy between reserved sectors, generally operated by former public incumbents, and sectors open to competition. Under these circumstances, the effective operation of an internal market based on undistorted competition requires that the relations between undertakings operating on both reserved and competitive markets be transparent and clear. In

⁴⁶ Joined Cases 83/01, 93/01 & 94/01 P, *Chronopost v. Ufex*, para. 51 (Dec. 12, 2002), available at <http://curia.eu.int./jurisp/cgi-bin/form.pl?lang=en&Submit=Submit&docrequire=alldocs&numaff=C-83%2F01+P&datefs=&datefe=&nomusuel=&domaine=&mots=&resmax=100> (Opinion of Advocate General Tizzano).

⁴⁷ Joined Cases 83/01, 93/01 & 94/01 P, *Chronopost v. Ufex*, para. 47 (July 3, 2003), available at <http://curia.eu.int/en/index.htm>.

⁴⁸ *Id.*

⁴⁹ *Id.*

addition, the operator of a public service network should not be allowed to take advantage of its position on the reserved market to gain undue competitive advantages in markets open to competition. At the same time, a state-owned undertaking must be able to pursue a genuine commercial strategy, organize its economic activities as a private company would, and gain access to competitive markets.⁵⁰ This is not only accepted under the EC law principle of neutrality,⁵¹ but is also highly desirable; it allows for public services to be financed through revenues gained in competitive markets, thus enhancing the efficiency of public network industries.

Against this background, the ECJ's judgment in *Chronopost* can be regarded as a significant contribution. It defines the criteria needed to assess the relations between activities carried out in the reserved sector and those subject to competition. With *Chronopost*, the Court added some eagerly awaited guidelines to its previous ruling in the *SFEI* case, which had left both national authorities and the Commission with too much discretion in defining "normal market conditions." It recognized the validity of a straightforward and clear method to verify whether the transfer of resources and the provision of services between firms like La Poste and Chronopost entail undue cross-subsidies.

By requiring that variable costs and network costs (plus a return on the invested capital) both be covered, the Court has excluded the recourse to external parameters—such as pricing practices of other firms—for the purposes of assessing the consistency of intra-group transactions with EC state aid rules. The indication of cost-coverage as a sufficient condition to exclude the application of Article 87 (1) of the EC Treaty to cases such as *Chronopost* can be welcomed as a significant step towards legal predictability. It is now established under EC law that a state-owned company is free to pursue its strategic goals, including the promotion of its subsidiaries vis-à-vis their competitors. However, economies of scale deriving from the use of a public network, conceived for the provision of SGEIs, cannot be entirely transferred onto activities performed in neighboring markets. Indeed, the price paid for access to the network must cover part of the costs of the network itself as well as a return on the capital invested on it.

Therefore, with the *Chronopost* ruling, the Court has set a bright-line standard, and compliance with this standard can be easily monitored by the Commission and made subject to judicial control. However, some questions still remain. In particular, to what extent is it still possible to refer to "normal market conditions?" Is the cost-based approach sufficient to guarantee that competition is not unduly distorted?

⁵⁰ Commission Decision 2002/149/CE, SNCM, 2002 O.J. (L 50) 66, at para. 114.

⁵¹ See, EC TREATY, *supra* note 2, at art. 295.

B. Two Steps Back: A “Competing Monopolist”?

As noted above, the ECJ was called upon to make a clear-cut choice between two divergent interpretations of the *SFEI* ruling, which in fact correspond to a precise policy choice. On the one hand, the CFI tried to ensure that the use of a public network would not affect the conditions of competition on downstream markets, and notably that the state-owned operator would not derive any undue benefit from the economies of scale of the network itself. It could be reasonably argued that access to such a unique infrastructure was *per se* a relevant competitive advantage. The ECJ and the Commission, on the other hand, chose to focus on the question of cost coverage, assessing La Poste and Chronopost’s relationship from the provider’s perspective, and avoided addressing the issue of the transference of scale economies from the reserved sector to the market.

In its reasoning, the ECJ did not dwell on an economic assessment of the consequences deriving from the use of one method instead of the other. Nor did the Court acknowledge how different the approaches are between the Commission and the CFI, if one takes into account the necessity of maintaining a sound level of competition on the market. Instead, the ECJ insisted on the necessity of carrying out an analysis based on “objective and verifiable elements,” i.e. the costs for the provision of the services rendered.⁵² As a result, while it might appear to be a clarification of the principle defined in *SFEI*, the ruling in *Chronopost* rather constitutes a clear departure from the “normal market conditions” test. In fact, the ECJ maintained that no benchmark existed in order to compare the situation of La Poste with that of a private group of undertakings.⁵³ Therefore, the notion of “normal market conditions” had become purely hypothetical and was to be assessed not against a “normal market” operator, but against the monopolist itself.

While the ECJ made clear that its criteria were chosen to ensure the highest possible level of legal certainty, the Court’s reasons for defining costs borne by a monopolist as “normal market conditions” are somewhat obscure. The ECJ has asserted that it is impossible to compare a public monopolist with a private operator, underlining the fact that the creation and maintenance of its network are not in line with a purely commercial approach.⁵⁴ It went even further by saying that a private undertaking would have never created a network such as that operated by La Poste. On this basis, it is not clear how the costs of this network can then turn into “normal market conditions” for the purposes of the application of Article 87 of the EC Treaty. It could be argued that, with the *Chronopost* ruling, the ECJ has

⁵²*Chronopost*, *supra* note 1 at para. 39, available at <http://curia.eu.int/en/index.htm>.

⁵³ *Id.* at para. 38.

⁵⁴ *Id.* at para. 36.

shaped a paradoxical profile of a “competing monopolist.”

It follows from the Court’s ruling that a monopolist’s intervention in competitive markets, whereby the benefits of its unique cost structure and economies of scale and scope are transferred to its subsidiaries, does not raise competition concerns, provided that the costs allocated to the competing subsidiary have not been underestimated or fixed in arbitrary fashion.⁵⁵ In this respect, any interested party remains able to detect and challenge abusive cross-subsidization practices enacted through an incorrect allocation of the costs.

The conclusion reached by the Court appears even more paradoxical once the *Chronopost* ruling is compared with the recent judgment on the *Altmark* case, which was pronounced three weeks later.⁵⁶ In *Altmark*, the ECJ was asked to clarify whether the compensation granted for fulfilling a public service obligation (“PSO”) could constitute state aid and, therefore, infringe Article 87 of the EC Treaty.⁵⁷ Essentially, the Court ruled that PSO compensations do not constitute state aid as long as the following four conditions are met:

1. The recipient undertaking is actually required to discharge clearly defined public service obligations;
2. The compensation is calculated according to predetermined parameters established in an objective and transparent manner;
3. The compensation is proportionate to the cost incurred in discharging the public service obligations;
4. Where the undertaking is not chosen in a public procurement procedure, “the level of compensation needed has been determined on the basis of an analysis of the costs which a typical undertaking, well run and [...] able to meet the necessary public service requirements, would have incurred in discharging those obligations.”⁵⁸

It could be argued that the fourth condition set out by the Court cannot be easily reconciled with the principle defined in *Chronopost*. It is unclear how national judges, or the Commission itself, can establish the correctness of the level of compensation on the basis of the comparison with a “typical undertaking.” As noted *supra*, the Court in *Chronopost* has said that, at least in certain cases, public services providers have a peculiar structure that

⁵⁵ *Id.* at para. 40.

⁵⁶ Case C-280/00, *Altmark Trans GmbH v. Nahverkehrsgesellschaft Altmark GmbH* (July 24, 2003), available at <http://europa.eu.int/jurisp/cgi-bin/form.pl?lang=en&Submit=Submit&docrequire=alldocs&numaff=C-280%2F00&datefs=&datefe=&nomusuel=&domaine=&mots=&resmax=100>.

⁵⁷ *Id.* at paras. 30-31.

⁵⁸ *Id.* at paras. 89-93.

has “no equivalent on the market.”⁵⁹ The Court therefore seems to have ruled out the possibility of making the comparison required in *Altmark*. It has been pointed out that one possible solution to reconcile the two rulings is that the fourth condition in the *Altmark* case should not operate in cases like *Chronopost*.⁶⁰ While this solution would allow for the application of the other three criteria in all cases, it would not be consistent with the *Altmark* ruling, since it removes the efficiency criterion, which is implied in the fourth condition thereof.

C. *Chronopost* in Context: The European Community Debate on Services of General Economic Interest

The *Chronopost* judgment can be further read in the context of the regulation of SGEIs in the European Union. In the Community legal order, both the courts⁶¹ and the regulators⁶² have contributed to the creation of a framework that both promotes competition and allows the proper funding of services of general economic interest. Such a framework embraces a view to guaranteeing their provision, which is considered as a factor of social and economic cohesion. As a result, member states are allowed under certain conditions, to compensate firms for the net additional costs incurred for the provision of a public service imposed by their public authorities. This framework is shaped to prevent the overcompensation of public service obligations, or the transfer of resources intended to cover public service costs from reserved activities to competitive ones. It is also aimed at preventing possible misallocations, whereby costs generated in the carrying out of competitive activities are shifted onto the reserved sectors. The main instruments that are used to prevent and act against anticompetitive cross-subsidizations are EC state aid rules, Transparency Directives,⁶³ and sector-specific rules regulating the universal service provision.

During the 1990s, the process of creating the internal market, the

⁵⁹ *Chronopost*, *supra* note 1 at para. 36.

⁶⁰ See A. Bartosch, *Clarification or Confusion? How to Reconcile the ECJ's Rulings in Altmark and Chronopost*, 3 EUR. ST. AID L. Q., at para. 384 (2003).

⁶¹ See, e.g., Case C-320/91, *Criminal Proceedings Against Paul Corbeau*, 1993 E.C.R. I-2533; Case T-106/95, *FFSA v. Commission*, 1997 E.C.R. II-229; Case C-157/94, *Commission v. Netherlands*, 1997 E.C.R. I-5699; Case C-266/96, *Corsica Ferries France SA v. Gruppo Antichi Ormeggiatori del Porto di Genova Coop. arl*, 1998 E.C.R. I-3949.

⁶² See, e.g., Council Directive 97/67 on Common Rules for The Development of The Internal Market of Community Postal Services and The Improvement of Quality or Service, 1998 O.J. (L 15) 14, 20; Council Regulation 2408/92 on Access for Community Air Carriers to Intra-community Air Routes, 1992 O.J. (L 240) 8, 10; Council Regulation 3577/92 Applying the Principle of Freedom to Provide Services to Maritime Transport Within Member States, 1992 O.J. (L 364) 7.

⁶³ Commission Directive 80/723, 1980 O.J. (L 195) 35, *amended by* Commission Directive 2000/52, 2000 O.J. (L 193) 75.

constraints on public finances deriving from the EMU, and technological evolution led to the progressive privatization and/or liberalization of public utilities in Europe. The opening of the markets was achieved either through Community legislation or through the action of the Commission and EC courts. Such opening challenged national monopolies through competition rules, particularly Article 86 (1) of the EC Treaty.⁶⁴ The progressive creation of a competitive environment in sectors such as post, energy, electronic communications and transport has been counterbalanced by the growing attention to the maintenance of adequate public services at all levels.

Whereas liberalizing legislation contains several provisions to limit competition, with the same aim and a view to guaranteeing the provision of universal services, the Court and the Commission have used the provision under Article 86 (2) of the EC Treaty, which allows for an exclusion of the application of competition rules.⁶⁵ Furthermore, both the Commission and the Council have issued a number of soft-law documents, restating the importance of SGEIs in the European Union.⁶⁶ Finally, SGEIs are mentioned both in Article 16 of the Treaty of Amsterdam and in Article 36 of the EU Charter of Fundamental Rights, thus establishing legal protection at the highest level of Community legal order.⁶⁷

⁶⁴ Case C-202/88, *French Republic v. Commission*, 1991 E.C.R. I-1223; Case C-179/90, *Merci Convenzionali Porto di Genova v. Siderurgica Gabrielli*, 1991 E.C.R. I-5889; Case C-41/90, *Höfner v. Macrotron*, 1991 E.C.R. I-1979; Case C-55/96, *Non-Contentious Proceedings Brought by Job Centre Coop. arl*, 1997 E.C.R. I-7119; Case C-320/91, *Criminal Proceedings Against Paul Corbeau*, 1993 E.C.R. I-2533.

⁶⁵ Article 86 (2) of the EC Treaty states that:

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 competition, in so far 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.

EC TREATY, *supra* note 2, art. 86 (2).

For reference to Article 86 (2) of the EC Treaty as a justification for State aid, *see* SNCM, *supra* note 50. *See also* Commission Decision 2001/156 on the State Aid Implemented by Spain in Favour of the Maritime Transport Sector, 2001 O.J. (L 57) 32; Commission Decision 2001/851 on the State Aid Awarded to the Tirrenia di Navigazione Shipping Company by Italy, 2001 O.J. (L 318) 9.

⁶⁶ *See* sources cited *supra* note 3.

⁶⁷ Article 16 of the EC Treaty states that:

Without prejudice to Articles 73, 86 and 87, and given the place occupied by services of general economic interest in the shared values of the Union as well as their role in promoting social and territorial cohesion, the Community and the Member States, each

It is not surprising then that, in the reasoning of *Chronopost*, the Court took account of the Universal Service Obligations binding on *La Poste*. The ECJ acknowledged that those obligations could justify the making up and the operation of the public postal network.⁶⁸ It seems to us that the Court admits, although implicitly that *La Poste*'s subsidiaries could benefit from part of the economies of scale deriving from the public network. These advantages were not to be qualified as state aid but rather as an inherent consequence of the use of a network created for a legitimate purpose, i.e., the provision of a SGEL.⁶⁹ While it is not possible to say whether the Court would have taken a different decision, had the state owned network had justifications other than the Universal Postal Service, it appears from the text of the judgment that the function of the network has played a significant political role.

IV. CONCLUSIONS

With the *Chronopost* judgment, the Court provided a welcome clarification on the relation between reserved activities and competitive activities in the context of the application of state aid rules to the network industries. In the case at issue, the Court fixed as a benchmark for evaluating the compensation for the logistical and commercial assistance the costs borne by the "monopolist."⁷⁰ In the lack of market criteria, these costs represented the only objective and verifiable elements available. What is more, given that a mere reference to the additional costs of the assistance would allow to pass the benefits of the network (scale and scope economies) onto the subsidiary, the Court not only referred to the additional variable costs incurred in providing the services at stake, but also included an appropriate contribution to the fixed costs arising from the use of the network and an adequate return on capital investment, in so far as it was used for the competitive services rendered. The reference to part of the network costs, in particular, aims at avoiding that the economies of scale resulting from the network are transferred, as such, to the competitive activities.

In this regard, *Chronopost* goes beyond the *SFEI* judgment. The latter merely refers to undetermined "normal market conditions," leaving a wide margin of appreciation as to the circumstances in which these conditions are

within their respective powers and within the scope of application of this Treaty, shall take care that such services operate on the basis of principles and conditions which enable them to fulfill their missions.

EC TREATY, *supra* note 2, art. 16.

⁶⁸ *Chronopost*, *supra* note 1 at para. 32–34.

⁶⁹ *Id.* at paras. 34–36.

⁷⁰ *Id.* at para. 39.

fulfilled. Aware of the shortcomings of the above principle, the Court adopted a new benchmark, which is far from being a specification of “normal market conditions.” The costs of the network operator on the upstream market are the costs of a monopolistic operator. It follows that, in the absence of other objective and verifiable elements, the monopoly costs represent the “normal market conditions” (hence, the *Paradox of the Competing Monopolist*).

Ultimately, using the monopolist costs might allow for more flexibility in cases where, such in *Chronopost*, companies entrusted with a SGEI grant assistance to their subsidiaries operating in competitive markets. It remains to be seen to what extent this favorable attitude of the Court will allow for a less austere application of state aid rules in the network industries.

