Joined Cases M-312/12 and M-365/12

Sepp
v
Prokuratuur

and

European Commission
v
Republic of Kapitaal

1 Kapitaal is a member state of the European Union, being one of the 2004 intake of new member states from eastern and southern Europe. For over 40 years since the war it had a centrally planned economy. The first post-independence government which held office from 1991 to 1996 took the view that Kapitaal was thus left with the legacy of 40 years of economic stagnation; and, to counter it, it embraced vigorously ordoliberal economic policies which, it is near universally accepted, led to the Kapitaalian 'economic miracle' and annual double-digit growth, which has faltered only with the onset of the 2008 economic crisis.

2 The fourth constitution of the Republic was promulgated by the interim government shortly after the 1991 elections, approved by plebiscite, and came into force in 1992. It provides in part:

Article 1
The State

'1. The Republic of Kapitaal is a democratic, capitalist and freedom loving state.

2. All State authority derives from the Kapitaalian people.

3. It is the fundamental purpose of the State to protect the rights and liberties of the people and contribute to their economic wellbeing. That wellbeing is best safeguarded and augmented by minimal State intervention in economic life and strict adherence to the principles of the free market, from which the legislative, executive, and judicial institutions of the State may not derogate.

4. ....'.

Article 15
The State Assembly

'1. The national parliament shall be called and known as the State Assembly, which is recalled after 52 years of forced prorogation.

2. The sole and exclusive power of making laws for the State is hereby vested in the State Assembly; no other legislative authority has power to make laws for the State.'

....

Article 79
Amendment of the Constitution

'1. ....

2. ....

3. 'Amendment to this Constitution affecting the principles laid down in Article 1 is inadmissible.'

....

Article 136
International Relations

1. Customary rules and general principles of public international law form part of the law of the State insofar as determined by the State Assembly.

2 The State may participate in international organisations if it is not in conflict with the interests and independence of the State.'

3 The Constitution also provides for the creation of a Constitutional Court, as follows:

Article 93
The Constitutional Court

'1. There shall be a Constitutional Court of the State.

2. The membership of the Constitutional Court shall comprise any and all persons who have held, but have now demitted, the office of president or of prime minister of the State. Any and all such persons shall hold the office of Judge of the Constitutional Court until their voluntary retirement or their death.

3. The Court shall rule:

a) on the interpretation of this Constitution in the event of disputes concerning the extent of the rights and duties of a State body;
b) in the event of disagreements or doubts respecting the formal or substantive compatibility of laws adopted by the State Assembly with this Constitution;
c) on constitutional complaints, which may be filed by any person alleging that one of his basic rights or one of his rights under Article 1 of this Constitution has been infringed by public authority;
d) ….

4. The Court shall annul any act of a State authority—including, for greater certainty, any judgment of a court of Kapitaal—which departs from this Constitution or, in the view of the Court, otherwise offends the dignity of the State.'

Further detail on the operation of the Constitutional Court is set out in an organic law. The Court assumed its duties and began operation in 1993.

4 Kapitaal faced formidable constitutional hurdles to Union membership, stemming primarily from Articles 15(2) and 136(2) of the Constitution. In order to adapt to membership the 2004 Law on Accession to the European Union was accorded the quality of a 'constitutional act', recognised to form an integral part of the Constitution. An unintended by-product of this was that the Constitutional Court acquired authority to test any 'act' addressed in Article 93(4) of the Constitution for compatibility with directly effective Community (now Union) law.

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5 A key component of the Kapitaalian economic miracle is the 1994 *Konkurrenz Lak*, or law of competition. The *Konkurrenz Lak* was modelled upon the (then) Community system of competition law, albeit with significant departures. It provides in part:

Article 4

(1) All agreements between undertakings, decisions by associations of undertakings and concerted practices which have as their object or effect the prevention, restriction or distortion of competition in trade in any goods or services in the State or in any part of the State are prohibited and void, including in particular, without prejudice to the generality of this paragraph, those which—

(a) directly or indirectly fix purchase or selling prices or any other trading conditions,

(b) limit or control production, markets, technical development or investment,

(c) share markets or sources of supply,

(d) apply dissimilar conditions to equivalent transactions with other trading parties thereby placing them at a competitive disadvantage,

(e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which by their nature or according to commercial usage have no connection with the subject of such contracts.

(2) The Competition Bureau established by this Law ('the Bureau') may grant a licence for the purposes of this Article in the case of—

(a) any agreement or category of agreements,

(b) any decision or category of decisions,

(c) any concerted practice or category of concerted practices,

which in the opinion of the Bureau, having regard to all relevant market conditions, contributes significantly to economic efficiency, and which—

(i) is not an agreement, decision or practice between competing undertakings; and

(ii) if an agreement, decision or practice between non-competing undertakings, the efficiency gain would, but for the anticompetitive qualities of the agreement, decision or practice, be impossible to achieve.

(3) A licence under paragraph (2) shall not be granted until the agreement, decision or concerted practice (as the case may be) has been notified to the Bureau, but any such licence may in the case of an agreement, decision or concerted practice to which paragraph (1) applies be made retrospective to the date of notification under that paragraph.

(4) A licence under paragraph (2) shall, while it is in force, and in accordance with its terms, permit the doing of acts which would otherwise be prohibited and void under paragraph (1).

6 The commercial courts of Kapitaal have determined that Article 4(1) operates subject to a *de minimis* principle, that is, an agreement, decision or practice must produce effects which distort competition 'appreciably' in order to fall within the prohibition. The Supreme Court (Commercial Division) has, through a number of cases, established a presumption that competition is not distorted appreciably

▪ if the aggregate market share held by the parties to the agreement does not exceed two percent on any of the relevant markets affected by the agreement, where the agreement is made between undertakings which are actual or potential competitors on any of these markets; or

▪ if the market share held by each of the parties to the agreement does not exceed five percent on any of the relevant markets affected by the agreement, where the agreement is made between undertakings which are not actual or potential competitors on any of these markets.

7 The *Konkurrenz Lak* was from the start, and still is, enforced by means of financial penalties imposed by the Competition Bureau for infringement of its provisions. In order to strengthen its enforcement by means of additional 'teeth', the following provisions were adopted in 1996 (with the words in square parentheses added by the 2004 Law Amending the *Konkurrenz Lak*):

Article 6

(1) An undertaking which—
(a) enters into, or implements, an agreement, or
(b) makes or implements a decision, or
(c) engages in a concerted practice,
that is prohibited by Article 4(1)[, or by Article 81(1) of the EC Treaty,] shall be guilty of an offence.

(2) In proceedings for an offence under paragraph (1), it shall be presumed that an agreement between competing undertakings, a decision made by an association of competing undertakings or a concerted practice engaged in by competing undertakings the purpose of which is to—
(a) directly or indirectly fix prices with respect to the provision of goods or services to persons not party to the agreement, decision or concerted practice,
(b) limit output or sales,
(c) share markets or customers, or
(d) limit the sale of goods by reference to geographic territory
has as its object the prevention, restriction or distortion of competition in trade in any goods or services in the State or in any part of the State [or within the common market], as the case may be, unless the defendant proves otherwise.

(3) In proceedings for an offence under paragraph (1) in which it is alleged that an agreement, decision or concerted practice contravened the prohibition in Article 4(1), it shall be a good defence to show that the agreement, decision or concerted practice in question is the subject of a licence granted by the Competition Bureau in accordance with Article 4(2).

Article 7

(1) An undertaking guilty of an offence under Article 6(1) shall be liable to a fine not exceeding [€5,000,000].

(2) An individual guilty of an offence under Article 6(1) shall be liable to imprisonment for a term not exceeding ten years.

Other than the 2004 amendments there has been no change to the *Konkurrenz Lak* since 1996.

8 In 1997 Kapitaal began to re-establish close economic ties with the neighbouring Republic of Lodmova, which had in fact been part of Kapitaal until 1940, with which Kapitaal still had strong ethnic, linguistic and cultural ties, and which was pursuing now very similar economic policies. In 1999 the two countries signed a 'Treaty of Friendship and Economic Cooperation and Integration' by which each undertook, *inter alia*, to maintain in force their respective competition laws (Lodmova having its own *Konkurrenz Lak* which is, *mutatis mutandis*, a copy of the Kapitaalian law), alteration by one

of the contracting parties being permissible only with the consent of the government of the other. The Treaty of Friendship and Economic Cooperation and Integration entered into force on 1 January 2000. It has not been abrogated. Lodmova itself applied for accession to the European Union in 2009, in 2012 was granted 'candidate status', but accession negotiations have yet to get underway.

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9 Early in 2011 AS Taluteadus, a Kapitaalian company engaged in agricultural research, developed a new plant variety, a hardy type of durum wheat (*triticum durum*), with all the hardness, protein, gluten tenacity, intense amber colour, nutty flavour and superior cooking quality of normal durum wheat but naturally resistant to mould, rust, blight, fungus, blotch and beetle and nematode infestation without need of fungicides or insecticides. The new wheat, 'Talu Durum', or *triticum durum Capitaalum*, is a distinct, uniform and new plant variety. It is also stable, but care must be taken to avoid the risk of cross-pollination with other wheat types, to which it is prone. Immediately it was developed, Talu Durum was registered by Taluteadus with the plant variety offices in Kapitaal, in a number of other EU member states, and in Lodmova, but not with the Community Plant Variety Office (CPVO) in Angers. The laws on plant varieties in each state confer upon a breeder who registers a new variety a monopoly, similar to a patent, on the germination, propagation, use and exploitation of that variety for a period of 20 years, in accordance with the rules of the International Union for the Protection of New Varieties of Plants (UPOV) of which all these countries are contracting parties.

10 Having itself neither commercial infrastructure nor adequate capital necessary to exploit Talu Durum, Taluteadus entered into licensing agreements with a Kapitaalian company AS Pollumtuit; with a number of firms in other EU member states; and with Grâudur JSC in Lodmova. Each of these firms is itself engaged in agricultural research, propagation and marketing. By the term of the agreements, Taluteadus granted exclusive propagation rights of Talu Durum to each licensee within the national contract territory, prohibited sub-licensing, required Taluteadus authorisation in the licencees' selection of growers, and prohibited active sales of Talu Durum outwith a licencee's contract territory. None of the contracts was notified to the Competition Bureau.

11 Talu Durum has met with rapid success. By the time of the 2011 winter wheat planting season it accounted for almost 20 percent of durum wheat planted in the European Union, durum wheat itself representing about a tenth of wheat production in the European Union.

12 Within months of signing the contracts, Pollumtuit was hit by wildcat industrial action, its operations effectively ground to a halt, and it found itself utterly unable to perform its contract with Taluteadus. Taluteadus therefore raised an action in the Commercial Court of Valuta (the main city of Kapitaal) seeking damages from Pollumtuit.

13 Publicity created by the civil action brought the existence of Taluteadus' contracts to the attention of both the Competition Bureau and the Prokuratuur, the Kapitaalian State prosecutor's office. Two investigations were launched, one by the Competition Bureau, the other by the Prokuratuur. The first is still in train, but following a speedy criminal investigation, the Prokuratuur charged both Taluteadus and Sepp, its

managing director (and in Kapitaalian company law legally responsible for all conduct of the company), with offences under Article 6(1) of the *Konkurrenz Lak* for entering into, and implementing, an agreement prohibited by Article 4(1) of the Law. There was no mention of Article 101 TFEU in the indictment. In November 2011 both were convicted before the Correctional Tribunal in Valuta, Taluteadus sentenced to a criminal fine of €50,000, Sepp to an 18 month term of imprisonment.

14 Sepp appealed to the Supreme Court (Criminal Division), before which he argued that:

- The Prokuratuur was bound by Article 3(1) of Regulation 1/2003 to charge Sepp with an infringement of Article 101 TFEU alongside Article 4(1) KL, and the Correctional Tribunal bound equally to apply it. Had the Prokuratuur and Tribunal done so it would have enabled Sepp to invoke in his defence Article 48(1) of the EU Charter of Fundamental Rights with which Article 6(2) KL is, in Sepp's view, incompatible.
- His conviction is incompatible with Article 3(2) of Regulation 1/2003: as Article 101 TFEU and Article 4(1) KL pursue the same material mischief, but the prohibition of Article 101 is lifted in this case owing to the applicability of Regulation 772/2004 on technology transfer agreements, the operation of Article 4(1) KL must, in accordance with Article 3(2) be set aside. It is, says Sepp, a simple question of the primacy of EU law.

Counsel for Sepp further urged the Supreme Court to refer the case to the Court of Justice under Article 267 TFEU.

15 In its judgment of January 2012 the Supreme Court dismissed Sepp's appeal. As to the first ground of appeal it found that even if Article 3(1) of Regulation 1/2003 imposes upon the 'competition authorities of the Member States or national courts' an obligation to apply Article 101 TFEU to proceedings in which Article 6(1) KL is in issue if the conditions for the application of Article 101 are joined, the Prokuratuur is not a 'competition authority', and to claim that the Correctional Tribunal is under a duty to invoke Article 101 is fundamentally to misunderstand the nature of criminal proceedings. As to the second ground, it found no incompatibility between the operation of the Kapitaalian law and the requirements of Union law, for in its context (of a view of competition law much more rigorous than that of the Union), Article 4(1) KL pursues predominantly an objective different from that of Article 101 TFEU and is therefore saved from any obligation of compatibility created by Article 3(2) of Regulation 1/2003 by Article 3(3).

16 But the Court added:

> 'Even had we found an incompatibility between Kapitaalian and Union law, we owe our primary allegiance to the former and would prefer to give effect to it. As the Constitutional Court has many times observed, Article 1 of the Constitution is an expression of the 'material core' of the State. The *Konkurrenz Lak* gives practical effect to it; an interpretation of the *Lak* which would break the link with and imperil that material core is impermissible (Article 1(3)), even by the State's constituent authority (Article 79(3), the 'eternity clause'). To find otherwise would be to endow European Union law with an authority greater than that conferred upon it by the State through the instruments of accession. It cannot be so. In this matter we are persuaded to follow the path set by the German and Czech constitutional courts, which in our view set out logically, soundly and irrefutably the legal basis of, and the nature of law and logic which governs, the European Union.'

17 And went on:

> 'But this is a course in harmony, not in conflict, with EU law: and this because of Article 4 of the Treaty on European Union, which obliges the Union to respect the national identities of the member states and their fundamental political and constitutional structures. This had been only a faint murmur in earlier case law of the Court of Justice, but with its express inclusion by Lisbon, let us borrow from the Irish poet W.B. Yeats: 'all is changed, changed utterly'. The '*Herren der Verträge*' have with Lisbon, particularly with Article 4, re-fashioned the Union constitutional order and brought a more supple balance and a greater tolerance of variable geometry in the face of that which member states hold dearest. For us it is the material core of the State as articulated in Article 1 of the Constitution, which EU law now embraces and permits – indeed, obliges - us to protect.'

18 It further found that the 1999 Treaty of Friendship and Economic Cooperation and Integration with Lodmova pre-empted the application of any Union competition law which would have the effect of altering or weakening the application of the *Konkurrenz Lak*.

19 Finally, the Court declined the invitation to submit the case to the Court of Justice under Article 267 TFEU, with a curt dismissal from the president who said 'In our view the matter is one in which the law is perfectly clear on all issues. We need not take any of Luxembourg's valuable time simply in order that they tell us what we already know'.

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20 Sepp then lodged a constitutional complaint before the Constitutional Court. The Constitutional Court proved more sympathetic and, after hearing submissions from Sepp and from the Prokuratuur, made an order for a reference to the Court of Justice under Article 267 TFEU, asking the following questions:

1. **In what circumstances do national competition rules which address anticompetitive agreements, decisions and concerted practices pursue an objective different from that of Article 101 of the Treaty on the Functioning of the European Union such that they may derogate from the obligations of Article 3(2) of Regulation 1/2003 by authority of Article 3(3)?**

2. **In obliging the Union to respect the national identities of the member states and their fundamental political and constitutional structures, does Article 4 of the Treaty on European Union permit a member state to deviate from an obligation imposed by European Union law if necessary to protect the material core of its constitutional legal order?**

3. **Does the 1999 Treaty of Friendship and Economic Cooperation and Integration between the Republic of Kapitaal and the Republic of Lodmova have the effect of maintaining in operation in Kapitaal provisions of the *Konkurrenz Lak* which would otherwise be disapplied for incompatibility with European Union law?**

21 The Prokuratuur argued that the reference is inadmissible, for in its view the Constitutional Court is not a court or tribunal for purposes of Article 267. The Constitutional Court disagreed and proceeded with the order for

reference, rebuffing a suggestion from the Prokuratuur that it ask the question of the Court of Justice, for it would doubtless be a question which the Court would consider of its own motion if it saw fit.

22 The order for reference was received by the Registrar of the Court, who assigned to it case number M-312/12.

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23 The European Commission greeted the judgment of the Supreme Court with dismay and alarm. It shares the Prokuratuur's view that the Constitutional Court is not competent to make a reference to the Court of Justice. Immediately it sent Kapitaal a formal letter of notice in which it identified the failure of the Supreme Court to make a reference to the Court of Justice under Article 267 as a breach of the third paragraph thereof. It referred extensively to its previous investigation involving the paucity of references from the Swedish *Högsta domstolen* and its initiation of enforcement proceedings against Sweden in 2003 and threatened similar action against Kapitaal. Kapitaal did not respond. In May the Commission sent Kapitaal a reasoned opinion identifying again the alleged breach and demanding Kapitaal respond by the end of July. In August Kapitaal sent the Commission a reply, stating simply that the Supreme Court is not a court 'against whose decision there is no national remedy under national law', for any judgment of the Supreme Court is subject to annulment by the Constitutional Court, it is therefore a court with complete discretion as to whether or not to refer a case to the Court of Justice under Article 267, and it choosing not to do so does not engage Kapitaal in a breach of the Treaties.

24 The Commission thinks otherwise. On 1 September it submitted to the Court a formal written application under the second paragraph of Article 258 of the TFEU seeking declarations that,

- **by the failure of the Prokuratuur to indict Sepp for an infringement of Article 101 of the Treaty on the Functioning of the European Union, the Republic of Kapitaal has failed to fulfil its obligations under Article 3(1) of Regulation 1/2003;**
- **by the failure of the Supreme Court to refer to the Court of Justice the case of *Sepp* v *Prokuratuur*, the Republic of Kapitaal had failed to fulfil its obligations under Article 267 of the Treaty on the Functioning of the European Union; and**
- **by maintaining in force a judicial system whereby the final court of review, with plenary jurisdiction in matters of European Union law, is, by virtue of its composition and jurisdiction, not a court or tribunal within the meaning of Article 267 of the Treaty on the Functioning of the European Union, the Republic of Kapitaal has failed in its obligations under the second paragraph of Article 19(1) of the Treaty on European Union.**

The Registry has assigned to the case number M-365/12.

25 By order of 1 September the President of the Court of Justice ordered that Cases M-312/12 and M-365/12 be joined for purposes of written and oral procedure. In accordance with Article 23 of the Statute of the Court, the Registrar notified Sepp and the Prokuratuur (as parties to the main action in Case M-312/12) and the Republic of Kapitaal (as defendant in Case M-365/12). Sepp is represented by Kapitaal's most formidable advocate in

matters of European law, and because Sepp and the Commission have a common interest in the outcome, she has agreed to act also for the Commission in Case M-365/12. You are therefore invited to submit a single set of observations on behalf of Sepp and the European Commission (as applicants) and a single set of observations/statement of defence on behalf of the Prokuratuur and the Republic of Kapitaal (as defendants), to be received by the Court by 30 November 2012.