

STATES OF JERSEY

Corporate Services Scrutiny Panel Proposed Importation of Bovine Semen

MONDAY, 16th JUNE 2008

Panel:

Deputy P.J.D. Ryan of St. Helier (Chairman)
Deputy J.A. Martin of St. Helier
Connétable G.F. Butcher of St. John
Connétable P.F.M. Hanning of St. Saviour
Professor S. Hall
Ms. S. Power (Scrutiny Officer)

Witnesses:

Mr. C. Webb (Executive Director, Jersey Competition Regulatory Authority)
Mr. S. Farr (Legal Adviser, Jersey Competition Regulatory Authority)

Deputy P.J.D. Ryan of St. Helier (Chairman):

Good morning. Welcome to Corporate Services and our Sub-Panel looking into bovine semen importation, or the lack of as the case may be. **[Laughter]** Welcome to the executives from the Jersey Competition Regulatory Authority. Introductions first. Would you mind, for the record, because we are recording, so that we can recognise your voice, could you introduce yourselves, please?

Mr. C. Webb (Executive Director, Jersey Competition Regulatory Authority):

Sure. My name is Chuck Webb, Executive Director of the J.C.R.A. (Jersey Competition Regulatory Authority).

Mr. S. Farr (Legal Adviser):

I am Sebastian Farr. I am the Legal Adviser for that organisation.

Deputy P.J.D. Ryan:

We have Deputy Judy Martin; Sam Power, our officer; Constable Hanning; and myself, Deputy Patrick Ryan. Our adviser on the technical side, Professor Stephen Hall and the Connétable of St. John, Graeme Butcher. To launch straight in; what would be the implications of lifting the ban on semen importation on liquid milk controls as such as we have them?

Mr. C. Webb:

From a J.C.R.A. perspective, nothing really changes. The role of the J.C.R.A. is 3-fold, or 4-fold right now. We are the enforcer of Jersey's competition law; in that case we are very much a law enforcement agency. That law prohibits abuses of dominance and cartels and regulates mergers in Jersey. That is role number one. Role number 2; we are the regulator of Jersey's telecommunications industry. Role number 3; we are the regulator of Jersey's postal industries. In those cases telecom and post are quite similar. The 4th role, which is related to the top 3 is; we can be asked to advise the Minister for Economic Development on certain issues relating to monopolies, markets, et cetera. The most recent advice we provided there was in supermarkets. So, as such, the J.C.R.A. currently has no direct regulatory role in the dairy industry so, from our perspective, it has very little implication to what we do.

Deputy P.J.D. Ryan:

What we are looking for is your experience of competition law generally without United Kingdom, E.U. (European Union) generally. So we are looking for, as much as anything else, I think we are looking for a subjective view on what you feel the implications could be as opposed to what they may or not in law be now. We are looking for advice generally as to whether there are implications because many people have said that there are implications and what we are looking for you to say is whether that is right or wrong.

Mr. C. Webb:

Sure. It is not really an area that we have looked at in detail so, I mean, we have read the States' explanatory memorandum attached to the draft legislation and according to that the importation of semen would lead to benefits such as greater yield at a lower cost which, if those results pan out, would be pro-consumer and something that we would be in favour of but I want to stress; we have not looked at those issues independently so I, here, can give you no independent assessment of whether or not those claims would bear fruit or not. It is something we just have not looked into.

Deputy P.J.D. Ryan:

Because the question that I would like to ask is, would lifting the ban on the importation of semen and removing the so-called - I say so-called - closed herd argument that was used in the 2001 challenge. Are you familiar with the 2001 challenge?

Mr. C. Webb:

Yes, we are.

Deputy P.J.D. Ryan:

Yes. Would this weaken the case for maintaining whatever controls we have on the importation of liquid milk?

Mr. C. Webb:

I think that is a very difficult call because in 2001, I understand, there was a complaint made to the European Commission about the import restrictions in Jersey and the closed-herd argument was used as a justification for that and, as I understand it, the case went away; was not pursued by the European Commission. I think it is a hard call because you can never really judge with any degree of accuracy what goes on within the inner workings of the Commission. Was the case not pursued because of the closed-herd argument and, if so, was the lack of importation of semen -- how big was that in the Commission's mindset? I do not know. Or was it not pursued simply because the Commission had other priorities? That happens all the time as well. So I think that is very difficult to answer without having direct access to the Commission. The one thing I do note, however, is that I understand Guernsey has similar import restrictions on liquid milk. I also understand that Guernsey currently imports semen for Guernsey cows and it has not been yet tested by the Commission. But, again, the fact that it has not been tested in no way creates law.

Deputy P.J.D. Ryan:

I think we would need to ask the question of our lawyers, specifically, although I am aware that we do have a lawyer right here and now. It has been put to us that the controls that Guernsey exercises on the importation of liquid milk predate the accession to the E.U. of the United Kingdom and therefore predates protocol 3 that governs our relationship with the E.U. directly. Do you happen to know if that is true or not or if there is any substance to that?

Mr. S. Farr:

I have read protocol 3 and the relevant articles of the Accession Treaty and there is nothing in there which deals with pre-existing law as such. So the position as I see it is that the rules relating to the free movement of goods apply to Jersey and they prohibit quantitative restrictions and measures having an equivalent affect; so, in other words, things that make imports more difficult, if I can put it like that. There are, as you know, some grounds upon which such prohibitions or limitations can be justified, one of which is the health of humans or animals. Now, I read the explanatory memorandum that went with the draft regulations and I noted that there are a number of economic benefits listed there, for example, more milk from fewer cows and therefore lower feed costs and so on. While you will, of course, have to take your own legal advice, I will just make the point that the European Court has been very clear on the issue that an economic justification does not form part of those lists of justifications in Article 30 of the Treaty.

Deputy P.J.D. Ryan:

Let me just highlight the relevant point I think you made there, which was that you can have an overruling concern against the free movement of goods on the basis of health of animals?

Mr. S. Farr:

Health of animals is one of the issues.

Deputy P.J.D. Ryan:

That or health of humans?

Mr. S. Farr:

Health of humans or health of animals..

Deputy P.J.D. Ryan:

In this case it would be, presumably, health of animals that we would be ...

Mr. S. Farr:

That, I would imagine, would be the ground that would be put forward but I have to say, having read the explanatory memorandum, most of the stated benefits in there would tend to be economic, at least the way I have read that document.

Deputy P.J.D. Ryan:

Thank you. I think what you are saying is that there does not appear to be any substance to the pre-dating of whatever Guernsey does --

Mr. S. Farr:

That is right, yes.

Deputy P.J.D. Ryan:

-- to what Jersey could or could not do?

Mr. S. Farr:

Yes.

Deputy P.J.D. Ryan:

So it begs the question, and I do not expect you to answer, how does Guernsey do it? **[Laughter]**

Mr. S. Farr:

Well again, as Chuck has said, the Commission has limited resources when looking at infraction proceedings. For example, and this is a serious remark: I expect a number of potential infraction cases that are currently pending will go very much on the back burner as a result of Ireland's no-vote on the

Lisbon Treaty. That is just one example of why cases get put right down the list or frankly just evaporate.

Deputy P.J.D. Ryan:

We will just get our heads around that one. **[Laughter]** I think we had probably better go to B. and C. (?) on --

Mr. S. Farr:

The brown bees?

Deputy P.J.D. Ryan:

Yes. Brown bees, yes, what happened there?

Mr. S. Farr:

I have read the brown bees case, as you would expect. In my view it is slightly different. That case involved a prohibition on the import of any type of bee other than the brown bee on to the Island of Læsø, which is about 12 miles off the Danish coast, as I understand it. Now, the reason for that prohibition was that apparently, and again, I am afraid, I do not know the reason for this but brown bees are threatened with extinction if they crossbreed with any other type of bee. So, interestingly, the European Court held that the ban in question did constitute a measure having an equivalent effect to a quantitative restriction but that it could be justified, again, on grounds of animal health and clearly, if a species is going to become extinct, that must be a clear case of an animal health issue. Again, slightly different from what I have read in the explanatory memorandum to the draft law.

Deputy P.J.D. Ryan:

All right. Are you familiar with the convention on biological diversity?

Mr. S. Farr:

Again, I have read it in recent days. **[Laughter]**

Deputy P.J.D. Ryan:

“The U.K. government are acting on behalf of Jersey is undertaking to protect its farm animal genetic resources.” Now, could the importation of semen go against this obligation?

Mr. S. Farr:

I read the convention and I concluded that it was so widely drafted that almost anything is possible or not possible underneath it. To answer your question, Article 15(2), which I am afraid I do not appear to have brought with me, provides that: “The contracting parties to the convention shall facilitate access to

genetic resources for environmentally sound uses by other contracting parties.” Now, it seemed to me that that could be used to justify the import of almost anything falling within the terms of that convention. So the point I would make is that it is very widely drafted.

Professor S. Hall:

Yes. The F.A.A. (the Food and Agricultural Organisation of the United Nations) which concerns itself with animal genetic resources worldwide, has made it clear that their view is, as you correctly say, that genetic resources are there to be used, but also that the contracting parties have an obligation to protect them. Almost certainly, this has not been tested in any way.

Mr. S. Farr:

Not as far as I am aware.

Professor S. Hall:

So, almost certainly, if there is an obligation, it is not an explicit one, it is more within the spirit of the convention.

Mr. S. Farr:

Yes, I am sure that must be right.

Professor S. Hall:

There is a difference with the brown bees; where the health argument could be used because the import would lead to extinction, in other words, the destruction of a distinct life form, a distinct species, whereas, of course, we are not dealing with a distinct species, we are dealing with a distinct breed which is a subset of a species. So, insofar as the legal situation is, it would be hard, or would be impossible to make a case against importation on the grounds of the letter of the convention?

Mr. S. Farr:

Yes. I think that is right, yes.

Professor S. Hall:

Although it would probably be opposed to the spirit.

Mr. S. Farr:

That may well turn out to be the case. It is an extraordinarily widely-drafted treaty, but I have to say, I read it fairly quickly but I have read it in recent days.

Professor S. Hall:

Yes, and you are not alone in finding it not totally clear in regards to this sort of aspect.

Deputy P.J.D. Ryan:

Have we exhausted the legal ins and outs?

Professor S. Hall:

Just (a).

Deputy P. Ryan:

(a), yes. What are the legal reasons behind not being able to restrict importation of semen? Only to Jersey breed, it would seem? Only to restricting semen importation to Jersey breed only?

Mr. S. Farr:

Well, again I will just go back to the general rules on the free movement of goods but I have to say that, other than sort of discrimination arguments, it is rather difficult to point to any particular reason why the legislation cannot be narrower than it is, other than in the sense of the general rules on the free movement of goods.

Deputy P.J.D. Ryan:

Guernsey does it. What would happen if we did it?

Mr. S. Farr:

Well, I would imagine you would be subject to the same scrutiny that Guernsey is subject to.

Connétable P.J.M. Hanning of St. Saviour:

Would we be liable to more scrutiny because there are more Jerseys in the world? The point that Guernsey made to us that they were much smaller in number and that they could probably keep below the parapet.

Deputy P.J.D. Ryan:

Let me qualify that, and I think the words were actually used by the people in Guernsey, but Guernsey feels that the Guernsey way is that it is important to be unimportant.

Mr. C. Webb:

In my opinion I think it is notoriously difficult to gauge what will interest the Commission or not. It seems to be the risk of someone making a credible complaint to the Commission, is not materially different from Jersey to Guernsey, because I would imagine a complaint is more likely to come from someone within one of the 2 jurisdictions wanting to import semen; so I really cannot imagine it would

make a material difference. It is difficult to say because there are more Jersey cows outside of the home jurisdiction, whether or not that would peak the Commission's interest more.

Deputy P.J.D. Ryan:

I think the Guernsey scenario is slightly different in that they do allow the importation of live animals that are non-Guernsey, but they do not allow second breeding.

The Connétable of St. Saviour:

They allow the semen of other breeds but they are not allowed to - bulls are castrated, bull calves are castrated at 6 months and the animals --

Deputy P.J.D. Ryan:

But the point is that they do control it, whereas our law, as proposed, does not. Am I correct in thinking that?

Professor S. Hall:

Well, I think the background is that it has been said that if you allow the import of Jersey semen you have no justification for refusing the import of other breed semen and I think that is the status that needs to be checked. Because it is not a completely hypothetical thing and earlier this morning we heard about the surplus heifer calves being killed at a day old, which most people found really quite distressing. Well, if those cows had been inseminated with Aberdeen Angus semen you would have a calf that was worth rearing for beef, you see, so there would be several arguments for --

Mr. S. Farr:

I think in terms of the rules on the free movement of goods that is exactly the argument that would be put. Once you have agreed to let a particular genetic in then what is the justification for limiting it to a particular herd genetic? I am not saying there could not be exceptions to that, there probably are. One thing I would say with regard to free movement of goods cases is decided by the Court of Justice that it is really very difficult to draw precedents from any of them, because they do tend to be very fact-specific. That is the only caveat I would mention. But the leading book on the subject is Peter Oliver's book on free movement of goods and it is a jolly good one.

Professor S. Hall:

So, the answer is that one would impose a control and hope, because one is invisible, it is never challenged, and if it were challenged then tackle it.

Mr. S. Farr:

That may be the case.

Professor S. Hall:

In other words I suppose it is pragmatic.

Mr. S. Farr:

Yes, indeed, and the first thing that would happen is that Jersey would receive a “letter before action” from the European Commission, essentially that is what would happen, and you have then I think 3 months in which to rectify the situation.

Deputy P.J.D. Ryan:

I am going to put you on the spot a little and I do not suppose you are going to answer this question, but I am going to ask you anyway, as a lawyer. Would there be a danger, if we were to go down that route in our law, that our law would not get past Privy Council?

Mr. S. Farr:

There must at least be a risk of that, yes. There must at least be a risk of that. I have to say I have no experience of draft Jersey legislation going through the Privy Council. I have worked in many jurisdictions but I have only been here for about a month.

Deputy P.J.D. Ryan:

In that case I will not press you. Okay, that is the legal side. Do we have any more legal questions? Okay. Can we go back to a quick one? Just, if the controls on the liquid milk imports were lifted what role would the J.C.R.A. play in that? I am thinking particularly of predatory pricing. Would this be an area that you would be more than averagely interested in, do you feel?

Mr. C. Webb:

Yes, if the controls on liquid milk imports were lifted the companies selling milk in Jersey, both domestic and foreign, would be subject to enforcement under the Competition (Jersey) Law 2005, under which we are the investigative and enforcement authority. If there was an allegation of predatory pricing that is something that we could investigate -- predatory pricing can be a very serious abuse of dominance under the law. If there was an allegation and it was credible we could investigate it and if we found out that it was true the law gives us the full right to impose behavioural directions and impose fines on those found to be in violation of the law.

The Connétable of St. Saviour:

Can I just follow through with that? Given that it is a small island and a small market, could I ask how fast you could act in this case to stop it? Because a lot of damage could be done quite quickly.

Mr. C. Webb:

Yes, regulators come in when the body is already on the ground as they say. But the competition law gives us, if there is - to open an investigation you need reasonable cause to suspect there is a violation. How do we get a reasonable cause to suspect? That can come from many sources. It most often comes from people complaining to us but it can also come from information we receive via the *J.E.P. (Jersey Evening Post)* et cetera, but assuming it is a complaint there is a mechanism in the law that says we can impose interim measures, which is something that basically is an interim direction saying: "Thou shalt act in a certain way pending the outcome of the investigation" and the legal grounds to show that are I believe the public interest or harm to a particular person or class of persons. So, if a complainant would come in and say: "There is a predatory pricing out there and if you do not take care of it we are in imminent danger of going under" if they make a credible case to us we can impose interim measures. Then that would prohibit the conduct pending the outcome of the investigation. Of course as a matter of process, before we would put in place interim measures, the person or undertaking we are considering putting it in place against would have the right to see the draft motion and then comment on it, and they also have a right -- if we would still go forward despite their comments, they have the right of appeal in the Royal Court. That provision is in the law.

Deputy J.A. Martin of St. Helier:

Can I just check where you stand under the law, under the Competition Law on the other way round? Just say that if liquid milk was then allowed to be imported, or there was a challenge and we were importing liquid milk, do you have any controls to the bigger supermarkets maybe to use that and give milk very cheaply to the consumer out there? I think I have asked this question before on the telecoms, but it is a reverse of the predatory pricing to the loss leader.

Mr. C. Webb:

Predatory pricing and loss leading, Deputy Martin, I think it is kind of all the same vein in my mind, because you are still talking about cheap, low cost prices for milk. Now as the Competition Authority, our main mission is to promote consumer welfare in Jersey, consumer welfare in terms of lower prices and choice of goods and services. So I think as a Competition Authority, when someone comes in and complains about a low price being against the Competition Law we need to be careful because at the end of the day low prices is what we are here to try to facilitate. If someone comes in and says: "This is predatory" I think we would need to see the evidence before us. Under European Competition Law predatory pricing happens when a dominant firm is selling something below their own marginal costs of production and we would need to check and see if there is an actual predatory pricing case here based on the facts before us. If we do conclude that there is a predatory pricing case the law gives us a full ambit of remedies of which to impose, but it is something we could not do willy-nilly, let us say. It would just depend on the facts.

Deputy P.J.D. Ryan:

To get a direction from the Economic Development Minister on the Jersey dairy industry in general and milk imports in particular, there has to be a process that you would go through where you have to advise the Minister and he has to advise back, I think I am right in thinking that. To what extent can the J.C.R.A. take into account other, wider issues? For example the effect on the tourism industry and local - long term continuance of the supply of liquid milk - how much longer term thinking can you bring into this or is it all about the money short term, what is the cheapest product? Because a supermarket could obviously bring in liquid milk from the United Kingdom or even France and it is likely to be, without even going below their cost base as you said. I think you used the word “marginal”.

Mr. C. Webb:

Average marginal costs.

Deputy P.J.D. Ryan:

Average marginal costs. It could well be that it would satisfy that but would still be not in the best interests of the community as a whole. To what degree can you take those factors into account when you are advising the Minister and he is issuing a direction back to you?

Mr. C. Webb:

I think that is a very difficult question. Under Article 6(4) of the Competition Regulatory Authority (Jersey) Law the Minister for Economic Development can ask us for advice on matters of markets, monopolies, competition, et cetera, and Senator Ozouf most recently did so with respect to the question of a third supermarket in Jersey. So, the scope of our advice is very much limited to economic aspects and again being a competition law agency here with consumer welfare the main thing we are looking at is terms of prices to consumers, choice as well, but price is a big component. I think when you get to - I fully admit consumer price is not the only relevant consideration but I think if there is let us say in terms of the dairy industry, if there is a perceived conflict between low prices to consumers and what the government terms brown cows on green fields or the sanctity of the Jersey breed, I think the balancing that needs to take place is really a political question. It is not necessarily a question we can address. What does a society value more; low prices for milk which could come with imports or having the Jersey cow on green fields? That is a very difficult question. It calls for a balancing of competing interests that I think as an independent statutory authority here to promote competition, it is not one that we can take. I think that is really a call for Jersey’s elected officials.

Deputy P.J.D. Ryan:

Let us talk to something which is more I think in your normal domain. Jersey Dairy are looking to increase the Island’s export trade and they would be using the brand value of the Jersey Island cow to leverage a price advantage on things like butter and yoghurt and what have you. The profit that they

make from those items that they export, if those profits were used to subsidise the price of local milk downwards would this be something that the J.C.R.A. would be interested in?

Mr. C. Webb:

To use a lawyer's term, it depends. Cross-subsidisation I think is a - it is one of those buzzwords that are - for lack of a better term - buzzed about, but they are not in themselves per se violations of the Competition Law. Frankly, cross-subsidy is something every business on the face of the earth does literally every day. It is usually cross-subsidisation plus another conduct that can lead to Competition Law problems. So, with one exception I think, the one exception I can think of in terms of the precedents, this is pretty thin in terms of precedent, again I am talking about E.C. precedent, not Jersey precedent here; if you have a statutory monopoly in one area and you use the profits gained from that to get a competitive advantage in competitive markets that under some interpretations can be abuse of dominance, but that is not what we are talking about here. Here we are talking about profits gained in foreign markets themselves, let us assume, they are competitive, and using that to subsidise the price of milk here in Jersey. Again we are here to promote low prices for Jersey's consumers so to the extent that Jersey Dairy would be doing that and the prices themselves are remaining above the predatory level - I want to correct something, it is the standard test for predatory pricing is pricing below average variable cost, which most times equals marginal cost - but as long as Jersey Dairy's prices are above the predatory level then I see no inherent problem in that. If they are using it though to have predatory pricing in Jersey then that can be a potential problem.

Deputy P.J.D. Ryan:

But while there is no liquid milk being imported of course you have no predatory pricing issue, have you?

Mr. C. Webb:

That is true. Although if I can just say there is, as a result of our intervention before, there is now one domestic producer who for all intents and purposes is selling his milk outside of J.M.M.B. (Jersey Milk Marketing Board) to the extent, even without imports of liquid milk there is now a very limited form of domestic competition for milk, so you still have a potential complainant out there.

Deputy P.J.D. Ryan:

I think we have come pretty much to the end. I am going to ask you one last question. If the imports of liquid milk were permitted would the J.C.R.A. be able to exert any control over the price at which they were sold? This is linked to the predatory pricing issue. A major retailer might sell milk at a discount as a loss leader. I think we have really covered this. I do not think I really want to go much further with it. I think we have answered it in previous answers to previous questions. I think I will draw a halt there. Does anybody else have anything? Then I will just say thank you very much for your time this

morning. I look forward to seeing you some time again.