THE ANTITRUST EFFECTS OF THE FIXED CONVERSION RATE. THE CASE OF GERMAN BANKS

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The establishment of a common market is one of the fundamental goals of the Treaty of European Communities (art 2 EC). Anti-competitive behavior is forbidden in order to ensure that competition in the internal market is not distorted or negatively influenced (art 3 lit g EC) and to achieve a high degree of competitiveness and convergence of economic performance. The European competition rules support and complement the common market and play an essential role in integrating the market. In order to preserve this, in 2001 the European Commission applied a fine amounting to EUR 100.8 million to a group of five important banks from Germany, which have agreed to settle a commission of 3% for the currency exchange operations. The present paper discusses the implications of this decision from two important points of view: the infringement of competition law and the consequences related to Euro introduction.

Key words: banking system, common market, competition law, euro area, exchange rate

Introduction

The introduction of this sole currency was perceived, at least by the banking system, as a cost difficultly to recover. There is no doubt that this historic moment has caused incertitude among the market players and has generated favorable circumstances for the infringement of the legislation in the competition field. Thus, the Commission was not persuaded and it settled a fine amounting to EUR 100.8 million in 2001 to a group of five important banks from Germany, which have agreed to settle a commission of 3% for the currency exchange operations. The purpose of the said commission was to recover approximately 90% of the income determined by the margin of the currency exchange (the spread or difference between the selling rates and the buying rates) between the currencies from Euro area, which had to disappear on January 1st, 1999 for the settlement of a fixed and irrevocable currency exchange rate between them and the sole currency.

The European Council from Madrid has settled, in December 1995, the schedule for the transition to the sole currency and a common framework for the development of this process, but many details related to the technical preparation remained unsolved. Thus, starting with January 1st, 1999, for a three years period, Euro has existed only as virtual currency in the states from the economic and monetary union. In 1999, the member states of euro area were Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, Portugal, Spain, Netherlands; Greece joining the euro area in 2001.The national banknotes of the participant states have continued to circulate and to be part of a transaction through the currency exchange services, at a currency rate irrevocably established between them and Euro from January 1st, 1999, the units of the national currencies becoming subunits of Euro currency. Starting with February 1st, 2002, the national banknotes and coins have actually circulated in parallel with Euro for a six months period, being gradually withdrawn from circulation during this period.

Before January 1st, 1999, the earnings of the banks for the currency exchange transactions were exclusively represented by the difference between the selling rate and the buying rate of different currencies (spread). After this date, the fixed and irrevocable conversion rate between the currencies of the 12 states and Euro currency had as effect the disappearance of the double and automatically rate of the earning cashed by the banks as a result of these operations. Even if this fact had to lead to the decrease with 20% of the costs determined by the elimination of the currency exchange risk (by eliminating the fluctuations of the exchange rate), still the banks have considered that the currency transactions have to be taxed as a commission. The commission was going to cover

the storage, transfer, provision and processing costs connected with the sole currency, but also the inventory and risk coverage costs for the risk of receiving fake banknotes.

The recommendation of the European Commission from April 23rd, 1998, regarding the banking commissions levied for the conversion to Euro currency, stipulated only one good practice standard. Thus, the communitarian authority has not expressly requested that the currency exchange, between the currencies of Euro area, to be done without levy a commission (excepting the amounts transferred from Euro in the national currency and vice versa, within the transition period) nor has it imposed restrictions to the freedom of the banks in applying this commission according to their own-established policies. The only mandatory stipulation for the banks referred to the fact that the application means, for this type of commission, have to be based on transparency and informing of the consumers in due time and not by a coordination of behavior.

The exchange of information on actual and individual prices, turnover, delivery quantity, stock of inventory, exports et cetera that admits conclusions on the market strategy, may restrict the autonomy of the entrepreneur and thus competition.45 An increase in transparency by the sharing on a regular and frequent basis of information concerning the operation of the market (on the non-oligopolistic market) may stimulate competition (CFI, 1994).

The case analysis

The developed banks, whose currency exchange operations were significantly contributing to the total profits, were the most affected by the consequences of adopting the common currency. The loss of some additional incomes in a technologically readapting period was felt in a more profound way by the great institutions, with a developed infrastructure, whose exchange offices, with an activity exclusively based on currency operations, could not be supported during the transition period, although their activity continued in the same manner, even more sustained. For example, Deutsche Reisenbank (Deutsche Genossenschaftsbank AG is a group that holds 67% of Deutsche Verkehrsbank AG shares, and the latter holds all the shares in Reisenbank AG, which is the only company around the group that is exclusively active on the retail exchange market) had in 1997 approximately 60 exchange offices and 300 associates and 80% of the obtained profits were coming from the exchange operations, which were going to decrease with 40% after the introduction of Euro currency. Furthermore, Bundesbank, the Central Bank of Germany, was bound, according to art. 52 of ESCB (the European System of Central Banks) statute, to buy the currencies of the states from Euro area, from the banks or the public, free of any commission, during the transition period. In this way, the other banks from the system would have been forced to apply a similar treatment, to perform exchange operations free of commission or with low commission. The effects would have been felt by the Dutch banks, forced to review their earning margin, or to face the risk of movement, with regard to the currency market, from Holland towards Germany, where the costs of the transactions would have been more attractive. The pressure over the German banks for setting a commission also came from the Dutch GWK Bank.

In order to assess whether an anticompetitive restriction falls under the prohibition of horizontal agreements, one has to define the market it (potentially) affects. This requires the analysis of the relevant market characterized by three dimensions: the product or service, the geographic area affected and the time horizon (Eilmansberger, 2003; Stockenhuber, Schröter, 1999).

Thus, *the relevant market of the product in this case is formed of the Euro subunits exchange service,* in which at least a part of the transaction contains banknotes and coins of the 12 states that are members of Euro area, this service being mainly offered by the banks and exchange offices. The German system is dominated by the universal banks, which at the end of 1998 did not exceeded 3400, having more than 45 000 subsidiaries, a wide range of specialized banks such as mortgage banks or other financial institutions such as building societies (Bausparkassen).

Confronting with an inevitable fact, which was going to decrease their profits, **Commerzbank AG, Dresdner Bank AG, Bayerische Hypo- und Vereinsbank AG, Deutsche VerkehrsBank AG, Vereins- und Westbank AG** appreciated, as a result of some successive meetings and discussions in 1997, that they can not handle the costs determined by the sole currency only if they continue the application of 3% banking commission during the transition period. This fact has helped them to recover 90% of the losses they would have unconditionally suffered between January 1st and July 1st 2002. If the appliance of a commission, even of 3%, was in full accordance with the recommendations of the Commission, not existing any interdiction regarding this, ***the commonly taken decision would have also been considered as a violation of art. 81***, which regulates the agreements between companies.

Art 81 EC forbids collusions between undertakings that may affect trade between member states and which have the object or effect of restricting competition within the common market. The establishment of a common market is one of the fundamental aims of the Founding Treaty (art 2 EC). Anti-competitive conduct is forbidden in order to ensure that competition in the internal market is not distorted (art 3 lit g EC) and to achieve a high degree of competitiveness and convergence of economic performance (Bapuly, 2006).

It is not accidentally that the five banks, which infringed the provisions of art. 81, form the group of the commercial banks (Kreditbanken – a distinct category among the universal banks) also known as „the big four", and their share on the retail currency market represents an average between 70% and 80%. Although the Commission did not make this distinction in the analysis of the case, they can be seen on the *sub-market delimited by the segment of commercial banks as an oligopoly*, which is automatically subjected to the trend of coordinating the behavior in order to preserve the profits and consolidate a position on the respective market. The fewer the companies on the market, the more likely that collusion among them will be found (Maks, Witte, 2004). It would not have been that simple, and the stake not so important for the 594 savings offices or 2 256 cooperative banks present on the banking market from Germany, whose influence, determined by a reduced market share, would have been an insignificant one.

It is not surprising the fact that Deutsche mark held at that point in time the supremacy between the most requested exchange currencies, both for buying and selling on the Union territory. Thus, of the total volume of the selling transactions with the national currencies of the states from Euro area of approximately EUR 17 billion in 1998, 35% were represented by the sales performed with Deutsche marks. At the same time, the German currency held more than 50% of the total volume of buying transactions, evaluated at EUR 24.7 billion.

European Commission's Decision

On December 11th 2001, the European Commission decided to apply to the five banks, who have agreed on the application of the commission, fines between EUR 2.8 million and EUR 28 million, depending on their importance on the relevant market, based on the income obtained within the previous financial exercise. In order to obtain a greater discouraging effect for this type of practices, for some of the banks participating in the agreement (Commerzbank AG, Dresdner Bank AG and Bayerische Hypo - und Vereinsbank AG), the value of the fine was doubled, taking into account their size and the available resources. To the initial amount, reflecting the seriousness of the understanding, an increase of 40% was added, representing the duration of the infringement. Although the understanding had as object the application of the commission between January 1st, 1999 and December 31st 2001, the Commission applied the fine, taking into consideration the time of decision-making, namely October 15th 1997.

Having as object the way of taxing the transactions with currencies under the form of a commission, but also of the level of this taxation of approximately 3%, in order to recover some future losses, the understanding of the German banks have been considered a serious infringement of art. 81 (direct pricing) forbidden *per se*, ***without existing the need to demonstrate an effect.*** The understanding did not have as result the application of a 3% fixed commission by all the banks which have not participated in the understanding, but the **causing or non-causing of the effects on the market is not relevant in the assessment of this type of understandings, especially if the object is the price.** In fact, we are dealing with the harmonization of price policies and the alignment of prices regarding the purchasing or selling of bills of member states in euro area. Anyway, the common discussions took into considerations a margin of the commission between 2 and 4%, but finally, none of the banks practiced a commission under 3%. The legislation in the competition field forbids the coordinated behavior of the participants or only their intention to align the price (in our case, the price for the currency exchange service) to the prejudice of the consumer, without being important if the effects were concretely caused, are about to be caused or are just probable.

The concept of an agreement is defined as the "concurrence of wills between economic operators on the implementation of a policy, the pursuit of an objective, or the adoption of a given line of conduct on the market, irrespective of the manner in which the parties' intention to behave on the market in accordance with the terms of that agreement is expressed" (Bayer case, 2000). The full implementation of the will is not necessary.

Regarding the benefits to consumers it is important to know that the term of a "consumer" is to be understood in a broad sense: it refers not only to the consumer of a product, but also covers the general public being directly and indirectly affected (e.g. consumers of environmental benefits). Lower prices a greater consumer choice, the improvement of life quality (health of the general public, reducing environmental pollution, improvement of security) show a fair share of the benefits (European Commission, 1996, 1988, 1989, 1999).

The understanding of German banks had an explicit character, existing concrete evidence of the agreement (multiple meetings ascertaining documents, facsimiles and invitations), whose object or effect was the diminution of the competition, being capable to affect the commerce between the member states. Decisions in terms of art 81 taken by associations of undertakings express a legally or factually binding will. Non-binding recommendations are treated as agreements between members who implemented them after attaining general meetings where they were discussed (ECJ, 1994).

In spite of the fact that the respective understanding was referring to the banking market from Germany and cross-border regions from Holland, the European courts think that any diminution of the competition, which regards the territory of a member state, by its nature it has the effect of enforcing the division of the market at national level, which contradicts the principles of the sole market. Still, in this case, the exchange services with the currencies of the 12 member states imply multiple operations of selling and buying banknotes on the international markets by the banks, as result of the foreign currency demand, which is encountered in each state. The currency exchange is guided towards consumers in general and especially the tourists (both from and out of the Community), who wish to make payments within Euro area. In other words, it means a cross-border service, with effects on the inter-communitarian commerce.

Conclusions and implications for Romania

According to the officially expressed intentions of adopting the European sole currency, Romania will adopt Euro between 2012-2014, after it will have accessed the European exchange rates mechanism (ERM II) between 2010 and 2012. Among other measures, this fact also means the maintenance of the exchange rate between Euro and the Romanian currency within the limits -2.25%, +2.25%. Among the states from the Central and Eastern Europe, which acceded to EU in 2004, Estonia, Lithuania, Slovenia, Cyprus, Latvia and Malta were in the preliminary stage of adopting Euro (ERM II), some of them succeeding to adopt Euro (Slovenia in 2007, Cyprus and Malta in 2008). For Slovakia, Czech Republic and Poland 2009-2010 perspective is the most realist one, while the bets for Hungary (with a record in budgetary deficit over the last year) rather indicate the year 2014.

It should be specified, before introducing Euro, the banks do not have an explicit commission for the currency transactions. The consumers pay for any currency exchange a fee hidden in the difference between the sale rate and the buying rate of the respective currency (and in Romania it is wrongly perceived as 0%). In Germany, before introducing Euro, this fee was varying from 1.5% to 7%, depending on the type of currency. Together with the disappearing of the double rate, through the existence of the fixed and irrevocable convertibility between the other currencies and Euro (an inevitable fact before adopting Euro), the existence of the commission will be directly perceived by the consumer through a percentage applied to the value of the transactions. Sometimes, this acknowledgement has dramatic effects on the banking sector, as it has happened in Germany, where more than 700 complaints submitted by the consumers have apprise the Commission with regard to the commissions practiced on the currency exchange, and implicitly, lead to the investigation and application of a fine amounting to EUR 100.8 million given to the bank.

Romania may adopt Euro currency before Hungary or not, but the German experience is relevant for Romania due to at least two viewpoints. First, an important step, such as the introduction of Euro has to be prepared and assessed in order not to surprise the actors on the banking market, or the authorities and consumers. Each of them has to know in due time which are the available instruments, when and how they need to access them in order not to break the competition rules: The authorities have to issue in due time clear norms and regulations together with an adequate interpretation and communication to the financial-banking environment, which should provide it with a facile and less expensive conversion towards Euro, banking institutions should correctly and transparently apply these norms, and the consumer should know which is his/her role in the implementation of the competition legislation. Secondly, the application of an individual banking policy under any form, even with the risk of bearing some costs on short term is preferred instead of a common agreement against the consumer, likely to be sanctioned by the competition law.

Another important conclusion is that the Communitarian competition policy aims at protecting consumers as well as undertakings. In the end the law applicant must continuously consider recent developments in the European jurisprudence and topical literature covering the rapidly evolving situation. Of course the law applicant must also interest himself in the current economic underpinnings in order to get a holistic view of the competition policy. Using the right tools enhances chances of making Europe a functioning competitive market (Bapuly, 2006).

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