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Communication from the Commission to the Council and the European Parliament on the role of penalties in implementing Community internal market legislation

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INTRODUCTION

Following the intense legislative activity required in order to establish the internal market, the Community is now focusing on the effective operation of the common rules introduced. In particular, it needs to ensure that Directives are correctly incorporated into national law and, more generally, that Community measures are effectively implemented. This involves, among other things, deploying appropriate human and material resources, expanding administrative cooperation between the various bodies responsible for implementing the common rules, and providing natural and legal persons who suffer harm as a result of breaches of internal market rules with access to effective means of redress.

As regards the last area mentioned, in its communication to the Council entitled "Making the most of the Internal Market: Strategic programme" (COM(93) 632 final of 22 December 1993) the Commission stressed the need to improve the transparency of national arrangements for imposing penalties in the event of non-compliance with requirements deriving from the common rules.

Section B.III of the strategic programme ("Redress: Access to justice and judicial cooperation") expressly provides for the Commission to recommend:

> "improving the transparency of national sanctions by requiring that they be systematically notified [by the Member States] with transposition measures; appropriate provisions will be written into future legislative proposals in the Internal Market area and Member States will be asked to communicate information in relation to existing legislation."

Since the effectiveness of penalties forms an integral part of the overall machinery for ensuring that the internal-market rules are implemented, the purpose of this communication is to inform the Council and the European Parliament of the Commission's reasoning and plans with regard to this particular aspect of the strategic programme. This communication constitutes initial guidelines in a more comprehensive framework for discussions.

I. PENALTIES THAT ARE EFFECTIVE, PROPORTIONATE AND DISSUASIVE

Article 5 of the Treaty establishing the European Community stipulates that: "Member States shall take all appropriate measures, whether general or particular, to ensure fulfilment of the obligations arising out of this Treaty or resulting from action taken by the institutions of the Community."

The Court of Justice has ruled that, where Community legislation does not specifically provide any penalty for an infringement or refers for that purpose to national laws, regulations and administrative provisions, Article 5 of the Treaty requires the Member States to take all measures necessary to guarantee the application and effectiveness of Community law, in particular by making the penalty chosen effective, proportionate and dissuasive.[1]

As in any legal system, it is important to deter those bound by Community law from neglecting their obligations and to ensure that any infringement is duly penalized.

Accordingly, only a consistent approach to the question of penalties in the internal-market context is capable of ensuring both fair competition under fair trading conditions and the protection of those aspects of the general good covered by common rules.

Ensuring fair competition under fair trading conditions

Since compliance with internal-market legislation imposes direct or indirect costs on businesses, the potential benefits of non-compliance (short-term profit or evasion of common restrictions) should not outweigh the penalties incurred - as is the case, for example, if penalties are insignificant or only hypothetical.

In some cases, the conditions of fair competition would be undermined or harmed by deficient national rules on penalties. This could also lead, in certain circumstances, to distortions of competition prejudicial to the free movement of goods and services in the Community - something which is totally unacceptable in the internal market.

Protecting those aspects of the general good covered by common rules

Yet the importance of ensuring compliance with internal-market legislation extends far beyond the economic issues relating to the free movement of persons, goods, services and capital.

In particular, the internal-market rules require the attainment of a high level of protection with regard to health, safety, the environment and consumers.

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1 See, in particular, paragraphs 23 and 24 of the judgment in Case 68/88 *Commission v Greece* [1989] ECR 2965.

The absence of effective, proportionate and dissuasive penalties for infringing Community law would, therefore, damage the very credibility of common legislation by exposing the Union's citizens and their environment to risks that are unacceptable to the individual and to society as a whole.

II. THE LIMITS OF REFERRAL TO NATIONAL SYSTEMS OF PENALTIES

Under Community law, implicit referral - via straightforward application of Article 5 of the Treaty - or explicit referral to national systems of penalties is regarded as the norm, whereas defining common penalties remains the exception. This general state of affairs is fully in accordance with the subsidiarity principle.

The Community's legislative activity in the internal-market field is based on need and proportionality.

However, such a position is politically and socially tenable only if national systems of penalties and the way in which they are applied do not jeopardize the effectiveness, proportionality and dissuasiveness of the penalties in question.

Consequently, the existence of different national systems of penalties is compatible with the proper functioning of the internal market only if those characteristics are respected by all concerned, if need be via adaptation of those national systems.

It follows from the case-law of the Court of Justice that, where Community legislation does not specifically provide any penalty for an infringement or refers for that purpose to national laws, regulations and administrative provisions, the Member States, while remaining free in their choice of penalties, must ensure in particular that infringements of Community law are penalized under conditions, both procedural and substantive, which are analogous to those applicable to infringements of national law of a similar nature and importance and - the Court adds - "which, in any event, make the penalty effective, proportionate and dissuasive".[2]

Accordingly, where the effectiveness, proportionality and dissuasiveness of the penalty would not be guaranteed by applying an existing national system of penalties, the Member State concerned must either choose another system of penalties that satisfies those criteria, adapt its existing system or introduce a special system in order to meet the requirements deriving from Article 5 of the Treaty.

According to the well-established case-law of the Court of Justice, a Member State may not plead provisions, practices or circumstances existing in its internal legal system in order to

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2 See paragraph 24 of the judgment referred to in footnote 1.

justify applying a national system of penalties that does not comply with its obligations under Community law.[3]

There is no apparent reason to believe that, where a Member State determines the penalties relating to the Community or national rules applicable, those penalties will not be effective, proportionate and dissuasive, since it is in that country's interest as a State based on the rule of law - in terms of the confidence both of its own nationals and of the other Member States of the Union - to ensure that the rules applicable on its territory are effectively enforced.

Nevertheless, given the - in some cases - significant differences noted by the Commission in the course of assessing the transposal and application of the common rules, it is important to ensure that national systems of penalties are sufficiently transparent for their effectiveness, proportionality and dissuasiveness to be confirmed.

A particularly good example: public procurement

The internal market comprises an area without internal frontiers within which goods, persons, services and capital are able to move freely in accordance with the provisions of the Treaty. Community internal-market legislation, therefore, covers a diversity of fields including foodstuffs, financial services, the recognition of diplomas, means of transport and communication, direct and indirect taxation, and the right of residence. It takes into account the need to protect such important aspects of the general good as public health and human life, the environment, industrial and commercial property, the fairness of commercial transactions, and consumers.

However, it is not necessary to look at each of these areas in order to understand the limits of referral to national systems of penalties. Community legislation on public procurement provides by itself an example that is all the more significant because it expressly requires Member States to provide for remedies and to impose certain penalties if the rules applicable are breached.

In spite of these specific provisions, the transposal of the directives concerned[4] is hardly satisfactory and has already led the Commission to institute infringement proceedings against several Member States.

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3 See, in particular, the judgment in Case C-74/89 *Commission v Belgium* [1990] ECR I-491, confirmed *inter alia* by that in Case C-217/88 *Commission v Germany* [1990] ECR I-2879.

4 Council Directive 89/665/EEC of 21 December 1989 on the coordination of the laws, regulations and administrative provisions relating to the application of review procedures to the award of public supply and public works contracts, and Council Directive 92/13/EEC of 25 February 1992 coordinating the laws, regulations and administrative provisions relating to the application of Community rules on the procurement procedures of entities operating in the water, energy, transport and telecommunications sectors.

The Commission's reasons for doing so include the following:

- the review body is not an independent court or tribunal within the meaning of Article 177 of the EC Treaty;

- that body has insufficient powers (in certain cases, it is unable to order interim measures or has difficulty in doing so), or its powers are confined to certain types of contract.

Consequently, firms do not always have access to effective means of redress when they consider that their interests have been harmed, and the effectiveness of the relevant national penalties is weakened as a result.

In some instances, the penalties' proportionality and dissuasiveness can likewise be jeopardized: compensation arrangements are a case in point.

The public procurement directives do not lay down detailed rules regarding the amount of compensation. Consequently, in some Member States it is minimal, covering -for example - only the costs incurred in the course of submitting a bid, while in others it covers the firm's loss of earnings (i.e. the profit that the firm would have made had it been awarded the contract).

Given the economic importance of each contract covered by the directives (more than ECU 200 000 for each supply contract, and more than ECU 5 million for each works contract), it can hardly be disputed that the significant difference in compensation arrangements affects how awarding authorities and firms behave.

This situation can sometimes create distortions in competition, thereby jeopardizing the free movement of the goods and services concerned within the internal market.

That is why, in addition to examining national legislation, the Commission is attempting to assess their actual implementation. Accordingly, an analytical grid has been proposed within the framework of the Advisory Committee for Public Procurement, but it has not yet been possible to perfect the grid owing to inexplicable difficulties experienced by the national authorities in transmitting the relevant data.

III. LESSONS AND CONCLUSIONS

A Community issue

In public procurement, as in the other areas of the internal market, the effective implementation of Community legislation depends on several indissolubly linked factors.

The effectiveness, proportionality and dissuasiveness of the penalties for breaching Community law depend, in the first place, on the common rules being transposed and/or implemented correctly and effectively, and on sound administrative cooperation which is itself based on transparency.

In its communication to the Council and the European Parliament on the development of administrative cooperation in the implementation and enforcement of Community legislation in the internal market (COM(94) 29 final of 16 February 1994), the Commission stressed that uneven or incomplete application of Community law would not only reduce the overall benefits of the internal market and affect the interests of the citizens or enterprises concerned but also jeopardize the mutual confidence which underlies the whole internal-market structure.[5]

In its resolution on the same subject, the Council itself noted that it is essential for the proper functioning of the Community to increase mutual confidence and transparency between administrations and thereby ensure that Community legislation is enforced effectively, efficiently and uniformly in all Member States.[6]

The penalties issue is not, therefore, one which is purely national in scope and which can be viewed separately from the general problems associated with the operation of the internal market.

Sectoral solutions

Nevertheless, as explained above, both the scope of internal-market legislation and the specific nature of the areas it covers necessitate a pragmatic and sectoral approach to the question of penalties.

In some cases custodial penalties may be necessary (as in the suppression of the money-laundering operations addressed by Directive 91/308/EEC[7]), while in others civil liability may be appropriate (such as for the non-fulfilment of obligations under contracts concerning package travel, package holidays and package tours as provided for in Directive 90/314/EEC[8])

This pragmatic, sectoral approach is already illustrated in other areas of Community legislation, such as the Common Agricultural Policy, the Common Fisheries Policy and the Common Transport Policy (areas in which penalties often range from pecuniary sanctions to the withdrawal of a "licence", a "permit" or an "authorization"), or in the work in progress on the protection of the Community's financial interests.

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5 See point 11 of Annex I ("state of play") to the communication.

6 Council resolution of 16 June 1994 on the development of administrative cooperation in the implementation and enforcement of Community legislation in the internal market (OJ No C 179, 1.7.1994, p. 1).

7 Council Directive of 10 June 1991 on prevention of the use of the financial system for the purpose of money laundering, OJ No L 166 , 28.6.91 p. 77

8 Council Directive of 13 June 1990 on package travel, package holidays and package tours, OJ No L 158, 23.6.90 p; 59

The advent of the internal market has highlighted the fact that Member States are jointly responsible for administering the common external frontier. It was this consideration, in particular, which led the Heads of Member States' Customs Administrations to declare, in their December 1993 statement concerning a framework strategy for Customs 2000, that "our services will, in cooperation with the Commission, examine and report in 1994 on the range, classification and degree of seriousness of customs infractions ... taking account of the provisions of the Community Customs Code".

The public-procurement field is a further example which clearly demonstrates that the possibility of introducing common penalties or systems of penalties within the internal market should not be dismissed out of hand.

Only if the national systems of penalties for non-fulfilment of obligations under Community law are transparent can the Commission

- ensure that those national systems are effective, proportionate and dissuasive, and

- thereby confine Community action as regards penalties to what is strictly necessary in order for the internal market to function properly in each sector concerned.

Transparency alone is the key to mutual confidence and an indication of a common desire not to conceal any problems.

At the same time, transparency in no way prejudges any action which the Community might choose to take in individual sectors so as to ensure that the internal market functions properly.

Practical measures for the Commission to consider

In its role as guardian of the Treaty, the Commission is required to ensure that directives are correctly incorporated into national law and, more generally, that Community law is implemented effectively and efficiently.

Accordingly, the Commission will see to it that, from now on, measures whose notification is expressly required by Community provisions stipulate the relevant penalties. As stated in the strategic programme on the internal market, appropriate provisions will *inter alia* be written into future proposals for directives or regulations relating to the internal market (see examples of standard clauses given in the annex to this communication).

However, transparency is also called for in administering the existing body of Community law. That is why, in the context of monitoring the transposal and implementation of Community law, Member States will be called on to notify - where they have not already done so - all relevant information regarding their systems of penalties, and research will be undertaken in the sectors requiring further work.

Where necessary, and within the limits of its power of initiative, the Commission will take measures and/or make proposals with a view to resolving in an appropriate manner any sectoral problems that arise in connection with penalties. If need be, those measures and/or proposals may involve the introduction of common penalties that satisfy the criteria of effectiveness, proportionality and dissuasiveness required in order to implement Community internal-market legislation.

Practical measures for the Council and the Member States to consider

When discussing the memorandum from the French Presidency on penalties for breaches of Community law and its effective implementation , the Council will have the opportunity to stress the political importance of this issue for the proper functioning of the Community in general, and the internal market in particular.

A clear and firm political commitment by the ministers responsible for the internal market, supported by the Heads of State or Government of the Member States within the European Council, should make it possible to rally support among the national authorities for mutual transparency with regard to penalties and should enable the Council and the Member States to discuss openly and constructively the solutions which the Commission will, if necessary, propose in this area.

Such a commitment would be in line with the declaration on the implementation of Community law (No 19) annexed to the final act of the Treaty on European Union

CONCLUSION

By means of this communication, the Commission calls on the Council and the European Parliament:

- to take note of its initial guidelines on penalties in the Internal Market field;

- to confirm the need for national systems of penalties in this area to be transparent;

- to give a firm commitment to supporting work on penalties, particularly in the following sectors: public procurement, customs legislation;

- to undertake to discuss openly and constructively the sectoral proposals which the Commission will be called upon to make during the coming months in order to ensure that penalties for breaching the internal-market rules are effective, proportionate and dissuasive.

ANNEX

Examples of standard clauses that the Commission intends to include in its future proposals for EC regulations and directives

The following examples, which are purely indicative, in no way prejudge the appropriate provisions that the Commission might wish to include in specific or sectoral legislation.

For regulations:

"Member States shall lay down the system of penalties for breaching this Regulation and shall take all the measures necessary to ensure that those penalties are applied. The penalties thus provided for shall be effective, proportionate and dissuasive. Member States shall notify the relevant provisions to the Commission not later than ... and shall notify any subsequent changes as soon as possible."

For directives:

"Member States shall lay down the system of penalties for breaching the national provisions adopted pursuant to this Directive and shall take all the measures necessary to ensure that those penalties are applied. The penalties thus provided for shall be effective, proportionate and dissuasive. Member States shall notify the relevant provisions to the Commission not later than the date specified in Article ... (deadline for transposal of the Directive) and shall notify any subsequent changes as soon as possible."