REPORT FOR THE HEARING
delivered in Case 162/86 *

I — Facts

1. Council Regulation No 1837/80 of 27 June 1980 on the common organization of the market in sheepmeat and goatmeat (Official Journal 1980, L 183, p. 1) established a common organization of the markets for sheepmeat and goatmeat, with a price system and a trading system for the products listed in Article 1 of the regulation. Initially, the regulation distinguished five regions, the United Kingdom being region 5, and provided for three types of market support mechanism:

(i) an annual premium intended to offset the loss of income suffered by sheepmeat producers in a particular region during a given marketing year;

(ii) intervention measures in the form of aid for private storage and purchases by the intervention agency of certain products;

(iii) a variable slaughter premium for sheepmeat, payable under Article 9 in regions where the intervention measures were not applied. The premium could be paid by the Member States when the prices recorded on the representative markets were below a guide level corresponding to 85% of the basic price. The amount of the premium was to be equal to the difference between the guide level and the market price recorded in the Member States concerned. The necessary measures were to be taken to ensure, in the event of payment of the premium, that an amount equivalent to the premium was charged for the products in question where such products left the territory of the Member State concerned. That amount is generally referred to as 'clawback'.

2. Since region 5 was the only region where the variable slaughter premium was paid, Council Regulation No 871/84 of 31 March 1984 (Official Journal 1984, L 90, p. 35) replaced Article 9 of Regulation No 1837/80 with a new provision allowing the United Kingdom to pay a slaughter premium for sheep in region 5 in so far as it does not apply the provisions concerning intervention measures in the form of purchases by the intervention agencies.

Article 9 (3), as amended, provides that where the premium is paid the Commission is to take the necessary measures to ensure that an amount equivalent to the premium actually granted is charged on all products referred to in Article 1 (a) and (c) of Regulation No 1837/80 (as amended) when they leave the region.

Under Article 9 (4) the Commission, acting in accordance with the procedure laid down in Article 26 of the regulation, is to adopt detailed rules for the application of Article 9. These rules may provide, in particular, for the measures necessary to prevent any

* Language of the Case: English.

disturbance of trade resulting from the application of the premium system.

3. Rules for applying the variable slaughter premium were adopted by Commission Regulation No 2661/80 of 17 October 1980 (Official Journal 1980, L 276, p. 19). That regulation was replaced by Commission Regulation No 1633/84 of 8 June 1984 laying down detailed rules for applying the variable slaughter premium for sheep (Official Journal 1984, L 154, p. 27).

Under Article 1 (2) of the regulation the United Kingdom had the power to determine, subject to the definition given in Article 1 (1), the categories, qualities and weight limits of animals in respect of which the premium was to be payable.

Article 4 (1) of Regulation No 1633/84 provides that for the United Kingdom, the amount to be charged on departure from region 5 of fresh or chilled sheep carcasses (referred to in Article 1 (a) and (c) of Regulation No 1837/80) in respect of which the premium has been paid is to be fixed each week by the Commission at an amount equal to that of the premium fixed for the week during which the departure of the products in question took place.

Article 4 (2) provides for the lodging of security in respect of such products at a level not less than the forecast amount of the premium for the week preceding that during which departure takes place.

Article 4 (3) provides that the amounts applicable to the other products referred to in Article 1 (a) and (c) of Regulation No 1837/80 are to be determined by employing the coefficients referred to in Article 12 (3) and Article 13 (3) of Regulation No 1837/80.

4. By Regulation No 3451/85 of 6 December 1985 amending Regulation No 1633/84 laying down detailed rules for applying the variable slaughter premium for sheep (Official Journal 1985, L 328, p. 23), the Commission amended in particular Article 1 (1) and (2) of Regulation No 1633/84 and added a new paragraph 4 to Article 4 of that regulation.

Article 1 (1), as amended, withdraws the power given to the United Kingdom by Regulation No 1633/84 and itself determines the sheep in respect of which the premium may be paid. Article 1 (2) provides that the premium may not be paid in respect of: (a) rams or carcasses of rams or other male sheep or their carcasses having the characteristics of that of a ram, and (b) ewes or their carcasses. Article 1 (2) (a), however, allowed the United Kingdom to grant the premium in respect of rams or other male sheep or their carcasses exported from region 5.

The new Article 4 (4) is worded as follows:

'In the case of carcasses of animals referred to in Article 1 (2) (b) the amounts referred to in paragraphs 1 and 2 shall be calculated on the basis of a coefficient of 0.5. This coefficient shall be applied without prejudice to the coefficients referred to in paragraph 3.

The Commission shall review the said coefficient forthwith if there is any disruption to intra-Community trade.

Furthermore, the said coefficient shall be reviewed every six months in the light of the development of trade between region 5 and the other regions of the Community and the

trend in prices. Any decision to adjust the said coefficient shall be taken in accordance with the procedure laid down in Article 26 of Regulation (EEC) No 1837/80.'

5. Commission Regulation (EEC) No 9/86 of 3 January 1986 amending Regulation (EEC) No 1633/84 laying down detailed rules for applying the variable slaughter premium for sheep (Official Journal 1986, L 2, p. 14) deleted Article 1 (2) (a) of Regulation No 1633/84 and replaced Article 4 (4) of that regulation with the following new paragraphs (4) and (5):

'(4) For carcasses of animals other than those which may qualify for the premium, the amounts referred to in paragraphs 1 and 2 shall be determined using the following coefficients:

(i) lambs attaining a carcass weight less than or equal to 14 kg: O.10;

(ii) animals referred to in Article 1 (2) (a): 0.5;

(iii) animals referred to in Article 1 (2) (b): 0.5;

(iv) other animals: 0.5.

These coefficients shall be applied without prejudice to the coefficents referred to in paragraph 3.

(5) The Commission shall review these coefficients referred to in Article 4, first indent, forthwith if there is any disturbance in intra-Community trade. Furthermore, the Commission shall review these coefficients every six months in the light of the development of trade between region 5 and the other regions of the Community and the trend in prices. It shall take any decision to adjust these coefficients in accordance with the procedure laid down in Article 26 of Regulation (EEC) No 1837/80.'

6. Since in Great Britain the variable slaughter premium was not generally paid in respect of ewes from 20 October 1980, the date on which Regulation No 1837/80 came into force with regard to the variable premium, until 9 December 1985, the date on which Regulation No 3451/85 came into force, the United Kingdom operated a system of 'special export certification' (SEC). Under the SEC arrangements a variable premium was paid on the exportation of ewes and ewe carcasses, products covered by Article 1 (a) and (c) of Regulation No 1837/80, thus offsetting the 'clawback'. The United Kingdom based that system on its power under Article 1 (2) of Regulation No 2661/80, and subsequently of Regulation No 1633/84, to determine the categories, qualities and weight limits of animals in respect of which the premium was payable.

Regulations Nos 3451/85 and 9/86 put an end to that system, with the effect that rams and ewes and their carcasses were no longer eligible for the variable premium but remained subject to clawback.

7. Livestock Sales Transport Ltd (hereinafter referred to as LST) is a Kent company which exports meat and livestock from the United Kingdom. The producer of the sheepmeat in question was P. M. Johnson & Son (hereinafter referred to as Johnson).

The Intervention Board for Agricultural Produce is responsible in the United Kingdom for collecting clawback payable by exporters upon the exportation of sheepmeat.

8. In February 1986 Johnson sold to LST for exportation certain sheepmeat products which were not eligible for variable slaughter premium, and that meat was duly exported. By invoices dated 12 March 1986 the Intervention Board sought to recover from LST an amount equivalent to the variable slaughter premium which it claimed was due on the consignments exported.

9. LST and Johnson brought proceedings before the High Court of Justice, Queen's Bench Division, arguing that LST was not obliged to pay clawback on the export of the products in question on the ground that the Community provisions relied on by the Intervention Board were invalid.

The plaintiffs in the main proceedings argued essentially that Commission Regulations Nos 3451/85 and 9/86:

(a) are incompatible with the principle of non-discrimination laid down in Article 40 (3) of the EEC Treaty;

(b) are incompatible with the free movement of goods;

(c) were adopted by the Commission without it having competence to do so in accordance with the provisions of Article 9 (3) of Regulation No 1837/80, as amended; and

(d) do not satisfy the requirement of sufficiency of reasons laid down in Article 190 of the EEC Treaty.

10. By an order of 22 May 1986 the High Court of Justice, Queen's Bench Division, decided pursuant to Article 177 of the EEC Treaty to stay the proceedings until the Court of Justice should have given a preliminary ruling on the following question:

'Are Commission Regulations (EEC) No 3451/85 of 6 December 1985 and (EEC) No 9/86 of 3 January 1986, each amending Commission Regulation (EEC) No 1633/84 laying down detailed rules for applying the variable slaughter premium for sheep, invalid in so far as they require 'clawback' pursuant to Article 9 (3) of Council Regulation (EEC) No 1837/80 to be charged in respect of products which are not eligible for variable slaughter premium?'

11. The order of the High Court of Justice was received at the Court Registry on 4 July 1986.

12. In accordance with Article 20 of the Protocol on the Statute of the Court of Justice of the EEC, written observations were submitted on 8 September 1986 by the Commission of the European Communities, represented by D. Grant Lawrence, a member of its Legal Department, on 2 October 1986 by LST and Johnson, the plaintiffs in the main proceedings, represented by C. Holme, of Bracher Son and Miskin, Solicitors, assisted by Stuart Isaacs, barrister, and on 6 October 1986 by the United Kingdom of Great Britain and Northern Ireland, represented by B. E. McHenry of the Treasury Solicitor's Department, assisted by Gerald Barling, barrister.

13. Upon hearing the report of the Judge-Rapporteur and the views of the Advocate General, the Court decided to open the oral procedure without any preparatory inquiry.

It nevertheless requested the Commission to reply in writing to a number of questions; the Commission acceded to that request within the prescribed period.

II — Written observations submitted to the Court

The Commission submits that the reply of the Court should be that consideration of the question submitted has disclosed no factor of such a nature as to affect the validity of Regulations Nos 3451/85 and 9/86.

In its observations the Commission analyses the submissions of the plaintiffs in the main proceedings in so far as they are briefly set out in the decision of the national court, but emphasizes that in these circumstances it is difficult for it to reply in detail to the parties' arguments. It reserves the right to reply at the hearing to the detailed arguments in the observations submitted by LST and Johnson.

The Commission also deplores the fact that the Intervention Board apparently did not submit to the English court any arguments in favour of the validity of the Community legislation and simply concurred in the reference requested by LST and Johnson.

LST, Johnson and the United Kingdom submit that the reply of the Court should be that the regulations in question are invalid in so far as they require the charging of clawback on products which are not eligible for variable slaughter premium.

In addition to its observations, the United Kingdom refers to its pleadings and the documents submitted by it in Case 61/86 *United Kingdom* v *Commission* [1988] ECR 431.

Five main submissions are put forward in the observations, with the exception that the United Kingdom does not allege any breach of the principle prohibiting discrimination;

A — Lack of competence on the part of the Commission

B — Misuse of powers

C — Breach of the principle prohibiting discrimination laid down in the second subparagraph of Article 40 (3) of the EEC Treaty

D — Breach of the fundamental principles of the EEC Treaty with regard to the free movement of goods

E — Breach of Article 190 of the EEC Treaty.

A — *The Commission's lack of competence*

1. LST and Johnson submit that Regulations Nos 3451/85 and 9/86 are invalid in so far as they require the charging of clawback in respect of products which are not eligible for variable slaughter premium; the Commission lacked the competence to make the regulations in question in their present form; it failed to exercise the powers conferred on it by the Council for the implementation of the rules laid down by the Council, in breach of the last indent of Article 155 of the EEC Treaty.

LST and Johnson point out that the provisions of Article 9 (3) of Regulation No 1837/80, amended by Regulation No 871/84, constitute the sole legal basis for the Commission's power to charge clawback. They make it clear that clawback is 'an amount equal to the premium actually

granted'; consequently, where no premium has been 'actually granted', any amount charged by the Commission is not in the nature of 'clawback' and the Commission has no power to charge it. Furthermore, Article 9 (4) of Regulation No 1837/80, as amended, makes it clear that the Commission is only empowered to adopt detailed rules 'for the application of this article'. The meaning of 'clawback' put forward by LST and Johnson is supported by the second recital in the preamble to Regulation No 1837/80, inasmuch as the word 'recover' necessarily implies the payment back of premium which has actually been paid.

They find further support in the judgment of the Court of 15 September 1982 in Case 106/81 *Kind* v *EEC*, [1982] ECR 2885 and the Opinion of the Advocate General, which use the words 'recovering' and 'recovered'; clawback, by its nature, can not embrace a charge in respect of animals not eligible for premium.

LST and Johnson also note that the Council's view in the *Kind* case was that clawback involved the repayment of a financial benefit which had actually been granted.

In the alternative, LST and Johnson argue that in so far as Regulations Nos 3451/85 and 9/86 provide that clawback is to be charged at different rates depending upon the product in question, they are contrary to Article 9 (3) of Regulation No 1837/80, which requires that clawback should be an amount equal to the premium actually granted, since variable slaughter premium is granted at a weekly flat rate.

2. The United Kingdom also submits that the Commission has gone beyond the powers conferred on it by the Council and infringed the last indent of Article 155 of the EEC Treaty.

The United Kingdom states that Article 9 (3) of Regulation No 1837/80, as amended, constitutes the legal basis and defines the exact scope of the 'clawback' mechanism. Clawback is a financial charge designed to recover, on export, an amount of money equivalent to any variable premium 'actually granted' on any of the products in question and its purpose is so far as possible to neutralize any premium granted on a product in Great Britain in the event that such product is exported. It would be unfair to seek to 'recover' a sum of money from a person who has not received it.

According to the United Kingdom, the words 'actually granted', which were specifically added to Article 9 (3) of Regulation No 1837/80 when it was amended by Council Regulation No 871/84, are to be contrasted with the earlier passage 'should the premium referred to in paragraph 1 be paid in region 5 . . .'. The latter is clearly a reference to the general availability of variable premium in that region, whereas the words 'actually granted' can only refer to an actual grant of premium on a particular product. In so far as Commission Regulations Nos 3451/85 and 9/86 purport to provide for clawback on products ineligible for the grant of variable premium those regulations are inconsistent with Article 9 (3) and are invalid.

The United Kingdom considers that its interpretation is supported by additional factors:

(i) In the second recital in the preamble to Regulation No 1837/80 it is stated that 'an amount equivalent to that premium should be recovered'; the word 'recovered' indicates that the regulation is concerned with something which has been paid.

(ii) Similarly, in the context of Council Regulation No 1311/85 of 23 May 1985 on the granting of a premium for the slaughter of certain adult bovine animals in the United Kingdom (Official Journal 1985, L 137, p. 20), clawback applies, despite the use of slightly different wording, only to products on which premium can be paid. As appears from its submissions in the *Kind* case [1982] ECR 2902, it is the Council's view that in this respect there is complete consistency between the sheepmeat legislation and the beef and veal legislation. The United Kingdom does not suggest that the beef and veal scheme is identical to the sheepmeat scheme, but each scheme, in its own manner, makes it quite clear that clawback does not apply to products ineligible for grant of the premium.

(iii) In the United Kingdom's view, there is no suggestion in the judgment or the Opinion of the Advocate General in the *Kind* case that clawback could conceivably operate in respect of animals which did not qualify for the grant of premium. On the contrary, the Court considered that clawback was intended to offset exactly the effects of the slaughter premium. It would be beyond the ability of the Commission or of anyone else to calculate the exact effect of a premium on the prices of products which do not receive that premium, even assuming that it would be possible to establish the existence of any effect. The only basis upon which one could have pretensions to such exactitude in this context would be where one was recovering an amount of money equivalent to an amount which had actually been granted. In the United Kingdom's submission, in the *Kind* case the Court was clearly referring to such a situation. That is confirmed in a passage of the Opinion of the Advocate General which speaks of a simple 'mechanism for recovering' aid and of an 'amount already collected' being 'recovered'.

The United Kingdom goes on to submit that in order to justify the imposition of clawback at varying rates and on non-eligible animals the Commission has been obliged to distort the language of both Article 9 (3) of Regulation No 1837/80, as amended, and the judgment of 5 September 1982 (*Kind*). Even if Council Regulation No 1837/80 did authorize clawback in respect of animals which have never received premium a sliding scale of clawback would be prohibited by the words of the regulation which require the clawback to be an amount equivalent to the premium actually granted. There is only one rate of premium at any given time.

Furthermore, it is difficult realistically to regard the varying rates in question as 'offsetting exactly' the indirect effects (if any) of the premium.

The United Kingdom also points out that the Commission's interpretation creates an internal conflict in the current version of Regulation No 1633/84. Whereas Article 4 (1) provides that the amount to be charged is to be equal to that of the premium, Article 4 (4) provides that only a proportion of that sum is to be charged in respect of non-eligible animals.

3. In the Commission's submission, Article 9 (3) of Regulation No 1837/80, as amended, provides that where variable

premium is actually granted on any product covered by Regulation No 1837/80 the effects of that premium on all products falling within Article 1 (a) and (c) of the regulation must be clawed back when those products leave Great Britain. The words 'actually granted' relate not to the amount of the clawback but to the conditions which must be fulfilled for the clawback to come into operation. The Commission emphasizes that during the brief period between the entry into force of Regulation No 1837/80 and the introduction of the SEC arrangments the United Kingdom charged clawback on all products covered by Article 1 when they left Great Britain, whether or not they had received premium.

The Commission considers that the judgment of 15 September 1982 (*Kind*) confirms its interpretation and that clawback can operate even in respect of animals which have not received the premium. Both the judgment and the Opinion of the Advocate General place considerable emphasis on the need to confine the effects of the variable premium system to the region where that premium is granted. It is naïve to suggest that a premium which is paid on a large proportion of the United Kingdom production of sheepmeat (approximately 85%) has no effect whatsoever on the price of sheepmeat products on which the premium is not paid.

B — *Misuse of powers*

1. LST and Johnson refer in this regard to the summary of the United Kingdom's arguments in Case 61/86 published in Official Journal 1986, C 166, p. 2. They are not in a position to comment on the meetings of the Management Committee for Sheep and Goats or on the first draft of what became Regulation No 3451/85; however, they adopt the arguments of the United Kingdom.

2. The United Kingdom submits that Article 9 (3) of Regulation No 1837/80, as amended, empowers the Commission to take the 'necessary measures' to ensure that premium granted is recovered on the export of the animals in question and that Article 9 (4) of that regulation requires the Commission to adopt detailed rules 'for the application of this article'. The Commission, it says, has used those powers for a different purpose, that is to say, to maintain exports of mutton from region 5 (Great Britain) to region 2 (France) at a particular level in relation to the total quantity of sheepmeat products exported from region 5 to region 2. That is not a lawful use of the power delegated by the Council regulation and is contrary to the last indent of Article 155 of the EEC Treaty. The Commission's intention in adopting the offending provisions is apparent from the minutes of the relevant meetings of the Management Committee for Sheep and Goats and from the first draft of what is now Regulation No 3451/85 (Annexes 7 and 8 to the application in Case 61/86).

At the meeting of the management committee on 4 November 1985 the Commission's representative stated that the proposed legislation included a procedure for revision of the clawback coefficient on exported ewes in the event of the percentage of ewe exports to France in relation to the total percentage of exports of sheepmeat to that Member State 'diverging by 22% (bracket 19.5 to 24.5)'.

The fourth recital in the preamble to the draft Commission regulation referred to a traditional volume of trade from region 5 to region 2, and the corresponding provision in the draft regulation spoke of a bracket of 19.5% to 24.5% of the total quantity of sheepmeat products dispatched from region 5 to region 2.

At a subsequent meeting on 11 November 1985, the Commission's representative indicated that no reference could be made in the legislation to the numerical bracket triggering the review procedure, but confirmed that that was a purely formal modification.

According to the United Kingdom, nothing which the Commission said or did following those meetings indicated that it had changed its initial purpose or its principles of review.

3. The Commission did not deal specifically with this submission in its observations; the decision of the national court does not indicate that any argument was put to it on this point by LST and Johnson.

C — *Breach of the principle prohibiting discrimination laid down in Article 40 (3) of the EEC Treaty*

1. LST and Johnson submit that the charging of clawback on sheepmeat which is not eligible for variable slaughter premium is a breach of the prohibition of discrimination because it treats United Kingdom sheepmeat producers differently from producers in other Member States. Moreover, that difference in treatment is arbitrary and devoid of any adequate justification and is not based on objective criteria. The charging of clawback on products in respect of which premium is not paid results in discrimination against British producers, restricting their ability to export such products to other Member States, because the prices which they obtain from exporters are less than they would obtain if clawback was not payable by the latter.

LST and Johnson emphasize that in both Great Britain and France the market price for mutton is determined by the supply of ewes coming on to the market; the supply of ewes on the market is itself determined by the size of the breeding flock; the size of the breeding flock is determined by the total level of support for sheepmeat and not by the method of support. There is no evidence that the variable slaughter premium method of support for lamb has any influence on the market price for mutton.

LST and Johnson consider that proof of discrimination is to be found in annex 7 to their observations; during the first half of 1986, the market price of lamb was some 11% higher than in the first half of 1985, whereas the market price for ewes was about 2% lower.

2. The United Kingdom has not advanced this submission.

3. The Commission considers that this submission is misconceived. By the very fact that the slaughter premium exists only in Great Britain and not in any other region of the Community, British producers are in an

objectively different situation from producers in other regions. By definition, in regions where no premium is paid there can be no question of neutralizing its effects. The fact that there is no clawback on exports of sheepmeat products from other regions is based on objectively justified grounds and thus is not discriminatory in nature.

D — *Breach of the fundamental principles regarding the free movement of* goods

1. LST and Johnson submit that it is settled law that the provisions of the Treaty on the free movement of goods cannot be derogated from by the Community institutions in the general sector of agriculture except in the most extreme circumstances. They refer in that regard to the submissions of the Commission in the judgment of 16 March 1977 in Case 68/76 *Commission* v *France* [1977] ECR 523 and the judgment of 20 April 1978 in Joined Cases 80 and 81/77 *Commissaires réunis* v *Receveur des douanes* [1978] ECR 927. They submit that in the circumstances of this case the clawback charged in respect of products which are not eligible for variable slaughter premium constitutes a charge having equivalent effect to a customs duty, prohibited under Article 9 (1) of the EEC Treaty, and a measure having equivalent effect to a quantitative restriction on intra-Community trade, prohibited under Articles 30 and 34 of the Treaty. In the alternative, they submit that it constitutes a measure having an effect equivalent to a quantitative restriction.

(a) According to LST and Johnson, the Court's reasoning in paragraph 21 of the judgment of 15 September 1982 (*Kind*) leads to the conclusion that in the circumstances of this case the clawback is a charge having equivalent effect to a customs duty. The decision in *Kind* was based on the fact that the charge was intended to 'offset exactly' the effect of the variable slaughter premium, and the Court was not concerned with the situation where clawback was charged without any premium having been paid.

(b) LST and Johnson submit that the effect, if not the intention, of the charging of clawback on products not eligible for variable slaughter premium is equivalent to that of a quantitative restriction on the exportation of such products from Great Britain to other Member States. The fifth recital in the preamble to Regulation No 3451/85 and Article 4 (5) of Regulation No 1633/84, in its present form, strongly suggest that the intention of the Commission is to use clawback in order to regulate the level of exports of products not eligible for variable slaughter premium. In any event, clawback has had that effect, and over the first seven months of 1986 total United Kingdom exports of mutton to France were 37% lower than their level a year earlier.

2. The United Kingdom makes essentially the same observations. It also emphasizes that it cannot realistically be claimed that the rates of clawback in question offset exactly any alleged effects, which the Commission concedes can only be indirect.

3. The Commission refutes this submission.

(a) The Court has already held in the *Kind* case that the clawback system provided for in Article 9 (3) of Regulation No 1837/80 does not constitute a charge having equi-

valent effect to a customs duty since, in the words of the Court, it is 'in reality intended to offset exactly the effects of the slaughter premium'. In the Commission's view, its regulations comply precisely with the wording of that regulation by charging clawback on sheepmeat products which leave Great Britain at a rate which reflects the exact effect of the premium in each case.

(b) Nor do the provisions on clawback contained in the contested regulations constitute a measure having equivalent effect to a quantitative restriction on exports and imports.

It cannot be deduced from the provisions of Article 1 (2) of Regulation No 3451/85, which added a fourth paragraph to Article 4 of Regulation No 1633/84, and Regulation No 9/86, which replaced the last two subparagraphs of Article 4 (4) with a new Article 4 (5), that they constitute a measure having equivalent effect to a quantitative restriction on exports and imports. They include no undertaking to change the rate of clawback in defined circumstances. The provisions on review should rather be seen as an undertaking by the Commission to keep the whole situation under review in the interests of prudent management of the market.

E — *Infringement of Article 190 of the EEC Treaty*

1. LST and Johnson consider that the Commission has failed to state adequately the reasons on which Regulations Nos 3451/85 and 9/86 are based; those regulations must therefore be annulled on the ground that they are contrary to Article 190 of the EEC Treaty.

Regulation No 3451/85

(a) LST and Johnson point out that in the second recital in the preamble it is stated that a premium granted for the slaughter of lambs automatically has an effect on the prices of other animals of the ovine species, but no reasons are given why such an automatic effect should exist, other than the bland and unsubstantiated assertion that the sheep market is characterized and dominated by the production and marketing of lambs. LST and Johnson contend that it is the market price for lamb which determines the variable slaughter premium and not vice versa. As Annex 9 to their observations shows, changes in the market conditions for lamb can alter the amount of the premium. Since the premium is a support measure designed to stabilize producers' returns rather than the market price for lamb, the statement in the second recital is not tenable.

(b) LST and Johnson go on to point out that in the second recital it is also stated that it has emerged in the past that an additional reduction in the price of sheep other than lambs in Great Britain can cause serious disturbances in trade with the other regions of the Community, in particular in traditional trade with France. That simple assertion does not provide a sufficient reason for the adoption of the regulation.

In their view, there is no evidence that the premium on lamb has caused serious disturbance of the French market for ewes. The growth in the volume of exports of

ewes from Great Britain was a natural consequence of the opening up of the French market. Despite the large reduction in the volume of mutton exports since the entry into force of the contested regulations, prices have fallen on the French market. That confirms that exports from Great Britain have had no significant influence.

LST and Johnson also observe that in both Great Britain and France the market for lamb and the market for other sheep are distinct. Consequently, any reduction in the price of other sheep will not cause any significant disturbance to the market for lambs.

(c) LST and Johnson point out that in the third recital in the preamble it is stated that clawback must be charged even in respect of exported products which do not benefit directly from the variable premium. However, not only is there no necessity for the charging of clawback in such circumstances, the Commission is not empowered to do so, as was observed under heading A above.

In the fourth recital in the preamble it is stated that a coefficient should be introduced for ewes and ewe meat to take account of the benefit indirectly derived in respect of such products from the granting of the variable premiums for lamb. However, the Commission has provided no indications making it possible to determine the existence and extent of the alleged benefit, which is in any event disputed.

Finally, LST and Johnson point out that in the fifth recital in the preamble it is stated that in order to prevent disturbances through artificial trade a coefficient of 0.5 seems appropriate. However, the Commission has provided no evidence of the existence of artificial trade or of disturbances and does not explain why a coefficient of 0.5 seems appropriate.

Regulation No 9/86

LST and Johnson make the same observations, *mutatis mutandis.*

They add that the second recital in the preamble to Regulation No 9/86 states that the 'appropriate' coefficients should be fixed for sheep and sheepmeat other than ewes and their meat and that the third recital refers to the introduction of 'differentiated' coefficients. No justification is given for the assertion that the coefficients introduced by the regulations are appropriate, or for the introduction of coefficients at a non-uniform rate.

2. The United Kingdom considers that a number of important propositions in the preamble to the contested regulations are wholly unsupported by reasons and are inherently implausible in the light of available evidence.

Regulation No 3451/85

(a) According to the United Kingdom, it cannot be accepted that the variable premium for lambs has an automatic effect on the price of mutton, and even if such an effect exists its extent is wholly speculative. It is not even certain that the price of lamb is invariably affected by the payment of the premium. It is perfectly possible to envisage circumstances where prices would remain unchanged on the removal of variable

premium, for it must be remembered that variable premium is not a cumulative subsidy. According to Article 5 (6) of Regulation No 1837/80, as amended, the average amount of variable premium paid must be deducted from the 'loss of income' which is the basis of the annual premium paid to producers. Consequently, if the variable premium were abolished the annual premium would automatically increase by a corresponding amount. The Commission's reference to automatic effects on prices is therefore unacceptable without at least some reasons which would reveal the economic background envisaged.

The United Kingdom adds that it must also be borne in mind that Article 5 of Regulation No 1837/80, as amended by Regulation No 871/84, contains a mechanism intended to ensure that the market support measures are limited to lamb meat by requiring that the amount of the annual premium for ewes should be reduced by a coefficient 'expressing for each region the normal annual production of lamb meat per ewe'.

(b) With regard to the assertion in the second recital concerning serious disturbances in trade, the United Kingdom points out that the Commission does not even indicate whether these disturbances relate to the French market for lamb, for mutton, or both. The United Kingdom was not aware of any such disturbances. The reference to disturbances in trade cannot relate to the situation in 1985, when consignments of United Kingdom sheepmeat products to France decreased in relation to 1984 levels. In 1986, when the level of exports of United Kingdom mutton was reduced by the unlawful clawback, the price of ewes in France fell, which indicates that there was no significant connection between the two factors.

The United Kingdom also refers to Annex 9 to its application in Case 61/86 in support of its assertion that there is no level of trade with France which can legitimately be called 'traditional'. It must be emphasized, moreover, that since 1980 trade in ewes and ewe meat between Great Britain and France has been carried on under the SEC arrangments, that is to say with a variable premium being granted and clawed back at 100%. If that is the traditional trade referred to by the Commission, it is now being distorted by the unwarranted imposition of clawback where no corresponding payment can be made.

If the 'serious disturbances' relate to the market for lambs in France, it should be pointed out that that market is not significantly affected by imports of mutton from Great Britain. The market for lamb and the market for mutton in France are two separate markets, and prices often move in contrary directions. The investigations carried out by the United Kingdom suggest that lamb and mutton are not substitutable to any significant degree.

The United Kingdom considers that any serious disturbances in trade envisaged by the Commission are much more likely to have been the result of exports of sheepmeat products from Ireland.

In those circumstances, the United Kingdom submits that the Commission's failure to identify the serious disturbances and the relevant markets and to explain what is

meant by traditional trade represents a fundamental defect in the legislation.

(c) The United Kingdom also disputes the assertion in the third recital to the effect that clawback must be charged even in respect of exported products which do not benefit directly from variable premium, and refers to its observations regarding the Commission's lack of competence.

The United Kingdom states that the assertion in the fourth recital that ewes and ewe meat benefit indirectly from the grant of variable premium on lambs cannot be accepted as an obvious truth; it is therefore incumbent upon the Commission to indicate the extent of the alleged benefit and how it arises. Moreover, if there is an indirect advantage, that advantage is indirectly removed when clawback is applied on the export of the lambs. To apply in addition a direct clawback on ineligible animals involves a form of double recovery which is itself a distortion of trade.

With regard to the assertion in the fifth recital to the effect that a 50% coefficient is appropriate in order to prevent disturbances through artificial trade between region 5 and other regions of the Community, the United Kingdom considers that the Commission's reasoning is deficient in the following important respects:

(i) The Commission does not explain why, when there have been no disturbances or artificial trade, it should suddenly become necessary to impose a financial charge on certain exports while at the same time disqualifying the products in question from entitlement to the corresponding premium.

(ii) The Commission gives no indication whatsoever of the basis for its view that a 50% clawback on animals ineligible for the premium is appropriate. In fact the rate was chosen completely at random, and that coefficient cannot correspond 'exactly' or even approximately to any alleged indirect benefits.

(iii) The Commission does not state the criteria to be applied in reviewing the coefficient.

Regulation No 9/86

According to the United Kingdom, its remarks concerning insufficient reasoning apply equally, *mutatis mutandis*, to Regulation No 9/86; in particular, the imposition of differential rates of clawback without explanation is unacceptable.

3. The Commission denies that the statements of reasons are insufficient.

(a) The Commission points out that in Great Britain producers of ewes and producers of lambs are not two separate and distinct categories. In the vast majority of cases a producer raises both lambs and ewes. The lambs are sold for meat and the ewes are used for breeding and later sold. The amount which a producer derives from the sale of both categories of animals is a function of the total price which he can receive for the two categories, and his income depends on his total production of lambs and ewes. If a substantial part of his production (that is to say, the lambs) did not receive a subsidy in the form of a premium, the producer would seek to protect his total income by increasing his

prices. That is quite clear from the fact that variable premium can account for up to 40% of a producer's total return. If that large and valuable part of his income were removed it is clear that, in economic terms, the producer would seek to increase his income by increasing the prices of all his products and not simply those of lambs. Thus the removal of variable slaughter premium on lambs would also have an effect on ewes.

The Commission adds that the second recital in the preamble to Regulation No 3451/85 emphasizes the importance of lamb production.

(b) The Commission points out that pursuant to Article 9 (4) of Regulation No 1837/80, as amended, it is under a duty to take the measures necessary to prevent any disturbance of trade resulting from the application of the variable premium, and that in 1985 exports of sheepmeat from Great Britain to France were increasing, two-thirds of that increase being accounted for by an increase in exports of ewes.

According to the Commission, ewes, which represent only 15% of United Kingdom sheepmeat production, were accounting for a much larger percentage of total sheepmeat exports from Great Britain to France, and that proportion was increasing; ewes were thus being disposed of to a large extent not on the domestic market but on the market of another Member State. The Commission considers that that situation constituted a disturbance of trade within the meaning of Article 9 (3). Field studies undertaken by the Commission's staff in France, it says, showed that consignments of sheepmeat from Great Britain consisted usually of a mixture of lamb and ewe meat. Certain of the better cuts of ewe meat were put on sale alongside equivalent cuts of domestic French lamb. Apart, perhaps, from colour, the cuts were strikingly similar, except that the British ewe meat was considerably cheaper, a fact which proved attractive for the French consumer. The effect was thus not on the mutton market in France but on the lamb market.

The Commission considers that the action taken by it has remedied that situation. There has been no disastrous fall in the price of ewes on the United Kingdom domestic market; prices have remained firm and have in fact continued to increase. The level of exports of ewes from Great Britain to France has of course fallen, but that fall has not been disastrous, and exports are about 50% of the high level of the previous year.

(c) With regard to the charging of clawback on products in respect of which premium has not been paid, the Commission refers to its observations concerning its alleged lack of competence.

With regard to the rate of 50%, the Commission observes that in late 1985 it was increasingly concerned by what it considered to be the serious disturbance of trade between Great Britain and France, and in those circumstances Article 9 (4) of Regulation No 1837/80, as amended, obliged it to intervene. In an attempt to

resolve the problem the Commission was faced with differing and often conflicting assertions by the Member States. Faced with a difficult situation in a very complicated market the Commission considers that it acted as a prudent manager of the market, and it is satisfied that subsequent events confirm that it made the correct decision. Even so, it included in the regulations wide review clauses to ensure that the figure of 50% could be reviewed and corrected if necessary. In the event, trade has stabilized and a review has not been necessary.

III — Replies to the questions put by the Court

1. The Commission was requested to submit to the Court the date on the basis of which it fixed the coefficients laid down in Regulation No 9/86. The Commission explains that at the relevant time it was concerned by the distortions taking place on the market in sheepmeat, the scope of which is indicated by the statistics produced during the written procedure. Since the solutions proposed by the States principally concerned were diametrically opposed, the Commission, after studying the problem on the spot in France, preferred to adopt an intermediate solution and to include wide review clauses in its decision. In the event the Commission's approach was vindicated and no modification has been considered necessary.

2. The Commission was requested to submit to the Court the data which led it to maintain in its defence that the slaughter premium for lambs accounts for 40% of the income of sheep producers and to admit in its rejoinder that it varies between 29 and 35% from year to year. It was also requested to explain how those figures could lead to the same result, namely the fixing of the coefficients laid down in Regulation No 9/86. The Commission replied that a distinction must be drawn between the average figure which could amount to up to 35% and the actual maximum figure which could reach 40%. What is important for producers is not the average figure but the actual figure on sale since most producers specialize in supplying a specific market, for example the spring market, the Easter market or the summer market.

3. The Commission was requested to state whether or not, during the period in question, there were disturbances in trade which led it to adopt the contested regulations. It explains that faced with the problems experienced by the market in sheepmeat at the relevant time it proceeded in two steps; since ewe meat clearly posed the more serious problem, it began by dealing with that before turning to other products. If it had dealt with all products at once the economic realities would have become distorted.

4. The Commission was requested to state in what manner the recitals in the preambles to the contested regulations take account of the points raised in the Court's first, second and third questions. The Commission replied that the fifth recital in the preamble to Regulation No 3451/85 sets out the factors which led the Commission to fix the coefficient for ewe meat. The sixth recital refers to the circumstances in which the

coefficients for other products will be fixed. The first two recitals in the preamble to Regulation No 9/86 refer to the procedure followed in fixing the various coefficients.

The second recital in Regulation No 3451/85 refers to the effect of the premium on the price of animals which do not benefit from the premium and to the serious disturbances in trade. Since the aim of Regulation No 9/86 is merely to complete the task begun by Regulation No 3451/85 it is the latter to which reference is made in the second recital in Regulation No 9/86.

F. Schockweiler
Judge-Rapporteur