Changes in Competition Policy Over the Last Two Decades

UOKiK 1990 2010

20 years of the Office of Competition and Consumer Protection

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Edited by Dr Małgorzata Krasnodębska-Tomkiel

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This publication marks the 20th anniversary
of the Polish Office of Competition and Consumer Protection

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Plac Powstańców Warszawy 1

00-950 Warsaw, Poland

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FOREWORD

The events of 1989, when for the first time in almost half a century the people of Poland had the possibility to independently determine their future, initiated the process of economic transformation in this country. The introduction of the free market entailed a number of legislative changes. Among the legal acts laying down the foundations for the new system there was also the Act on counteracting monopolistic practices - the legal basis for the establishment of the Antimonopoly Office. Starting its operations in 1990, the new institution was not only to ensure that the newly obtained economic freedom does not evolve into anarchy, but also to shape the scope of this freedom. Therefore, apart from the responsibilities regarding counteracting monopolistic practices, the Office was also given the power to influence the structure of the economy by exercising control over the restructuring processes of enterprises.

In the following years, the responsibilities of the authority were repeatedly increased and its priorities changed. In 1996, the Office received its present name - the Office of Competition and Consumer Protection - and since then has also been protecting the interests of non-professional market participants. Another significant change took place in 1999 when the Office started monitoring State aid. 1st May 2004, the day of Polish accession to the European Union, was a turning point, although Polish competition and consumer protection law had been harmonised with the Community regulations much earlier.

Within the last 20 years, for many reasons, the operations of competition agencies all over the world have undergone significant changes. This was mainly the result of the progressing globalization and dynamic technological development. Instruments used by the institutions to protect competition as well as respective legal provisions needed to evolve in parallel with the changing realities. This publication attempts to take a closer look at these changes. It is an exceptional platform bringing together voices of the leading figures in competition protection in Poland and internationally: heads of competition offices, representatives of international organizations, judges, economists and lawyers.

The publication is divided into four parts. The first section is dedicated to competition policy and seeks to find out why efficient competition is the basis for a proper functioning and development of the market economy. The next two chapters concern merger control and State aid. These are the only cases when competition authorities respond ex-ante – before any distortion of competition occurs. The final part of the book covers challenges standing before competition policy. The continuously growing importance of information technology in social relations and economy has reshaped the way that enterprises operate now. Both their organisation and the way they operate on the market are determined to a growing extent by new technologies and high-tech means of communication. Competition authorities have to respond to these changes.

Importantly, many papers in the publication are dedicated to competition policy in the time of crisis. This is fully justified as many economies are still struggling with the effects of the current economic downturn.

Concluding, I would like to express my gratitude to all the authors for devoting their time and energy to prepare articles for this publication and thus mark the 20th anniversary of the Office of Competition and Consumer Protection. I hope you will enjoy the book.

Małgorzata Krasnodębska-Tomkiel

President of the Office of Competition and Consumer Protection

Chapter I

COMPETITION-RESTRICTING PRACTICES

Scott Hammond and Ann O'Brien

THE EVOLUTION OF CARTEL ENFORCEMENT OVER THE LAST TWO DECADES: THE U.S. PERSPECTIVE

1. INTRODUCTION

In 1990, the sanctions in cartel cases brought by the Antitrust Division of the U.S. Department of Justice were not sufficiently severe and the original Corporate Leniency Program was simply not producing cases. Two decades later, the landscape has dramatically changed in cartel enforcement in the United States and around the globe. The world has seen the proliferation of effective leniency programs, ever-increasing sanctions for cartel offenses, a growing movement to hold individuals criminally accountable, and increased international cooperation among enforcers in cartel investigations.

The Antitrust Division has spent the last two decades building and implementing a "carrot and stick" enforcement strategy by coupling rewards for voluntary disclosure and timely cooperation pursuant to the Corporate Leniency Program with severe sanctions. In addition, the Antitrust Division utilizes all available investigatory tools to create a significant risk and fear of detection and prosecution for violators of U.S. antitrust laws. The seeds of this "carrot and stick" enforcement strategy were planted by the Antitrust Division in the mid-1990s and began to bear fruit over the next decade. Since the mid-1990, the Antitrust Division has uncovered and prosecuted dozens of international cartels, secured convictions and jail sentences against culpable U.S. and foreign executives, and obtained hefty corporate fines. In recent years, competition enforcers around the world have intensified their cartel enforcement efforts and achieved similar results. For instance, Poland's Office of Competition and Consumer Protection has seen its leniency program flourish and recently produced record fines of almost 100 million euros imposed upon cement producers for their cartel conduct.

This paper will trace the evolution of cartel enforcement over the last two decades, highlighting U.S. milestones and achievements critical to the current success of cartel enforcement programs around the world.

2. THE CARROT: PROLIFERATION OF EFFECTIVE CORPORATE LENIENCY PROGRAMS

Number of Jurisdictions with Leniency Programs	
1990	Today
1	50+

The single most significant development in cartel enforcement is the proliferation of effective leniency programs.[1] The advent of leniency programs has completely transformed the way competition authorities around the world detect, investigate, and deter cartels. Cartels by their nature are secretive and, therefore, hard to detect. Leniency programs provide enforcers with an investigative tool to uncover cartels that may have otherwise gone undetected and continued to harm consumers. While the notion of letting hard core cartel participants escape punishment was initially unsettling to many prosecutors, the Antitrust Division recognized that the grant of full immunity was necessary to induce cartel participants to turn on each other and self-report, resulting in the discovery and termination of the conduct, the successful prosecution of the remaining cartel participants, and damage recovery for victims. Moreover, the hope was that the benefits of leniency would extend beyond the cartels it directly uncovered and that the very existence of the leniency policy would be viewed by executives as raising the risk of detection and punishment, leading to greater deterrence of cartel activity.

The original version of the U.S. Corporate Leniency Program dates back to 1978. However, the original Corporate Leniency Programas was rarely utilized and the Antitrust Division received on average only about one leniency application per year. No leniency application made under the original program resulted in the detection of an international or large domestic cartel. In August 1993, the Antitrust Division revised its Corporate Leniency Program to make it easier and more attractive for companies to come forward and cooperate with the Antitrust Division.[2] Three major revisions were made to the program: (1) leniency is automatic for qualifying companies if there is no pre-existing investigation;

1 In the United States, the terms corporate "immunity", "leniency" and "amnesty" are all synonymous and refer to a complete pass from criminal prosecution for a company and its cooperating employees. Under the U.S. Corporate Leniency Program, only one company can qualify. In other jurisdictions, including the E.U., leniency programs offer a 100 percent reduction from fines (referred to as "full immunity") and also offer cooperating companies that do not win the race for full immunity the possibility of a fine reduction (referred to as "leniency"). For purposes of this paper, "leniency" refers to full immunity.

2 Antitrust Division, U.S. Department of Justice, *Corporate Leniency Policy* (1993), available at http://www.justice.gov/atr/public/guidelines/0091.htm.

(2) leniency may still be available even if cooperation begins after the investigation is underway; and (3) all officers, directors, and employees who come forward with the company and cooperate are protected from criminal prosecution.[3]

These revisions made the program more transparent and raised the incentives for companies to report criminal activity and cooperate with the Antitrust Division. As a result of these changes, the Antitrust Division has seen a nearly twenty-fold increase in the leniency application rate, making the Leniency Program the Antitrust Division's most effective investigative tool. Leniency programs provide unparalleled information from cartel insiders about the origins and inter-workings of secretive cartels. In the United States, companies have been fined more than 5 billion dollars for antitrust crimes since Fiscal Year 1996, with over 90 percent of this total tied to investigations assisted by leniency applicants. The Antitrust Division typically has approximately 50 international cartel investigations open at a time, and more than half of these investigations were initiated, or are being advanced by information received from a leniency applicant.

The success of the Antitrust Division's revised leniency program led to the adoption of similar voluntary disclosure programs by other jurisdictions. For example, Canada had some form of leniency in place since 1991 and the European Commission's first leniency notice was adopted in 1996. However, these programs, like the Antitrust Division's pre-1993 leniency program, lacked sufficient transparency and predictability to effectively induce self-reporting. When Canada issued its Immunity Bulletin in 2000 and the European Commission issued its revised Leniency Notice in 2002, the corporate leniency programs of the United States, the European Union and Canada came into substantial convergence.[4]

3 For a fuller discussion of these changes and the application of the Division's Corporate Leniency Policy, see *Frequently Asked Questions Regarding the Antitrust Division's Leniency Program and Model Leniency Letters*, by Scott D. Hammond and Belinda Barnett (November 19, 2008), available at, http://www.justice.gov/atr/public/criminal/239583.htm; see also "Cornerstones of an Effective Leniency Program", speech by Scott D. Hammond, before the ICN Workshop on Leniency Programs (Nov. 22-23, 2004), available at http://www.justice.gov/atr/public/speeches/206611.htm; "When Calculating the Costs and Benefits of Applying for Corporate Amnesty, How Do You Put a Price Tag on an Individual's Freedom?", speech by Scott D. Hammond, Fifteenth Annual National Institute On White Collar Crime (March 8, 2001), available at http://www.justice.gov/atr/public/speeches/7647.htm; "Detecting And Deterring Cartel Activity Through An Effective Leniency Program", speech by Scott D. Hammond, before International Workshop on Cartels (November 21-22, 2000), available at http://www.justice.gov/atr/public/speeches/9928.htm; "Making Companies An Offer They Shouldn't Refuse", speech by Gary R. Spratling, before Bar Association of the District of Columbia's 35th Annual Symposium on Associations and Antitrust (February 16, 1999), available at http://www.justice.gov/atr/public/speeches/2247.htm; "The Corporate Leniency Policy: Answers To Recurring Questions", speech by Gary R. Spratling, before ABA Antitrust Section 1998 Spring Meeting (April 1, 1998), available at http://www.justice.gov/atr/public/speeches/1626.htm.

4 Canada subsequently revised its immunity program in 2007, available at http://competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/h_02000.html, and issued a revised draft bulletin on leniency for those ineligible for immunity in 2009, available at http://competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/03027.html. The European Commission again revised its leniency program in 2006, available at http://ec.europa.eu/competition/cartels/legislation/leniency_legislation.html.

The convergence in leniency programs has made it much easier and far more attractive for companies to simultaneously seek and obtain leniency in the United States, Europe, Canada, and in a growing list of other jurisdictions where the applicants have exposure. In the last decade, many other jurisdictions around the world have implemented leniency programs and today over 50 jurisdictions, including Poland, have leniency programs in place. Leniency programs have led to the detection and dismantling of the largest global cartels ever prosecuted and resulted in record-breaking fines in Australia, Brazil, Canada, the European Union, Japan, Korea, Poland, the United Kingdom, the United States, and other jurisdictions.

Effective leniency programs create a race among conspirators to disclose their conduct to enforcers, in some instances even before an investigation has begun, and quickly crack cartels that may have otherwise gone undetected. However, simply creating a leniency program does not ensure that it will be *effective*. The business community and the private bar must have confidence in a leniency program or there will be no race to the enforcer's door to take advantage of it. There are three essential cornerstones that must be in place before a jurisdiction can successfully implement a leniency program. First, the jurisdiction's antitrust laws must provide the threat of severe sanctions for those who participate in hard core cartel activity and fail to self-report. Second, organizations must perceive a high risk of detection by competition authorities if they do not self-report. Third, there must be transparency and predictability to the greatest extent possible throughout a jurisdiction's cartel enforcement program, so that companies can predict with a high degree of certainty how they will be treated if they seek leniency, and what the consequences will be if they do not.[5] These three major cornerstones – severe sanctions, heightened fear of detection, and transparency in enforcement policies – are the indispensable components of every effective leniency program.

Effective leniency programs destabilize cartels. If cartel members have a significant fear of detection and the consequences of getting caught are too severe, then the rewards of self-reporting become too important to risk losing the race for leniency to another cartel member, or perhaps to its own employee if individual leniency is available. The dynamic literally creates a race to be the first to the prosecutor's office.

5 For a fuller discussion, see "Cornerstones of an Effective Leniency Program", speech by Scott D. Hammond, before the ICN Workshop on Leniency Programs (Nov. 22-23, 2004), available at http://www.justice.gov/atr/public/speeches/206611.htm.

Consider the "empty seat at the table" scenario. Five members of a cartel are scheduled to hold an emergency meeting, but when the meeting starts there is an empty seat at the table. One of the conspirators has unexpectedly not arrived at the meeting and is not returning phone calls. The cartel members at the meeting start to get nervous. Has the missing cartel member had a change of heart and abandoned the cartel? Has he already reported the others to the government? Or did he just miss his plane? In this environment, with the risk of detection and resulting sanctions so high, who can you trust? Each member of a cartel knows that any one of its co-conspirators can report the others in exchange for total immunity – a decision that will seal their fate. Imagine the vulnerability of cartel members in that position asking, "Can I really trust my competitors to look out for my best interests?" The answer to this question leads them directly to the prosecutor's door.

3. THE STICK: MOVEMENT TOWARD SEVERE SANCTIONS, INCLUDING INDIVIDUAL ACCOUNTABILITY

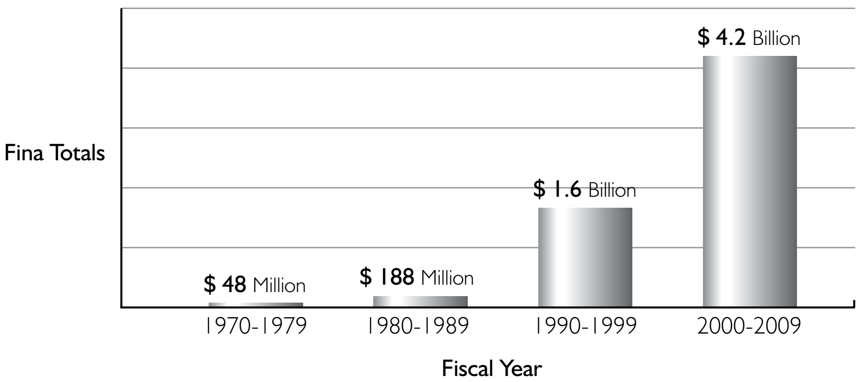
If the potential penalties that can be imposed upon cartel participants are not perceived as outweighing the potential rewards of participating in a cartel, then the fine imposed becomes merely part of the cost of doing business. The Antitrust Division has steadfastly emphasized the importance of individual accountability and stiff corporate fines to induce leniency applications and optimize deterrence of cartel conduct.

Over the last three decades, sanctions imposed in cartel cases brought by the Antitrust Division have increased exponentially. This increase is attributable to a number of factors, including increases in maximum penalties for antitrust crimes,[6] the Antitrust Division's reallocation of resources to focus on international cases involving larger volumes of commerce, the change in perception by judges as to the seriousness of antitrust crimes, and the increase in leniency applications.

6 In 1974 criminal violations of the Sherman Act became a felony with a maximum three-year term of imprisonment and fine maximums of $1 million for corporations and $100,000 for individual defendants. The statutory maximum jail time was unchanged for three decades, but fine levels were increased twice between 1974 and 2004. The maximum individual fine for criminal Sherman Act violations was increased to $250,000 in 1984, through a combination of the Omnibus Crime Control of 1984 and the Criminal Fines Enforcement Act of 1984, and the maximum corporate fine remained 1 million dollars. In 1990, the Sherman Act was amended to raise the maximum fines to 10 million dollars for corporations and 350,000 dollars for individuals. In addition, since 1984, fines in excess of the statutory maximum may be imposed pursuant to 18 U.S.C. § 3571(d), which provides for a fine of up to twice the gain derived by, or twice the loss caused by, the cartel. Recognizing the rising threat to U.S. businesses and consumers caused by cartels, in June 2004, Congress significantly raised the maximum penalties for criminal Sherman Act violations increasing the statutory maximum corporate fine to 100 million dollars, the statutory maximum individual fine to 1 million dollars, and the maximum jail term to 10 years.

These factors came together in the 1990s to produce record fines, and this trend has continued in the 21st Century.

Criminal Antitrust Corporate Fines By Decade



The Antitrust Division's sentencing statistics over the last two decades show a steady trend toward higher corporate fines for cartel offenses and longer jail sentences for individuals. For example, in Fiscal Year 1991 the average corporate fine for an antitrust offense in the United States was a little less than 320,000 dollars and the largest corporate fine ever imposed for a single Sherman Act count was 2 million dollars.[7] In the mid-1990's the amount of corporate fines began to grow steadily, with multimillion dollar fines becoming more commonplace.[8] In 1996, corporate fines reached a new order of magnitude when the Archer Daniels Midland Company ("ADM") paid a 100 million dollar fine for its participation in two international antitrust conspiracies (lysine and citric acid) in the food and feed additives industry. Then-Deputy Assistant Attorney General of the Antitrust Division Gary Spratling predicted that the historic ADM fine was not an aberration, and that we would see more corporate fines above $100 million dollars.[9] This prediction quickly proved to be accurate. In April 1998, UCAR International agreed to pay a 110 million dollar fine for its participation in the graphite electrodes conspiracy and in 1999, SGL agreed to pay a $135 million dollar fine for its role in the graphite electrodes conspiracy. These record fines

7 See "The Trend Towards Higher Corporate Fines: It's A Whole New Ball Game", speech by Gary R. Spratling, Deputy Assistant Attorney General, Antitrust Division, before ABA National Institute On White Collar Crime (March 7, 1997), available at http://www.justice.gov/atr/public/speeches/4011.htm.

8 See id.

9 See id.

were quickly eclipsed in May 1999 when the worldwide vitamin cartel was exposed and pharmaceutical giant F. Hoffmann-La Roche Ltd agreed to plead guilty and pay a record 500 million dollar criminal fine for leading the conspiracy and BASF AG agreed to pay a 225 million dollar fine for its role.

The ADM fine truly was the tip of the iceberg for large corporate antitrust fines. The Antitrust Division's record of cracking large international cartels affecting huge amounts of commerce and obtaining nine-figure fines has continued in the new millennium with the Antitrust Division's prosecutions of cartels in the air transportation (more than 1.6 billion dollars in criminal fines obtained to date), liquid crystal display (more than 860 million dollars in criminal fines obtained to date), and dynamic random access memory (more than 730 million dollars in criminal fines obtained to date) industries, among others. To date, the Antitrust Division has obtained 18 fines above 100 million dollars[10] and this trend shows no signs of decline, with the Antitrust Division obtaining just over 1 billion dollars in fines in Fiscal Year 2009.

Other jurisdictions, most notably the European Union, have also steadily raised fines over the last two decades and imposed increasingly large penalties against cartel participants. Before 1990, the highest cartel fines imposed in Europe were fines totaling 60 million ECU on 23 petrochemical producers for price fixing in the plastic industry.[11] Since 2006, the European Commission has imposed more than

10 See Sherman Act Violations Yielding a Corporate Fine of $10 Million or More, available at http://www.justice.gov/atr/public/criminal/sherman10.htm.

11 Press Release, European Commission, Commission Imposes Heavy Fines On Cartels In The Plastic Sector (December 21, 1988),

1 billion euros in cartel fines per year, reaching a high of over 3 billion euros in 2007.[12] In December 2008, the Commission imposed its largest fines ever, ordering four car glass manufacturers to pay a combined total of more than 1.3 billion euros. Recently, Poland's Office of Competition and Consumer Protection levied record fines totaling almost 100 million euros on seven cement companies for price fixing in the construction industry.[13]

4. INDIVIDUAL ACCOUNTABILITY

The Antitrust Division's detection and prosecution of the worldwide vitamin cartel was important not only because it resulted in record fines, but because for the first time a foreign executive agreed to serve time in U.S. prison for his participation in an international cartel. The historic plea agreement the Antitrust Division entered into in May 1999 with a Swiss vitamin executive was the first that called for the imposition of jail time for a foreign national who had participated in an international cartel.[14] This plea agreement marked a watershed in the Antitrust Division's prosecution of international cartels. Before the filing of this case, foreign defendants prosecuted for their participation in international cartels, such as the lysine and citric acid cartels, had plead guilty but the Division did not seek a jail sentence in return for their admission of guilt, cooperation, and submission to U.S. jurisdiction. However, by 1999, the Antitrust Division's ability to successfully investigate and prosecute foreign nationals who violate U.S. antitrust laws had significantly advanced, with enhanced investigative tools and increased international cooperation. Thus, "no-jail" deals became a relic of the past.[15] Since May 1999, more than 40 foreign defendants have served, or are serving, prison sentences in the United States for participating in an international cartel or for obstructing an investigation of an international cartel. Foreign nationals from France, Germany, Japan, Korea, Norway, the Netherlands, Sweden, Switzerland, Taiwan and the United Kingdom are among those defendants.

available at http://europa.eu/rapid/pressReleasesAction.do?reference=IP/88/852&format=HTML&aged=0&language=EN&guiLanguage=en.

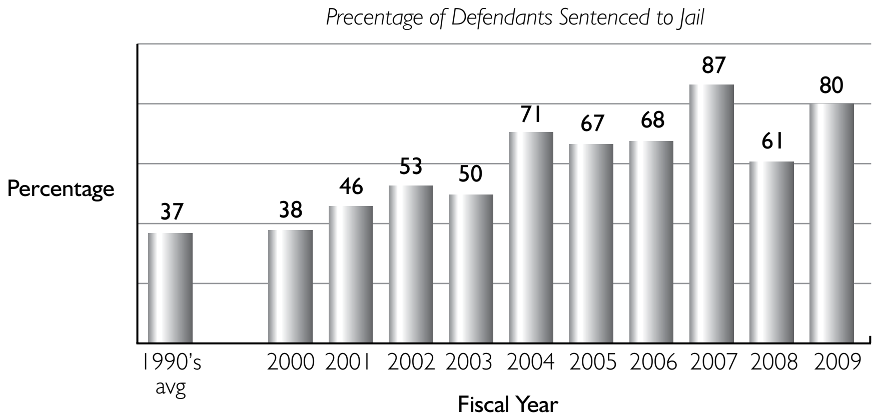
12 See EU cartel fine statistics (updated October 2009), available at http://ec.europa.eu/competition/cartels/statistics/statistics.pdf.

13 Press Release, Office of Competition and Consumer Protection, Cement cartel smashed (December 10, 2009), *available at* http://www.uokik.gov.pl/news.php?news_id=1768.

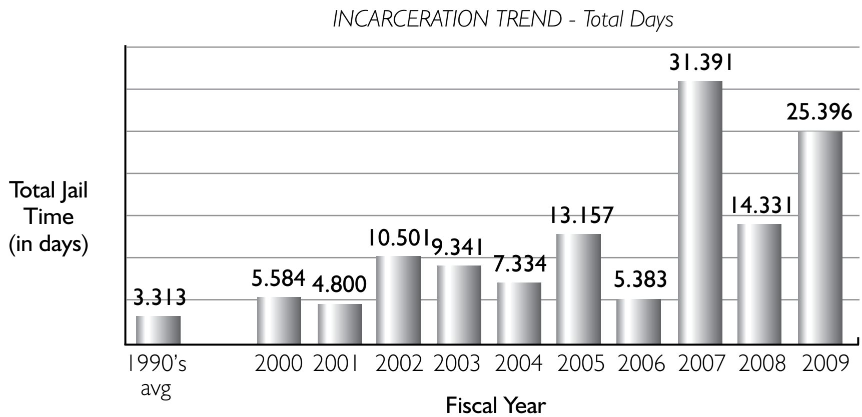
14 Plea Agreement at 7-8, United States v. Sommer, Crim. No. 3:99-CR-201-R (N.D. Tex. 1999), available at http://www.justice.gov/atr/cases/f2400/sommer.pdf.

15 See Scott D. Hammond, "Charting New Waters in International Cartel Prosecutions", speech before the ABA Criminal Justice Section's Twentieth Annual National Institute on White Collar Crime (March 2, 2006), available at http://www.justice.gov/atr/public/speeches/214861.htm.

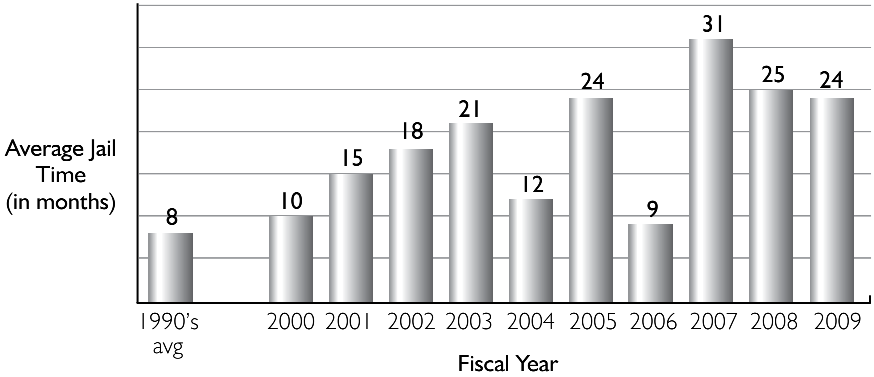
During the last decade, the Antitrust Division has made increased individual accountability a critical piece of its cartel enforcement program and the Antitrust Division's enforcement statistics demonstrate that individuals who violate U.S. antitrust laws are being sent to jail with increasing frequency and for longer periods of time. Since 2000, the Antitrust Division has seen a steady increase in the percentage of defendants sentenced to jail.



In addition, over the last decade the Antitrust Division has obtained successively greater jail sentences and set new deterrent marks, including the highest number of total jail days imposed in a fiscal year (31,391 in 2007) and the highest average jail sentence for all defendants in a fiscal year (31 months in 2007).



INCARCERATION TREND - Average Months



Consistent with the Antitrust Division's emphasis on promoting deterrence through individual accountability, the Antitrust Division also began prosecuting more culpable individuals from each corporate defendant. In the Antitrust Division's prosecutions of international cartels in the mid-1990s, it was typical for the Antitrust Division to prosecute only the single most culpable employee from each foreign company prosecuted. However, beginning in 1999 with the prosecution of six foreign executives from F. Hoffmann-La Roche and BASF for their participation in the vitamin cartel, the Antitrust Division began a policy of greater accountability for culpable executives. During the last decade, the Antitrust Division has routinely prosecuted multiple individuals from each corporate defendant, and over time, the Antitrust Division has tended to prosecute greater numbers of individuals from each corporate defendant.[16]

The prosecution of the vitamin cartel was also important because it helped trigger a rethinking of the adequacy of competition laws around the world. The vitamin cartel was one of the most pervasive and harmful ever prosecuted by the Antitrust Division. The cartel was so sophisticated that its members were able to carve up the world's billion-dollar vitamin market among a few multi-national companies and fix prices on a country-by-country basis around the globe for nearly ten years.

16 For example, in the rubber chemicals investigation, Crompton, which began to cooperate within days after the issuance of grand jury subpoenas, had three individuals carved out from its plea agreement. The next company to plead in that investigation, Bayer, had five individuals carved out of its plea agreement. A similar crescendo occurred in our DRAM investigation: Infineon had four individuals carved out of its plea agreement; Hynix had five carve outs; and Samsung had seven. For a fuller discussion of the Division's carve-out policies see "Charting New Waters in International Cartel Prosecutions", speech by Scott D. Hammond before the ABA Criminal Justice Section's Twentieth Annual National Institute on White Collar Crime (March 2, 2006), available at http://www.justice.gov/atr/public/speeches/214861.htm.

The vitamin cartel operated with such precision and profit that it was called "Vitamins, Inc." by its members. The cartel impacted products that appeared not only in the cupboards of Americans, but also worldwide.

The high-profile nature of the vitamin cartel and the nearly billion dollars in fines imposed against the vitamin cartel members in the United States[17] grabbed the attention of the foreign press, as well as foreign businesses and consumers. Many foreign business and consumer groups then began asking whether their governments would be acting to protect their interests against cartel behavior. The vitamin cases helped fuel a movement to rethink the adequacy of competition laws and law enforcement powers that was already beginning to take place in many governments abroad as a result of the lysine and citric acid conspiracies. These governments began to consider whether they had sufficient penalties in place to deter cartel activity; whether cartel activity should be treated as an administrative or a criminal offense; and whether individuals as well as corporations should be sanctioned for cartel offenses. Twelve individuals, including six European executives, were sentenced to serve time in U.S. prisons for their role in the vitamin conspiracy. Ultimately, other jurisdictions including Canada, the European Union, Australia, and Korea imposed then-record fines against participants in the vitamin cartel,[18] but no cartel member served a single day in jail outside the United States.

The Antitrust Division has long emphasized that the most effective way to deter and punish cartel activity is to hold culpable individuals accountable by seeking jail sentences.[19] That view is now gathering momentum around the world. In 2008,

17 For a listing of corporate fines imposed against corporate vitamin cartel participants, see Antitrust Division Sherman Act Violations Yielding a Corporate Fine of $10 Million or More, available at http://www.justice.gov/atr/public/criminal/sherman10.htm.

18 On September 22, 1999, Canada announced then-record criminal fines totaling $88.4 million against four participants in the vitamins cartel, see Press Release, Canadian Competition Bureau, Federal Court Imposes Fines Totalling $88.4 Million For International Vitamin Conspiracies (September 22, 1999), available at http://competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/00607.html; in December 2000, the Australian Competition and Consumer Commission announced that it was seeking then-record penalties of $26 million against three international vitamins suppliers for price fixing, see Press Release, Australian Competition and Consumer Commission, Court hearing on vitamins price-fix case: ACCC seeks record $26M penalty against international vitamin suppliers (December 5, 2000), available at http://www.accc.gov.au/content/index.phtml/itemId/87582/fromItemId/378010; in November 2001, the European Commission imposed then-record fines totaling € 855.22 million against eight companies for their participation in the vitamins cartel, see Press Release, European Commission, Commission imposes fines on vitamin cartels (November 21, 2001), available at http://europa.eu/rapid/pressReleasesAction.do?reference=IP/01/1625&format=HTML&aged=0&language=EN&guiLanguage=en; on April 18, 2003, the Korean Fair Trade Commission announced that it had imposed administrative fines totaling 3,916 million Won on six vitamin manufacturers for their participation in the vitamins cartel, see Korea Fair Trade Commission, KFTC News, Investigation results of the international cartel of 6 vitamin companies (April 29, 2003), available at http://eng.ftc.go.kr/files/bbs/2008/news04.doc.

19 For more information on Division policies and initiatives directed toward the prosecution of individual offenders, see "Charting New Waters in International Cartel Prosecutions", speech by Scott D. Hammond before the ABA Criminal Justice Section's Twentieth Annual National Institute on White Collar Crime (March 2, 2006), available at http://www.justice.gov/atr/public/

three executives were sentenced to lengthy jail terms in the United Kingdom for their participation in the marine hose conspiracy, marking the first jail sentences for a cartel offense under the 2002 Enterprise Act. In August 2008, the U.K.'s Office of Fair Trading continued its criminal prosecutions of individuals under the Enterprise Act when it announced charges against four British Airways executives in its investigation of price fixing of passenger fuel surcharges. Jurisdictions such as Australia, Chile, Greece, Mexico, the Netherlands, New Zealand, Russia and South Africa have recently adopted, or are considering, legislation that will criminalize cartel offenses. In addition, there have been major domestic criminal cartel prosecutions in a number of jurisdictions around the world. For instance, competition enforcers in Brazil, the Czech Republic, Denmark, Ireland, Israel, Japan, and Korea have teamed with public prosecutors to bring criminal charges against cartel offenders.

The adoption of criminal sanctions will certainly be an area of continued evolution in cartel enforcement around the world in the years to come.

5. THE CHASE: CREATING A FEAR OF DETECTION THROUGH THE USE OF INCREASED INVESTIGATIVE TOOLS

If executives perceive little risk of being caught by enforcers, then stiff statutory penalties alone will not be sufficient to deter cartel activity. During the last two decades, cartel enforcers around the world have utilized an increasingly robust arsenal of investigative tools to instill a genuine fear of detection among executives. The covert tape recordings of the lysine cartel that were used to convict cartel participants, and have since been shown by the Antitrust Division around the world as an example of a cartel in action, show the cartel participants brazenly mocking enforcers in the U.S., Europe, and Asia.[20] The lysine cartel members who were caught in the act clearly demonstrated a consciousness of guilt, but continued to meet because they had no fear of detection. Perhaps that is because such a large, global cartel had never before been detected and criminally prosecuted.

speeches/214861.htm; and "When Calculating the Costs and Benefits of Applying for Corporate Amnesty, How Do You Put a Price Tag on an Individual's Freedom?", speech by Scott D. Hammond, before the Fifteenth Annual National Institute On White Collar Crime (March 8, 2001), available at http://www.justice.gov/atr/public/speeches/7647.htm.

20 For a more detailed discussion of the content of the lysine tapes, see "Caught in the Act: Inside an International Cartel", speech by Scott D. Hammond at the OECD Competition Committee Public Prosecutors Program (October 18, 2005), available at http://www.justice.gov/atr/public/speeches/212266.htm. Copies of the tapes and transcripts are available at no charge by contacting the Antitrust Documents Group by phone: (202) 514-2481, Fax: (202) 514-3763, or e-mail: atrdocs.grp@usdoj.gov.

The lysine tapes provided a striking visual tour inside an actual cartel. As the Antitrust Division took the tapes around the world, members of the bar and business community witnessed the inner-working of a cartel with their own eyes. Members of this same cartel were sentenced to lengthy jail sentences and then-record fines were imposed against the corporate defendants. The successful detection and prosecution of the lysine cartel led to increased awareness in the international business community of the risks and the consequences of engaging in cartel activity.

The lysine tapes themselves also had a monumental impact on how many foreign governments viewed the efficacy of their investigative powers and sanctions. After the case, the Antitrust Division showed the tapes to enforcers at meetings of the OECD and also met individually with many foreign government officials and played the tapes for them. In many of those jurisdictions, the antitrust officials were already well aware of the harm caused by cartel activity, and they were already pushing for reform in their laws or in their investigative powers. Foreign enforcers arranged for Antitrust Division personnel to meet with key government policy makers such as treasury officials who held the purse strings for additional funding to fight cartels, legislative members who were contemplating changes in the law, and representatives of influential trade or business groups in an effort to help gain their support for increased enforcement. These stakeholders watched the tapes and saw with their own eyes how their businesses and their consumers had been victimized. Simply put, the lysine tapes caused some foreign governments to question, if not rethink, how they investigated and treated cartel offenses. Thereafter, numerous governments around the world began making cartels a top priority, devoting additional resources to cartel enforcement, and utilizing more traditional law enforcement tools such as search warrants and wire taps in cartel investigations. The global utilization of all available law enforcement powers in cartel investigation has helped to ensure that, in a growing number of countries, "crime in the suites" is treated the same as crime in the streets.

In the United States, since the 1990's the Antitrust Division has increased our arsenal of investigative tools in international cartel investigations to include the use of border watches, Interpol Red Notices, and extradition requests. These tools assist the Antitrust Division in gathering evidence, in shrinking the safe harbors for executives who have engaged in cartel offenses, and in providing strong incentives for those executives to accept responsibility and cooperate with Antitrust Division investigations.

6. THE GLOBAL NETWORK OF CARTEL ENFORCEMENT: INCREASED INTERNATIONAL COOPERATION

In today's global economy, cartels do not stop at national borders, so cartel investigations cannot either. There is a growing worldwide consensus that international cartel activity is harmful, pervasive, and is victimizing businesses and consumers everywhere. The shared commitment of competition enforcers to fighting international cartels has led to the establishment of cooperative relationships among competition law enforcement authorities around the world in order to more effectively investigate and prosecute international cartels.

One of the interesting developments in international cartel cooperation can be found in the work of the International Competition Network's (ICN) Cartel Working Group. Initiated in 2004, this working group is an important forum for agencies to share expertise regarding the challenges of cartel enforcement. Informed by input and experiences of the participating agencies, the working group seeks to identify the best investigative techniques and policy approaches from around the world. A main focus of ICN work in the cartel area is assisting agencies in honing their operational and practical skills. In this vein, the Cartel Working Group organizes the annual ICN Cartel Workshop, a continuation of the successful series of agency-led International Cartel Conferences initiated by the U.S. Department of Justice in 1999. This annual event – hosted in 2009 by the Egyptian Competition Authority – provides a venue for anti-cartel enforcers from around the world to come together, learn from each other, and develop close working relationships that serve as the basis for future cooperation.

The ICN has assisted cartel enforcers in developing cross-border relationships that have resulted in real-time coordination among enforcers conducting parallel investigations of the same cartel. In addition, the proliferation of effective leniency programs has resulted in an increasing number of applicants seeking leniency simultaneously in multiple jurisdictions. Enforcers can then coordinate investigative steps, share – with the applicant's consent – information provided by a mutual leniency applicant, and coordinate searches. Coordinated searches and other investigative steps are becoming more prevalent.

Two recent high-profile examples of successful cooperation and coordination are the air transportation investigation where the United States cooperated with authorities on five continents in order to coordinate the executions of search warrants on multiple subject locations in the United States and abroad. The filing of the Antitrust Division's plea agreement with British Airways calling for a 300 million dollar criminal fine coincided with the announcement by the U.K.'s Office of Fair Trading that the airline also agreed to pay a record fine of 121.5 million British pounds (approximately 250 million dollars) for its role in the passenger fare conspiracy.[21] To date, a total of 15 airlines and four executives have pled guilty in the Antitrust Division's ongoing investigation into price fixing in the air transportation industry. Collectively, the companies have paid or agreed to pay criminal fines totaling more that 1.6 billion dollars and four executives have been sentenced to jail time.

In addition, recent Antitrust Division coordination with the U.K.'s Office of Fair Trading and the European Commission regarding cartel conduct in the marine hose industry is a model of international coordination and the monumental results it can achieve. On the same day that the Antitrust Division and the FBI conducted multiple searches in the United States and arrested eight foreign executives in Houston and San Francisco for their roles in the marine hose conspiracy, the United Kingdom and European antitrust authorities searched locations in Europe.[22] The marine hose investigations also resulted in an international cooperation milestone when the Antitrust Division filed plea agreements with three British nationals in 2007, calling for lengthy jail sentences. For the first time, the Antitrust Division plea agreements anticipated and addressed the criminal prosecution of, and imposition of a jail sentence upon, the defendants for a cartel offense in another jurisdiction. The resulting charges in the United Kingdom against the defendants were the first criminal cartel offenses charged under the U.K.'s Enterprise Act since it came into force in 2003. The unparalleled level of cooperation in the marine hose cases not only made history, but it raised the stakes and provides a strong deterrent message for would-be cartel participants who seek to victimize consumers in multiple jurisdictions.

21 See Press Release, U.S. Justice Department, Antitrust Division, British Airways Plc and Korean Air Lines Co. Ltd. Agree to Plead Guilty and Pay Criminal Fines Totaling $600 Million for Fixing Prices on Passenger and Cargo Flights (Aug. 1, 2007), available at http://www.justice.gov/atr/public/press_releases/2007/224928.htm; Press Release, U.K. Office of Fair Trading, British Airways to pay record £121.5m penalty in price fixing investigation (Aug. 1, 2007), available at http://www.oft.gov.uk/news/press/2007/113-07; Press Release, U.K. Office of Fair Trading, OFT response to U.S. Department of Justice statement (Aug. 1, 2007), available at http://www.oft.gov.uk/news/press/2007/114-07.

22 See Press Release, U.S. Justice Department, Antitrust Division, Eight Executives Arrested On Charges Of Conspiring To Rig Bids, Fix Prices, And Allocate Markets For Sales Of Marine Hose (May 2, 2007), available at http://www.justice.gov/atr/public/press_releases/2007/223037.htm; Press Release, OFT launches criminal investigation into alleged international bid rigging, price fixing, and market allocation cartel (May 3, 2007), available at http://www.oft.gov.uk/news/press/2007/70-07.

7. CONCLUSION

As we see the next generation of jurisdictions adopt criminal sanctions or leniency programs, join in simultaneous coordinated raids on target companies around the world, or impose a record fine, it is worth noting that the DNA for these developments dates back to policies and practices that were put in place by the Antitrust Division in the 1990s and proliferated and flourished through the dedicated efforts of global cartel enforcers over the last two decades.

Alberto Heimler

PAYMENT CARDS PRICING PATTERNS: THE ROLE OF ANTITRUST AND REGULATORY AUTHORITIES

1. INTRODUCTION[23]

In recent years electronic payment systems have increasingly replaced more traditional instruments, like checks and cash.[24] In some countries checks have even been abolished. These developments have modernized the way people pay for their purchases, leading to a more efficient and less costly environment. The next frontier, already experimented in a number of countries, is to use mobile phones as payment devices, at least for small purchases. Irrespective of this significant increase in payment options, it is not at all clear that market participants make optimal choices of payment instruments for a number of reasons. First of all, the pricing of payment services does not ensure that consumers choose the less costly method of payment. Furthermore, the opaqueness of many charges associated with their use may further distort the way people decide how to pay for what they buy.

While cash and checks have been (and are) thoroughly regulated, the card transaction is determined by market forces and, at least in principle, disciplined by competition. However, antitrust authorities and regulators have been increasingly concerned about a number of possible restraints of competition and market failures. First of all, a very important part of the cost of using a card, the interchange fee, is determined at the network level, and applies to all participating banks, possibly leading to a violation of the antitrust rules against anticompetitive agreements. Furthermore, card holders are not aware of the costs associated with using them and do not choose between alternatives considering their total cost. They simply consider their private benefit, for example, the reward they receive at the end of the year for using a certain type of card. As a result, the highest-

23 Sections 3 and 4 of this paper have been to a large extent taken from a recent paper I have written with Sean Ennis, A. Heimler, and S. Ennis, (2008), "Competition and Efficiency in Payment Cards: Which options for sepa?" World Competition, 31: 19-35.

24 For an OECD-wide description of recent developments in the competition-regulatory interface in card payments and for a thorough analysis of the competition problems associated with cards, see Sean F. Ennis, "Competition and Increased Efficiency for Retail Payments in Cards", (2006) Background Paper to the Roundtable Discussion on Competition and Regulation in Card Payment Services, Working Party on Competition and Regulation, Competition Committee, OECD, Paris, June. http://www.oecd.org/dataoecd/0/30/39531653.pdf.

-reward/highest-cost, not the lowest-cost payment instrument is chosen. Consequently, free market competition may result in the high-cost payment system being preferred to its low-cost rivals.

Merchants complain that a common interchange fee is a way for otherwise competing banks to collude on the fees they charge for card transactions, and to avoid negotiating with vendors. Indeed, the only possibility merchants have to discipline a network is to refuse accepting the card it promotes. It is not a very effective negotiation device, however, since consumers expect merchants to accept all available cards. Indeed, networks know that merchants would continue to accept their card, even at relatively high price. As a result, networks may be able to set their interchange fees at a very high level, leading to high merchant fees, and to supranormal profits for the networks and their card issuing banks, while there is nothing merchants can do to discipline them.

The networks respond that interchange fees are essential for the proper operation of card payments. Setting up of a common interchange fee reduces transactions costs, avoiding the need for all banks to enter into bi-lateral negotiations. Furthermore, interchange fees, by imposing that merchants partly cover the cost of cardholders, modify the incentives for consumers to use cards, ensuring that an optimal number of users and merchants join the network. In other words, the real objective of the fee is to balance the two sides of the payment card market to maximize the value of the network, including the value of card services for both parties.

There is some truth in both of these propositions.

In their effort to maximize the use of cards by consumers, the networks have introduced a number of constraints on the pricing of payments services by merchants, for example by prohibiting them to discriminate prices on the basis of the way consumers choose to pay (no discrimination rule). Furthermore, the networks impede non banks from joining the system or reduce the ability of their members to choose the service provider they wish. These constraints have a negative effect on entry and on long run competition. In general, however, the fact that merchants cannot charge consumers differently accordingto their choice of payment instrument leads to an increase in the average cost of payments, which shifts the retailer supply curve upwards. It is like a tax that is translated on final prices, of course depending on the elasticity of demand.

In other words, the costs of payments are (at least in part) passed on to all consumers, which means that consumers who always pay by cash or check (assuming that there are no additional charges associated with the use of these payment instruments) also cover the extra costs originating from purchases by card. As a result, consumers that purchase without cards or with low cost cards are likely to provide an implicit "subsidy" to card users or to high-cost card users.

This paper starts with a discussion of the economics of a card transaction in section 2. It then describes the competition effects of non price restraints imposed on merchants in section 3, while in section 4 these non price restraints will be discussed with respect to the interchange fee. Section 5 will describe a different way of solving the usage externality problem in the absence of an interchange fee. Section 6 will contain a brief description of some countries' experience with payment cards reform. Section 7 concludes.

2. THE ECONOMICS OF A CARD TRANSACTION AND THE INTERCHANGE FEE

Cards are vertically differentiated with respect to other payment instruments. Like checks, they allow people to do their purchases without carrying cash. However, the wide security (for both consumers and retailers) associated with a card transaction is not available in the case of checks. Additionally, unlike checks that circulate only domestically, cards have a worldwide coverage. Finally, unlike any other payment instrument, cards allow consumers an easy access to distant Internet purchases.

For a payment to be completed, cards issuers have to agree with acquirers of card services on the terms by which they will settle their debit and credit relationship. One possibility would be bilateral negotiations between the issuing and acquiring banks. This would involve countless bargaining, a very costly and inefficient undertaking. This is why the adopted solution has been for issuers and acquirers to develop a joint venture that identify a platform over which a number of services are performed and that sets several system-wide rules, including pricing conditions. These system-wide rules differ depending on the organization of the network, which may be four-party or three-party.

In a four-party system (either for credit, or for debit), like Visa and MasterCard, the participants in a card transaction are: the card holder, the card issuer, the merchant and the financial institution that provides acquiring services to him. Through a terminal (usually not a dedicated one, but one open to a number of payment platforms), the merchant communicates the amount of the sale and the consumer's card information to the acquirer. The latter consults the payment platform, which in turn, verifies if sufficient funds remain available to the customer. If these financial resources are available, the transaction is authorised. The merchant's account will be credited the amount of the purchase minus the compensation of the acquirer, and minus the interchange fee (agreed multilaterally) that goes to the issuer.

In a three-party system (usually only for credit), like American Express and Diner's Club, the acquirer and the issuer are part of the same firm. The participants to a card transaction are: the card holder, the merchant, and the card company. In other words, the merchant contracts directly with the payment platform. Through a terminal (usually the same that is used for other platforms), the merchant communicates the amount of the purchase and the consumer's card information directly to the payment platform, which plays both the role of acquirer and issuer. If funds are available, the transaction is authorised and the merchant's account is credited the amount of the transaction minus the fee set by the platform. There is no interchange fee in a three-party system.

Contrary to cash or checks, in the case of payments by card, merchants do not receive the face value of the transaction and are not indifferent to the type of card used to conclude the transaction. At a first approximation, credit card payments are significantly more costly than those made through a debit card, even though the service provided is the same. For example, in a four-party system a credit card transaction would cost the merchant around 2-2.5% while a debit card one only 0.5%. On the other hand, consumers, those that choose how to pay, do not consider the merchant's cost when deciding which payment instrument to use. They simply consider their private benefit. For instance, they may prefer a credit over a debit card because by using the former, their bank account is debited only at the end of the month (so they enjoy a free interest rate period), they receive frequent flyer miles, monetary rebates, or gifts at the end of the year. More generally, if consumers have a number of cards with them, they may prefer using the one that provides them the highest reward. Very often this is the most costly card for the merchant.

As a result, incentives of consumers and merchants are not aligned. Merchants prefer that card holders use debit cards that cost them the least, and lead to an immediate posting of the sum on the merchant's account. Credit cards, an instrument preferred by card holders, are more expensive for the merchants because of a higher acquiring fee. Furthermore, the sum is transferred on the merchant's account some days after the purchase.

In four-party payment platforms it is agreed that on every transaction acquirers will pay to issuers an "interchange fee". The revenues generated allow issuing banks to subsidize cardholders in their use of the card. This fee is quite high, at least in some countries. For example, in the EU in 2004, the weighted average interchange fee for credit cards varied quite substantially country by country. According to the European Commission, "the difference between the highest (above 1.5%) and the lowest weighted average fees for credit cards in 2004 was about 250%".[25] Interchange fees are generally much higher for credit than for debit cards. This is why rebates and benefits are usually associated with the use of credit, but not debit cards. Furthermore, both issuers and acquirers pay a fee to the platform.

In three-party systems, there is no interchange fee, since a single institution is responsible both for acquiring and issuing. However, merchant discounts are usually considerably in excess of those in the four-party platforms, which is one factor that explains the reduced frequency of merchants' acceptance of three-party cards. The end-of-year rewards cardholders receive by using three-party cards are generally higher than those available in four-party systems.

Regulators (and sometimes even antitrust authorities) have often tried to justify the interchange fee only if it constituted a compensation for services provided by issuers to acquirers, *i.e.* assuming that their relationship is vertical. For example, in its 2005 decision on MasterCard, the British Office of Fair Trading regarded as "appropriate", the cost of providing a payment guarantee (fraud losses incurred by issuers and issuers costs associated with the process of authorizing the transaction) and the outlay of processing incoming transactions, while the Office considered "inappropriate" that the interchange fee compensate the issuing bank the expenses of providing a free interest period to card holders[26]. However,

25 See European Commission (2007), Report on the retail banking sector inquiry, Commission Staff Working Document, Com (2007) 33 final, p. 110.

26 See MasterCard UK Members Forum Limited, case number CA98/05/05 available at http://www.oft.gov.uk/advice_and_resources/resource_base/ca98/decisions/mastercard. The decision was suspended in June 2006 in order to allow the OFT to addrees the anticompetitive nature of both MasterCard and Visa interchnage fees. See OFT press release at http://www.oft.gov.uk/news/press/2006/97-06.

this vertical interpretation is not unique, and these "appropriate" costs can also be interpreted as services to cardholders and not to merchants (to ensure that payments will indeed be made), so as to allow them to conclude a transaction with a card.

Instead of the interchange fee being a compensation for services of the issuer to the acquirer, it can be interpreted as being essential for aligning the incentives of cardholders and merchants in order to optimize the diffusion and the use of cards. In particular, the networks, by setting the interchange fee, must recognize the need to attract consumers and merchants, both being crucial for the development of the paying platform. According to this view, the interchange fee does not have an input cost justification and it should be interpreted as a transfer between two sides of the market (cardholders and merchants), lacking any antitrust concern.

According to Evans and Schmalensee "payment systems have much in common with auction houses, exchanges, shopping malls, and video games consoles"[27]. In all these markets two groups need to come together before a market exists: sellers and buyers of art work, securities, consumer goods or buyers of video games systems and writers of video games applications. This is why these markets are called two-sided. Each of them has adopted its own specific rules for sharing costs between participants. In some cases only purchasers pay (auction houses and video games), in others only merchants pay (shopping malls), or both pay (stock exchanges). Also the market for payment systems needs both consumers and merchants for it to exist. However, there are three elements within the definition of two-sided markets. The first (and usually the only one considered) is that two groups of customers need to be present to give value to a product. It is crucial what both groups pay with respect to costs (one side may pay nothing). For example, men and women have both to be present in a disco for it to be a success, and not necessarily both pay the admission fee. Consequently, all that matters is not how much each gender pays, but how much they pay together. Competition among discos will ensure that extra-profits (calculated as the difference between revenues and costs incurred with running a business) amounts to zero. There is no separate analysis possible for each side of the market (there are not two profits, one for men and one for women, or two categories of costs). The second element of two-sided markets (which is seldom considered) is that the cost of the transaction is shared

27 See David S. Evans and Richard Schmalansee, "Paying with Plastic: The Digital Revolution in Buying and Borrowing", Second Ed., MIT, Cambridge, MA, 2005.

only among the parties of the transaction: other parties usually pay nothing. For instance, only actual purchasers of art work pay the auction house, viewers or other event participants generally are not charged. The third element for genuine two-sided markets to exist (which is also seldom considered) is that the optimal pricing structure, for example that only men pay in a disco, cannot be achieved by private negotiations between the two parties alone. In particular, not being able to identify beforehand the women interested in coming to the disco, men would not be able to voluntarily pay for them, if the admission ticket was gender neutral. Therefore, it is exclusively up to the owner of the disco to achieve the optimal pricing policy (men pay double and woman can enter for free).

In the case of payment systems, consumers need the card and merchants need to accept it. So both parties need to be present (element 1). However, it is not always the case that these two sides are the only ones to pay (element 2). While card users may pay the issuer a fixed annual fee for the card (sometimes they may get the card for free), merchants pay for the payment services they receive. However, merchants, since they are usually not allowed to discriminate between consumers according to the payment instruments they use, translate forward to all consumers the (average cost) of payment services they are charged. As a result, all consumers, *i.e.* also those not using the card, pay the costs of card transactions according to the elasticity of demand that merchants face. With respect to the two-sided nature of the card transaction, all final consumers, and in particular cash paying final consumers, are not the "other side".

Finally, the fact that most consumers have a number of payment instruments at their disposal (cash, checks, debit or credit cards, sometimes cards of more than one brand) may convince merchants that providing incentives to their clients to use the most convenient payment instrument would not lead to customers leaving the shop, aligning the cardholders' incentives with their own (element 3). Existing rules, like the no-discrimination rule, impede such efficiency-enhancing signalling on the part of merchants from taking place and the interchange fee may then easily become a collusionary device. Should the no-discrimination rule be eliminated, the success of a collusionary strategy pursued via a high interchange fee is weakened, but not annulled. The fact that retailers are allowed to pass on to their customers a high merchant fee does not imply that they would actually do so. As a consequence, merchants fees may continue to be spread among all consumers, the same way as the cost of a garage is spread among all customers of a supermarket (irrespective of the fact that they shop with an automobile or not).

Praeger et al (2009)[28] provide a hypothetical example to show how the interchange fee is important to allow for a beneficial transaction to take place: “Suppose that the issuer and acquirer each incur a production cost of $.50 for a card transaction. Assuming that they do not derive any direct benefit from the transaction, the issuer and acquirer each obtain a surplus of -$0.50. In addition, suppose the merchant derives benefits of $2.25 while incurring costs of $0.25, yielding a surplus of $2 for the merchant. Similarly, suppose the consumer experiences a benefit of $0.50 and a cost of $0.75, yielding a surplus of -$0.25.” As shown in the first column of Table 1, a card transaction is beneficial yielding a social surplus of $0.75. However, the transaction would not take place, because privately it is convenient neither for consumers, nor for the banks involved. Allowing a transfer on the part of the merchant of $ 1.50 divided equally among the three parties, as shown in the second column of Table 1, will make the transaction also privately convenient. With the transfer of $1.50 all parties will be willing to transact.

Table 1 An example of a transfer payment that induces an efficient transaction to take place

Costs and benefits from a hypothetical transaction	No interchange fee	With interchange fee
		$ 1.50 from merchant
		$ 0.50 to issuer
		$ 0.50 to acquirer
		$ 0.50 to consumer
Acquirer benefit	$ 0.00	$ 0.00
Less acquirer cost	-$ 0.50	-$ 0.50
Plus transfer	$ 0.00	$ 0.50
Acquirer surplus	**-$ 0.50**	**$ 0.00**
Issuer benefit	$ 0.00	$ 0.00
Less issuer cost	-$ 0.50	-$ 0.50
Plus transfer	$ 0.00	$ 0.50
Issuer surplus	**-$ 0.50**	**$ 0.00**

28 R. A. Praeger, M.D. Manuszak, E.K. Kiser, R. Borzekowski (2009), “Interchange Fees and Payment Card Networks: Economics, Industry Developments, and Policy Issues”, Finance and Economics Discussion Series Divisions of Research & Statistics and Monetary Affairs Federal Reserve Board, Washington, D.C.

Merchant benefit	\$ 2.25	\$ 2.25
Less merchant cost	-\$ 0.25	-\$ 0.25
Less transfer	\$ 0.00	-\$ 1.50
Merchant surplus	**\$ 2.00**	**\$ 0.50**
Consumer benefit	\$ 0.50	\$ 0.50
Less consumer cost	-\$ 0.75	-\$ 0.75
Plus transfer	\$ 0.00	\$ 0.50
Consumer surplus	-\$ 0.25	\$ 0.25
Social surplus	**\$ 0.75**	**\$ 0.75**
Private decision outcomes	No transaction occurs; issuer, acquirer and consumer do not participate	Transaction occurs; all parties agree to participate

Source: R.A. Praeger, M.D. Manuszak, E.K. Kiser, R. Borzekowski (2009), "Interchange Fees and Payment Card Networks: Economics, Industry Developments, and Policy Issues", Finance and Economics Discussion Series Divisions of Research & Statistics and Monetary Affairs Federal Reserve Board, Washington, D.C.

The transfer of charges from merchants to all other parties is solving what has been called by Rochet (2003)[29] usage externality. It derives from the inability of each party in the transaction to consider the costs and benefits of the others. Transfers, taxes and subsidies are the solutions economists have identified in the case of externalities. Interchange fees, however, are not the only solution to the usage externality question. I will come back to this question in section 5.

Besides usage externality, the interchange fee could also solve the so-called network externality. While usage externality is limited to the parties of the transaction, network externality originates from the fact that the more the value of the card increases, the more merchants accept it and the more consumers carry it. A large cardholder base makes the card more attractive for merchants, while a large merchant base makes the card more attractive for consumers. If network externalities exist, by shifting the cost from cardholders to merchants,

29 See Jean-Charles Rochet, "The Theory of Interchange Fees: A Synthesis of Recent Contributions", (2003) Review of Network Economics, 2(2): 97-124. http://www.rnejournal.com/articles/rochet_june03.pdf.

the interchange fee reduces the price for card holders, making the card more attractive to them, leading to an expansion of the network which is beneficial for both sides. With respect to the relevance of network externality, Katz (2001) argues (among others) that while a new network may need the interchange fee for expanding, a mature network may not need it[30]. Since Visa and Master Card are already well established networks, the issue of network externality does not arise for them and I will not consider it further.

3. NON PRICE RESTRAINTS IMPOSED ON MERCHANTS

3.1 THE NO SURCHARGE RULE

In the early stage of cards development, in order to increase the incentives for card holders to use their cards, it was prohibited to merchants to discriminate among customers according to the chosen payment instrument. Increasingly, this rule and others very similar to it have been challenged by competition authorities and by regulators.

The imposed neutrality of prices across payment instruments may have been necessary in order to convince consumers to get a card and to use it. Nowadays, since every bank deposit holder has at least two cards (a credit and a debit card) and very often carries also a number of other cards, such price homogeneity may be less important. In any case, the unfortunate impact of such rules is that they create a situation in which merchant costs differ according to the payment instrument chosen, but prices that consumers pay do not reflect these cost differences. This mandatory price coherence is inconsistent with the general principle that, in a market system, prices should be free to reflect costs.

Furthermore, the existence of the no-discrimination rule may allow four-party card systems to set a higher interchange fee than "optimal" and third-party systems to establish a higher merchant fee than "optimal". Since these rules ensure that the extra cost of the card payments will not be paid by their holders, the schemes may easily adopt an opportunistic behavior.

30 M. Katz (2001), "Network Effects, Interchange Fees and No-Surcharge Rules in the Australian Credit and Charge Card Industry", Reserve Bank of Australia, Sydney, August.

Many countries have already required relaxation of price coherence requirements. For example, the Reserve Bank of Australia (RBA) eliminated the no-surcharge rule for four-party card schemes in 2003 and obtained American Express and Diners Club's agreement to remove their anti-steering rules as well[31]. In Europe the UK, Netherlands and Sweden have followed suit. In Canada, the no-surcharge rule for Interac was ruled out, following an investigation by the Competition Bureau. The elimination of the no-discrimination rule in these countries did not lead all merchants to change their conduct and the single price policy has continued to be widespread. As a result it has been argued that the elimination of the no-discrimination rule did not have much effect and that, therefore, it was useless[32]. This is not necessarily the right conclusion. Indeed, the simple ability to impose surcharges or grant discounts has increased the negotiating options of merchants, giving them a better chance to press for lowering the acquiring fees, especially with respect to high merchant fee cards (three-party systems). Indeed without being able to impose the no-surcharge rule card networks are uncertain of whether merchants would price discriminate or not and therefore are clearly more disciplined.

Furthermore, even though the percentages remain low, the number of Australian merchants levying surcharges on credit card transactions has increased steadily. While in the early years only around 5 percent of retailers price discriminated against high-cost-card users, as of 2007 approximately 10 percent of small traders did so, 15 percent of large merchants, and 21 percent of very large ones, which implies that the reform was a success.[33]

3.2 THE NO STEERING RULE

In most jurisdictions, while merchants are not permitted to price discriminate according to the chosen payment instrument, they are also not allowed to direct customers to use certain payment instruments or prevent them from using others. While such a prohibition may be understandable from the perspective of a card brand, it does not enhance the efficiency of the system and it continues to make

31 The no-steering rule is described and discussed in section 3.2.

32 See Howard Chang, David S. Evans and Daniel D. Garcia Swartz, "The Effect of Regulatory Intervention in Two-Sided Markets: An Assessment of Interchange-Fee Capping in Australia", (2005) Review of Network Economics, 4(4): 328-358. http://www.rnejournal.com/articles/chang_et_al_RNE_dec05.pdf.

33 See Reserve Bank of Australia (2008) "Reform of the Australia's Payment System: Conclusion of the 2007/08 Review", page 14. Available at: http://www.rba.gov.au/PaymentsSystem/Reforms/RevCardPaySys/Pdf/conclusions_2007_2008_review.pdf.

sure that final prices and merchants' behaviour are completely neutral with respect to the choice of the payment instrument. Given that merchant fees are relatively high for credit cards, while being much lower for debit cards, retailers would clearly prefer their customers to use debit cards. However, should they decide not to accept credit cards at all (an option that they have), they would impede foreign customers (equipped exclusively with credit cards) from purchasing. This is why it is reasonable to allow merchants to provide an incentive for domestic buyers to use debit cards, while leaving credit cards preferentially for international shoppers only. The no-steering rule prevents retailers from inducing customers to use the less expensive payment instrument. There are no efficiency justifications for such a constraint and the no-steering rule should be eliminated.

3.3 THE HONOUR-ALL-CARDS RULE

The honour-all-cards rule requires merchants, once they agreed to carry a brand, to accept all cards issued under that name. Initially the requirement was meant to cover all credit cards. However, when credit card companies started to offer debit cards as well, the honour-all-cards rule was extended. In the United States after the Check Visa MasterMoney litigation, Visa and MasterCard were ordered to permit merchants to accept their cards of one type (e.g. debit) while rejecting the others (e.g. credit). In Europe debit cards are offered by national schemes and Visa and MasterCard are credit only (in some countries Visa and MasterCards offer debit card services as well). As a consequence, under present circumstances this rule is generally not restrictive in Europe.

As I will discuss it in section 5, the honour-all-cards rule should certainly be eliminated if the collective interchange fee is replaced by a bilateral fee. However, the rule could be maintained if the interchange fee is eliminated altogether.

4. THE NO-DISCRIMINATION RULE, THE NO-STEERING RULE AND THE INTERCHANGE FEE

By imposing that prices be invariant according to the chosen payment instrument, appropriate pricing rewards may induce consumers to choose the most expensive card, ignoring the cost that their choice induces on merchants (and on other final consumers). For example, credit cards provide free credit to consumers (payment is due at the beginning of the month) and sometimes flyer miles or other rewards in return for spending. These benefits have a positive value for users, but their cost (*i.e.* a high acquiring fee) is translated forward by retailers to all final consumers. Given that lower-cost forms of payment provide no reward to consumers, the higher-cost schemes may end up being the most popular ones.[34]

Governor MacFarlane of the Reserve Bank of Australia has argued that pricing strategies by card schemes lead to expensive payment solutions driving out cheaper ones, following a sort of Gresham's Law. "Instead of the bad currency driving out the good, we have the high-cost means of payment driving out the low-cost one. To take the most obvious example, a credit card offers the same service to a merchant – irrevocable payment – as a debit card, yet costs the merchant a lot more. To the cardholder, the credit card offers more – about 50 days free credit – yet it costs less, with the cardholder often receiving payment for using it. Clearly, the second condition for Gresham's Law is met, namely that the price signals to the decision-maker do not reflect the underlying costs, that is the "user pays" principle is not being applied. This tendency for competition to favour the high-cost product seems to be a feature of card-based systems around the world and explains the increasing attention given to the system by competition regulators."[35] The reference to Gresham's law is of course not fully appropriate and in fact Vickers argues: "Without pushing the analogy too far, the common point is that the high-cost means of payment (for the retailer) can tend to gain at the expense of the low-cost means – irrespective of any underlying efficiency advantage."[36]

Rochet and Tirole[37] recognize this problem, but suggest that competition on the issuer side will ensure that rebates to cardholders will eliminate extra profits from the two-sided relationship. According to them, possible extra-profits in payment schemes do not originate from the interchange fee (which is just a transfer between the two sides), but from a lack of competition among issuers (or less likely among

34 See J. Farrell, "Efficiency and Competition between Payment Instruments", (2006) Review of Network Economics, 5(1): 26-44. http://www.rnejournal.com/articles/farrell_march06.pdf.

35 See I.J. MacFarlane, "Gresham's Law of Payments", (2005) Talk to AIBF Industry Forum, at: http://www.rba.gov.au/Speeches/2005/sp_gov_230305.html accessed 6 April, 2006.

36 See J. Vickers, "Public Policy and the Invisible Price: Competition Law, Regulation and the Interchange Fee", (2005) Competition Law Journal, 5-16.

37 See Jean-Charles Rochet, "The Theory of Interchange Fees: A Synthesis of Recent Contributions", (2003) Review of Network Economics, 2(2): 97-124. http://www.rnejournal.com/articles/rochet_june03.pdf, and Jean-Charles Rochet and Jean Tirole, "Cooperation among Competitors: Some Economics of Payment Card Associations", (2002) RAND Journal of Economics, 33(4): 549-570, and Jean-Charles Rochet and Jean Tirole, "Platform Competition in Two-Sided Markets", (2003a) Journal of the European Economic Association, 1(4): 990-1029, and Jean-Charles Rochet and Jean Tirole, "An Economic Analysis of the Determination of Interchange Fees in Payment Card Systems", (2003b) Review of Network Economics, 2(2): 69-79. http://www.rnejournal.com/articles/rochet_and_tirole_june03.pdf.

acquirers). Should high switching costs prevent depositors from turning to a bank that offers less expensive card services, regulators should tackle the problem of high switching costs directly and should not regulate or eliminate the interchange fee.

In Europe most cardholders receive their cards from the financial institution where they have a checking account. The bank is certainly not chosen with respect of the credit card it offers, so competition can hardly discipline banks with respect to the pricing of payment systems. Furthermore, financial institutions often carry a number of cards (for example Visa, MasterCard, or even American Express). Banks, however, tend to suggest one card to depositors. It is true that consumers may ask for a different one, but they seldom do. The incentive of the issuing bank is to offer the card with the highest interchange fee, not the lowest. So, since cardholders usually do not pay for their card, nor for the use of it, competition can hardly discipline the behaviour of issuing banks. On the contrary, the high interchange fee will drive out the low interchange fee card, and therefore interchange fees between competing networks will tend to converge at the highest, not the lowest level. A further perverse result.

One thing that the two-sided market approach tends to ignore is that the acquiring fee is passed on to all consumers, and therefore there is free riding both for merchants and for cardholders, since the fee is also paid by shoppers (the lower the elasticity of demand retailers face) that use less expensive means of payment. Competition among issuers or acquirers would not eliminate this market failure. The free riding of expensive card holders can only be eliminated by a regulatory intervention.

First of all, the elimination of the no-discrimination rule would make this free riding less likely since retailers could always pass the fees on the purchasing cardholders. As a result, suppliers of card payment services charging an excessive interchange fee (in a four-party system), or an excessive merchant fee (in a three-party system) would risk a reduction in revenue because vendors may accept the expensive card, but would pass the extra cost to the cardholder who, as a consequence, might then use another means of payment. The whole negotiation game between suppliers of card services and merchants would change from what it is now when retailers can only refuse to accept the expensive card, a costly and unlikely action.

5. ALTERNATIVE WAYS FOR PAYING FOR CARD SERVICES: WHAT WOULD HAPPEN IF THE INTERCHANGE FEE WAS ELIMINATED?

If the collectively determined interchange fee was eliminated, it should not be replaced by bilaterally negotiated charges. Given the number of banks involved, shifting to bilateral relations would make the system significantly less efficient, and would not ensure the same coverage. An alternative would be that issuers charge cardholders for the use of the card and acquirers charge merchants. In this case, we would be back in the scenario of the first column of Table 1 and the cards would not be used.

Merchants could, however, voluntarily subsidize consumers, without the network deciding on the interchange fee and they would do so, only in so far as it is beneficial to them. This is described in the second column of Table 2.

Merchants, instead of being forced to pay an interchange fee that would subsidize issuers and cardholders (as described in column 1), could pay the acquiring bank $ 0.50 and support consumers that pay with a card by offering them a discount of $ 1. In turn shoppers would pay issuers $ 0.50. The elimination of the interchange fee leads to exactly the same equilibrium as before, but without the risk of the fee being set at a "too high" level and becoming an instrument for promoting a cartel. Furthermore, issuers could compete by offering lower fees to consumers and acquirers by offering lower merchant fees. Finally, retailers would subsidize cardholders according to the actual benefits they receive, opposed to the perceived benefit that networks believe/presume that they obtain.

Nobody knows how to identify the "optimal" interchange fee, even networks do not know how to do it and competition is not a disciplining force in this respect. What we know is that the current rate is far from perfect. The 2007 EC Report on the retail banking sector inquiry shows that in general the interchange fee has been set up at a very high level in the EU 25 member countries. According to the findings, most European issuing banks would have been profitable also without the interchange fee revenues. In particular, the EC Report argues that, "(I)t appears that 62% of all banks surveyed would still make profits with credit card issuing even if they did not receive any interchange fee revenues at all. In 23 EU Member States, at least one bank participating in the survey was able to make a profit from issuing credit cards without interchange fees."[38]

38 Page 127.

As Table 2 shows, eliminating the interchange does not imply imposing settlement at par[39]. Issuers and acquirers may charge customers (cardholders and merchants respectively) for the services they provide. Competition would then operate both on the issuer and on the acquirer side. Contrary to what happens now, when issuers tend to offer to cardholders the high interchange fee card, they would compete by providing consumers with the lowest cost card possible. The incentive of acquirers to reduce acquiring fees would not change. However, their fee could be substantially decreased, not being constrained by the interchange fee.

Table 2 An example of a card transaction without the interchange fee (In the second column the interchange fee is substituted by a charge levied on consumers that merchants decide to subsidize)

Costs and benefits from a hypothetical transaction	With interchange fee	No interchange fee but with the elimination of the non discrimination rule
	\$ 1.50 from merchant	merchants pay \$ 0.50 to acquirer and provider
	\$ 0.50 to issuer	and subsidize 1 \$ to consumers
	\$ 0.50 to acquirer	consumers pay \$ 0.5 to issuers
	\$ 0.50 to consumer	
Acquirer benefit	\$ 0.00	\$ 0.00
Less acquirer cost	-\$ 0.50	-\$ 0.50
Plus transfer/payment	\$ 0.50	\$ 0.50
Acquirer surplus	**\$ 0.00**	**\$ 0.00**
Issuer benefit	\$ 0.00	\$ 0.00
Less issuer cost	-\$ 0.50	-\$ 0.50
Plus transfer/payment	\$ 0.50	\$ 0.50
Issuer surplus	**\$ 0.50**	**\$ 0.00**

39 See Alan S. Frankel, "Monopoly and Competition in the Supply and Exchange of Money", (1998) Antitrust Law Journal, 66: 313-61.

Merchant benefit	$ 2.25	$ 2.25
Less merchant cost	-$ 0.25	-$ 0.25
Less transfer	-$ 1.50	-$ 1.50
Merchant surplus	**$ 0.50**	**$ 0.50**
Consumer benefit	$ 0.50	$ 0.50
Less consumer cost	-$ 0.75	-$ 1.25
Plus transfer/subsidy	$ 0.50	$ 1.00
Consumer surplus	**$ 0.25**	**$ 0.25**
Social surplus	**$ 0.75**	**$ 0.75**
Private decision outcomes	**Transaction occurs; all parties agree to participate**	**Transaction occurs all parties agree to participate**

Most customers have a number of payment instruments in their pocket. In the absence of no surcharging rule and of blending (the practice where acquirers charge an average fee to merchants irrespective of the card they negotiate), merchants would then have the incentive to induce customers to pay with the less costly solution. Merchants could then provide a monetary incentive for shoppers to choose the most cost efficient means of payment (offering for example rebates for low cost cards, or surcharges for high cost ones). The mixture of these instruments would be defined by cost considerations and by rivalry.

Eliminating the interchange fee might reduce the cost of card payments in a four-party system, but would have no effect on three-party schemes. In order to discipline three-party systems, rules like no surcharging or practices like blending should be abolished as well. Indeed, as Farrell has pointed out, regulators should try to achieve neutrality among substitutable payment instruments.[40] Farrell suggests that customers should have appropriate incentives to make good choices among the options they face. "Aligning cardholder incentives

40 J. Farrell, as note 5, *supra*.

for choice of payment instrument with the (joint) interests of the two-sided customer means making the merchant side indifferent about the payment instrument used. That is, it requires that the merchant's total acceptance costs, including merchant-side processing costs and merchant discounts as well as less-tangible convenience and security benefits, should be equal across payment instruments."[41] The elimination of the no surcharging rule and the prohibition of blending will achieve, via the market, a neutrality that would extend to three-party systems as well.

6. ANTITRUST ENFORCEMENT AND INTERCHANGE FEES

In recent years a number of antitrust authorities have opened proceedings against four-party card networks in order to verify whether the agreement establishing the interchange fee was anticompetitive. The Reserve Bank of Australia is the only regulator to my knowledge that has tackled the organizational structure of the payment card industry in order to increase competition to the benefit of merchants and cardholders[42]. I will briefly review some of those decisions.

In 1988 the French *Conseil de la Concurrence* investigated *Carte Bancaire* concluding in its decision that fixing the interchange rate was a restriction of competition because it provided a floor for acquiring fees, preventing the acquiring banks from freely negotiating with merchants[43]. While the Conseil concluded that the determination of an interchange fee was needed for a well-functioning system, it also inferred that the existing fee was not based on "objective" criteria. A new, less costly interchange fee was proposed by *Carte Bancaire* on May 1, 1990 and accepted by the Conseil in October of that year.

In Australia, the Payment Systems (Regulation) Act of 1998 gave the Reserve Bank (RBA) the formal powers to regulate card schemes. After four years of

41 J. Farrell, as note 5, *supra*.

42 Recently in the US credit cards have been criticized for the opacity of the charges to cardholders in the case of overdrafts. Legislation has been passed to address those concerns (the Credit Card Accountability, Responsibility and Disclosure Act). According to a New York Times October 22 editorial "the Act would end a great many odious practices. The companies, for example, could no longer deluge broke and unemployed teenagers with credit cards, driving them deeply into debt that they have no way of paying off. Credit card companies will have to verify the young person's ability to pay or get a signature from a responsible adult before credit is issued. The law prohibits arbitrary rate increases, penalties for customers who are late paying an unrelated bill — known as universal default — and the all-too-common scams in which companies charge cardholders new interest on debts that they have paid a month or two earlier and rig due dates so that payments are late by definition and subject to a hefty penalty."

43 Décision n° 90-D-41 du 30 octobre 1990, le Conseil de la concurrence.

analysis and research conducted partly together with the Australian Competition and Consumer Commission (ACCC), in 2002 the RBA stated that "Co-operative behaviour between competitors which involves the collective setting of prices is rarely permitted in market economies. Prima facie, such behaviour is anti-competitive and, where it is allowed, it typically requires some form of dispensation by competition authorities on the basis that there are offsetting benefits to the public."[44] In 2003, Visa and MasterCard interchange fees were required to be cost-based. As a result they declined from approximately 0.95 percent to 0.55 percent.[45] The lower interchange fees started on November 1, 2003 and merchant service fees have fallen by about the same amount. Besides capping the rate, the RBA prohibited payment systems from imposing no-surcharge rules on retailers and prohibited the honor-all-cards rule to be used to link the acceptance of debit to credit cards and vice versa. Furthermore, the Reserve Bank supported an increased transparency of average interchange and scheme fess.

The 2007/2008 review of the RBA 2003 regulatory decisions shows that "reforms have delivered significant benefits, improving the overall efficiency of Australia's payments system". As a result, the Reserve Bank has decided to step back from interchange regulation, on the condition that the industry took a number of steps to "strengthen the competitive environment". A new review was undertaken in August 2009 and if it shows that progress was not made, interchange-fee regulation will be reintroduced, with a much more stringent cap (3 percent).

When the capping of the interchange fees for Visa and MasterCard networks was decided in Australia in 2003, one major criticism has been that these changes were not applied to three-party systems like, for example, American Express and Diner's. As a result the market shares of these schemes were likely to increase. These fears did not materialize. For reasons presumably, at least in part, related to elimination of no-surcharge rules, anti-steering principles and the reduction in merchant fees in the four-party systems, American Express and Diner's merchant rates have also fallen since Visa and MasterCard fees were lowered. The most recent annual report of the RBA Payment systems board concludes that "(T)he combined average merchant service fee for the American Express/Diners Club schemes continued to decline in 2008/2009 falling by 0.1 percentage points to 2.04

44 See OECD (2006), "Background note" to the OECD Policy Roundtable on Competition and Efficient Usage of Payment Cards, available at http://www.oecd.org/dataoecd/0/30/39531653.pdf.

45 See P. Lowe (2005) "Reform of the payment system", Address by Dr Philip Lowe, Assistant Governor (Financial System), to Visa International Australia and New Zealand Member Forum, Werribee, 2 March 2005, http://www.rba.gov.au/publications/bulletin/2005/mar/pdf/bu-0305-3.pdf.

percent. These fees have fallen steadily since the implementation of the reforms and in June 2009 were around 0.43 percentage points lower than they were prior to the reforms",[46] a decline very similar in size to that obtained by regulation in the case of four-party systems.

On December 19, 2007 the European Commission decided that MasterCard had infringed Article 81 of the EC Treaty (101 TFEU) by collectively establishing the interchange fee for cross-border transactions. Six months were given to the network to come up with a proposal on how to ensure that Article 101 would no longer be breached. In particular the Commission was concerned that MasterCard's intra-EEA fallback interchange fees were inflating the base over which acquiring banks charge prices to merchants for accepting payment cards. The case was finally concluded on April 1, 2009 when the Commission issued a statement that it would no longer pursue MasterCard for non-compliance with respect to the 2007 decision. Following the new methodology proposed by MasterCard, "the maximum weighted average MIF per transaction will be reduced to 0.30 percent for consumer credit cards and to 0.20 percent for consumer debit cards. (...) Finally, MasterCard has agreed to change its system rules as of July 2009 in order to increase transparency and competition in the payment cards market."[47]

What is interesting to observe is that the Commission decision originated from a request of exemption under Article 81(3) (101 TFEU), presented by MasterCard with respect to its cross-border interchange fee. The Commission exempted the agreement that led to the introduction of the interchange fee, but it required that it be substantially lowered. Having become a sort of price regulator, the Commission issued a statement where it declares that it will continue to monitor the industry.

Is an antitrust authority the best placed institution for this?

There is no question that a regulator, like the Reserve Bank in Australia, would have much greater flexibility, accompanying the industry towards a more competitive

46 Payment systems Board (2009), Annual Report, Reserve Bank of Australia, page 14. Available at http://www.rba.gov.au/PublicationsAndResearch/PSBAnnualReports/2009/Pdf/2009-psb-ann-report.pdf.

47 See European Commission (2009), Press release of 1/4/2009 on Antitrust: Commissioner Kroes takes note of MasterCard's decision to cut cross-border Multilateral Interchange Fees (MIFs) and to repeal recent scheme fee increases". Available at: http://europa.eu/rapid/pressReleasesAction.do?reference=IP/09/515&format=HTML&aged=0&language=EN&guiLanguage=en.

environment and even changing completely the way the sector is organized. For instance, abolishing the interchange fee could hardly be achieved by an antitrust authority, only concerned that the agreed rate is "too high." A regulator would be much better suited since it could fine tune its approach.

7. CONCLUSION

Antitrust enforcers and regulators are increasingly concerned that payment card schemes do not operate for the public benefit. Some jurisdictions were worried that the interchange fees in four-party systems, more than being an instrument for addressing usage externality, had become a collusionary device setting a floor under which the charges could not go. Especially with the non discrimination rule in place, the excessive cost of payment services is transferred to all buyers, not just to cardholders. Market discipline is not sufficient. Cardholders (that do not pay for the cost of their choice) tend to use the payment instrument that offers the highest benefits to them, often the most costly. In turn, banks tend to offer to consumers the cards that provide the highest interchange fee.

A few competition authorities, e.g. the European Commission, have enforced the provisions against anticompetitive agreements to reduce the interchange fee to "more appropriate" levels. The same was done already six years ago by the Reserve Bank of Australia. The problem is that nobody knows exactly what this "more appropriate" level of the interchange fee precisely means, so the regulators and antitrust authorities are likely to be wrong.

The reduction of the interchange fee does not necessarily favour three-party systems as many have feared once the RBA lowered the Visa and MasterCard rates only. In Australia in the course of the years after the halving of the four-party interchange fee, also merchant fees for three-party systems were substantially reduced. Furthermore, the elimination of the no-surcharge rule that many had suggested would not produce any effect since retailers would continue to single price, led, in the course of the years, to an increasing percentage of merchants to price discriminate according to the chosen payment instrument.

A change in the organization of the industry, where the interchange fee is eliminated and issuers and acquirers charge, respectively consumers and merchants, could be much more market friendly. I have shown in the paper that usage externality could well be addressed privately by retailers and cardholders.

A regulator, for example in Europe in the process of creating Sepa compliant payment systems, would be much better suited for achieving this, since it could fine tune its approach.

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René Jansen and Ayesha Budd

NMA'S BAPTISM OF FIRE: BID-RIGGING IN THE DUTCH CONSTRUCTION SECTOR

1. INTRODUCTION

A discussion of competition law in the construction industry in Europe would be incomplete without reference to the bid-ridding cartel in the Dutch construction sector. The Netherlands Competition Authority (NMa), which was established in 1998, had not been in existence for long when it was faced with the task of tackling the Dutch construction industry's entrenched cartel system.

In 2001, the NMa initiated an investigation into a bid-rigging cartel within the construction industry of such magnitude that it may be considered to be the NMa's baptism of fire.[48] It was realized from the outset that an investigation of this proportion naturally needed to be tackled differently than the smaller, and less far-reaching cartels the agency (or most other competition authorities) had previously investigated.

This article will highlight some of the unique characteristics of this large-scale cartel investigation, commencing with a description of what bid-rigging is, and where it is most likely to occur. In order to demonstrate why the Dutch construction industry was such a fertile ground for bid-rigging, the specific characteristics of this sector will be outlined. Thereafter, the course of the investigations conducted by the NMa between 2001 and 2006 will be discussed, with a brief summary of the concurrent parliamentary enquiry conducted in this sector.

During this discussion, emphasis will be placed on the NMa's specially tailored fast-track procedure and sector specific fining guidelines. Reference will also be made to the court decisions which relate to the construction cases; and to the dimensions of the investigations. This article will conclude with an overview of the lessons learnt by the agency and the construction sector as a result of these unique investigations.

48 A baptism of fire is a derivation of the French expression "Baptême de feu" which refers to a soldier's first experience under fire in a battle. Today, it has come to mean anyone faced with a complex assignment before they have had a chance to undertake a similar task of a much smaller magnitude.

2. BID-RIGGING DEFINED

In its recent 2008 study of bid-rigging, the OECD defined bid-rigging, or collusive tendering, as an event which occurs when businesses (that would otherwise be expected to compete) secretly conspire to raise prices or lower the quality of goods or services.[49] When bid-rigging prevents the occurrence of effective competition, this often ultimately comes at the cost of the tax payer.

Government organisations and private companies often make use of a bidding process in order to maximize value for money. However, this gain may only be realized if the tendering companies genuinely compete against one another. When competition occurs, such benefits are reaped by commissioning entities, who are in many cases government institutions charged with the responsibility of utilizing public funds. Bid-rigging occurs in many forms and may be adapted to conform to the structure of a variety of "tender markets". The very nature of the bidding process would seem to dictate that each time a tender takes place, there is generally one winner and many losers. This would at first glance provide very little opportunity for collusion. However, cartelists are innovative, in order to circumvent this apparent "problem" and to stimulate the functioning of a bid-rigging cartel, it is common to create an incentive mechanism to allow the winner to redistribute the illicit profit amongst the other "bidders". The winner may compensate the losers by instigating (i) direct settlement via fake invoices; (ii) subcontracting the losers at excessively profitable terms; and/or (iii) using a system of bid-rotation, whereby every loser is eventually placed in a position to be a winner in a subsequent bidding round.[50]

The OECD Guidelines for Fighting Bid Rigging in Public Procurement mention other common features of bid-rigging including cover bidding, bid-suppression and market allocation.[51] Cover bidding occurs where a competitor agrees to submit a bid that (i) is higher than the bid of the designated winner, or (ii) will not be accepted either because it is too high or because it contains special terms that are known to be unacceptable to the purchaser. Cover bidding is designed to give the appearance of real competition. Bid-suppression schemes involve agreements between competitors in which they agree to refrain from bidding

49 "OECD Guidelines for Fighting Bid Rigging in Public Procurement, 2008 – helping Governments obtain the best value for money", http://www.oecd.org/competition (hereafter "OECD Guidelines").

50 Note by the Netherlands to the June 2008 OECD paper "Roundtable on Competition in the Construction Industry".

51 OECD Guidelines p.1-2, see footnote 2.

or to withdraw a previously submitted offer, so that the designated winner's bid will be accepted. Market allocation is achieved where competitors negotiate to carve up the market and agree not to compete for certain clients, certain types of projects, or in certain geographic areas.

There is a variety of factors that can influence whether a market is susceptible to bid-rigging. These factors include: (i) a culture of repetitive bidding for very similar products or services; (ii) a limited number of companies; (iii) little or no entry to the market; (iv) stable market conditions; and/or (v) well organised trade associations.

In the Netherlands, the construction industry was initially perceived as a large homogeneous market with many participants, which did not exhibit many of the above characteristics. However, further investigation revealed that on the contrary, the Dutch construction industry does exhibit such characteristics, as it is made up of many, much smaller, sub sectors/markets, where the conditions are extremely favourable to collusion. In fact, these markets are generally highly specialized with little or no supply-side substitution. The NMa's investigations also revealed that for large, complex, construction projects, only a limited number of large, vertically integrated, firms can in fact meet the specific tender requirements, with the result that individual tender projects may actually form quite small markets in their own right and exhibit many of the above-listed characteristics. The course of these investigations is described below.

3. DUTCH CONSTRUCTION CARTEL CASES 2001–2008

Prior to the establishment of the NMa in 1998 and the Dutch Competition Act in 1997, the Netherlands had subsequently been dubbed a cartel paradise. It is this culture, which had been cemented into the construction culture for decades, that the agency attempted to destabilize through its focused attention on the entire industry. In its search for evidence, the NMa undertook a series of dawn raids on construction company premises and implemented pioneering research methods, focusing on forensic IT. As the investigations developed, and further tips and complaints were received by the agency, it became clear that construction companies were consistently meeting with a view to sharing the market and coordinating their bids.

The NMa construction cartel story has two main rounds, the first ran from 2001 to 2003 and the second from 2004 to 2008.[52] Although the investigations were completed in 2006, several appeals are still being dealt with by the Dutch Courts as this article is being published. Some of the more interesting aspects of the appeals, which relate directly to the specifics of the bid-rigging investigation and associated administrative process, will be discussed further in this paper.

3.1 FIRST ROUND OF CONSTRUCTION CASES 2001–2003

In November 2001, a whistleblower on a Dutch television news programme "Zembla", unveiled the use of secret shadow accounts within the construction industry.[53] The whistle blower revealed that two very different sets of accounts had been maintained for many years. One of them was an official account, while the other kept track of the bid-rigging activities of a number of construction firms. It became apparent that this type of bookkeeping had been occurring in the construction industry at local, regional and national level for decades. The Zembla documentary highlighted these illicit practices and sparked off a series of formal investigations.

This was the outset of the first round of cases, which involved six cases of suspected anti-competitive behaviour in the Civil Engineering and Infrastructure sector.[54] The anti-competitive behaviour mostly related to infrastructural works commissioned by public authorities in the period 1998 to 2002. In December 2003, following investigations in the sector, 22 construction companies were fined more than 100 million euro for various bid-rigging and market sharing cartels.[55]

3.1.1 STRUCTURE OF THE VARIOUS BID-RIGGING CARTELS

The information uncovered by the NMa revealed that the majority of construction companies active in the Dutch market had taken part in the cartels using a variety of forms of bid-rigging. For example, each time a construction tender

52 For further information on these investigations, please visit the English section of the NMa's website on the construction cartel at: http://www.nmanet.nl/engels/home/News_and_publications/Theme_files/Construction_case/Construction_case_mainpage.asp.

53 These shadow accounts were those of the construction company Koop Tjuchem. See the NMa press release of 19 December 2003: "NMa beboet 22 bouwbedrijven voor kartelafspraken" (The NMa fines 22 construction companies for engaging in cartel agreements).

54 See the decision of the NMa of 25 April 2003 in case 3055/ Scheemda, and the cases of 18 December 2003 in case 2873/ Noord-Holland Acht, 3064/ Asfaltzware wegenprojecten Noord Holland, 2906/Heijmans en Solétanche Bachy, 3054/ Atletiekbanen and 3272/Herprofilering Mokerstraat en Aambeeldstraat.

55 See the NMa press release of 19 December 2003. See footnote 6.

was called in the civil engineering and infrastructure industry, a meeting was held between the construction companies to decide who had the so-called "right" to place the lowest tender – thereby winning the bid. The bids were rigged in such a way that those parties who did not earn the "right" to place the winning bid in one particular project would "earn" credits which, when enough had been accumulated, could be used in a subsequent tender project in order to "earn" the "right" to be the winning tenderer. To facilitate parties in keeping track of the credits earned by individual construction companies, the credits were recorded in the aforementioned shadow accounts.

In this way, a system was set up which allowed parties systematically to keep tally of who had earned the right to "win" the next bid. Thus, although the undertaking might not take part in every tender process, it would nevertheless remain loyal to the system, in order to benefit in future rounds.

By using this system the parties were, for a time, successfully able to artificially inflate prices. Without the system of rotating "rights" to "win" a bid, the companies would have been forced to compete with each other on price or quality in order to procure the tender. Competition would undoubtedly have led to lower prices or more attractive bid packages. This type of bid-rigging also occurred in other sectors.

Bid-rigging also took place in the pre-fabricated cement products sector. The companies involved split the market by dividing the right to win tenders from specific clients (such as local councils) amongst themselves.[56] In this system, each construction company would have the right to win all projects requested by a certain client. In most cases, in order to ensure that the "right undertaking" would win the bid, the construction companies agreed on who would offer lowest price beforehand.

In other bid-rigging agreements, where the requirements for the project were known beforehand (i.e. a specific type of paving stone required by a particular local council), the bid was rigged in such a away that only the "right" company would offer a tender which complied with these specifications. It often resulted in a minimal amount of tenders being offered per job. The trend was eventually noticed by clients, who raised their concerns with the NMa.[57]

56 See case 4155 and case 3183, issued on 13 October 2004.

57 See footnote 9.

For a more in-depth analysis of bid-rigging mechanisms with which the NMa has had to deal with in the construction cartels, see the NMa's decisions in the construction cartel cases.[58]

3.1.2 PARLIAMENTARY INQUIRY

Parallel to the NMa investigations, a parliamentary inquiry was launched. The resulting report[59] drafted by the "Parliamentary Committee of Inquiry" into the construction industry established the nationwide impact of the affair. It was clearly shown that public procurement procedures in the Dutch construction industry were open to abuse.

The findings of the Parliamentary Inquiry were that: (i) corruption and fraud were widely spread; (ii) competition in all areas of the construction sector was distorted; and (iii) the behaviour of public procurement officials was to be questioned. The Committee recommended that a public black list of offenders be created and that a new public procurement law be drafted. The Committee also recommended that in order to improve their effectiveness both the NMa and the Public Prosecutor should be given increased sanctioning powers. As a result of the Parliamentary Inquiry, significant public pressure was exerted to effect a thorough clean-up of the construction industry and restore sound business relations, challenging the NMa to achieve optimal enforcement results.

While the sanction procedures of the first round of investigations were being finalised in the course of 2003, the NMa commenced investigations into a second round of separate cartel offences, implicating the participation of even more sectors within the construction industry in bid-rigging offences.

3.2 SECOND ROUND OF CONSTRUCTION CASES 2004–2008

The second round of investigations was initiated in 2004, when in February of that year another set of "shadow accounts" was aired on the Dutch media. The accounts belonged to the firm Boele & Van Eesteren (a subsidiary of the Volker Wessels conglomerate) and related to the Housing and Utility Construction sector.

58 See NMa website (www.nmanet.nl).

59 "De Bouw uit de Schaduw - Parlementaire enquete Bouwnijverheid – Eindrapport" Tweede Kamer vergaderjaar 2002-2003, 28244, nrs. 5-6 (volumes 1-7) (translation: "The Construction Industry comes out from behind the shadows – Parliamentary Inquiry - Final Report", Dutch House of Representatives).

Following this airing, the NMa issued a sector-wide appeal for companies to report cartel offences by submitting leniency applications.[60] This appeal was known as the "*schoonschip oproep*" or "clean ship appeal".[61] The construction industry was particularly susceptible to the offer of leniency in exchange for information, given that it was uncertain just how much incriminating evidence the NMa already had in its possession.

In total, more than 481 companies heeded the call to come clean by filing leniency applications with the NMa. Though a number of investigations were already underway, these leniency applications significantly contributed to the second stage of intense investigations and sanctions procedures.

The Dutch government simultaneously issued its warning, referred to above, that construction companies should "come clean" on past illegal behaviour prior to 1 May 2004, or otherwise face exclusion from future tenders. The Dutch government backed its appeal by threatening that any parties who did not come clean and were subsequently held liable of participating in a cartel, would be blacklisted.[62] All the listed contractors would be barred from procuring any future government listed tenders.

4. THE SCALE OF THE INVESTIGATIONS

The investigations conducted by the NMa in the construction industry revealed that anti-competitive behaviour involving bid-rigging and the allocation of sales quota was endemic among companies in a range of sectors. Between 13 October 2004 and 16 November 2007, Statements of Objections were handed down under article 53 of the Dutch Competition Act in the following markets: civil engineering and infrastructure (2004); installation engineering (2005); housing and utility construction (2005); horticultural services (2006); prefabricated concrete products (2006); cable and pipeline construction (2006) and traffic light control installations (2007). In total, a phenomenal 1 391 companies were investigated and fines

60 For an English version of these guidelines see the "Leniency Guidelines on the non-imposition or reduction of fines" under articles 5L, 5b paragraphs 14, 57, 62, 88 and 89 of the Dutch Competition Act in Cartel cases 2007. However, for an official version of the guidelines in force at the time of these investigations, see Geconsolideerde tekst van de Richtsnoeren Clementietoezegging van 1 juli 2002, zoals gewijzigd bij besluiten, onder anderen van 28 maart 2006. These Guidelines were last amended in October 2009 see http://www.nmanet.nl/nederlands/home/Bedrijven/Clementie/Biecht_uw_kartel_op.asp.

61 See "NMa introduceert bijzondere sanctieprocedure voor de bouw", Actualiteiten Mededingingsrecht, nummer 10 December 2004.

62 This political step was never in fact taken.

of 240 million euro were imposed. Infringements were held to have covered a period of at least four years (mostly during 1998–2001) and in some cases longer.

4.1 HOW TO HANDLE AN INVESTIGATION OF THIS MAGNITUDE

The NMa developed many tools in order to collate the enormous amount of information collected and received in the aforementioned myriad cases. Alongside the special taskforce established within the Antitrust Department, the NMa's Legal Department set up a Construction Taskforce in order to most efficiently tackle this project. This taskforce was further split into dedicated teams, each specializing in separate construction sub-sectors.

As the scale of the investigation increased and the enormity of the NMa's baptism of fire was realized, measures were taken in order to cope with an increased workload for the young authority. The aforementioned specialized Construction Taskforce within the Legal Department, and a data base specifically developed to assist with drafting decisions in a more efficient way, meant that only 25-30 Legal Department case handlers were needed to work out approximately 1250 Statements of Objections in 2.5 years. The existence of a specialized taskforce within the Antitrust Department (comprising of 20 case handlers) meant that sector-specific knowledge was easily gained and retained.

A Chinese Wall existed between the specialized taskforces in the Legal Department and the Antitrust Department in order to ensure that the hearing officers remained impartial whilst determining the fines to be imposed on the construction companies. It is an important principle of Dutch competition law that the fining process is kept separate from the investigation.[63]

In its search for evidence, the agency undertook a series of dawn raids on company premises. Further tips and complaints were also submitted to the NMa from third parties. The NMa also implemented pioneering forensic IT research methods, and utilized specialized IT solutions in order to collate the vast amounts of data submitted. Special fining guidelines were issued for each sector involved and an accelerated or "fast-track" procedure was created for those parties who volunteered to take part. This fast-track procedure will be discussed at more length below.

63 See article 54a of the Dutch Competition Act. For an unofficial translation of the Dutch Competition Act, see http://www.nmanet.nl/engels/home/Index.asp.

5. INCENTIVES OFFERED TO ENSURE MAXIMUM COVERAGE OF THE INVESTIGATION

The NMa and Dutch government applied a carrot and stick principle in order to entice potential leniency applicants to "come clean". They did this in order to achieve the primary goal of the clean-up, which was to ensure that the investigation was not only effective but also efficient.

Strong political pressure was exerted by the Dutch government to ensure swift results. The agency also wished to prevent long procedures keeping both the NMa and the construction sector hostage for many years.

The "carrots" included (i) leniency to all those who provided value-added information prior to 1 May 2004[64]; and (ii) a 15 percent fine reduction to all undertakings willing to take part in the "fast-track" procedure; plus the incentive that (iii) all fines would be based purely on the turnover achieved in 2001 rather than on the entire duration of the infringement.

The "sticks" included (i) the threat that the NMa would impose substantial fines; and (ii) the threat that the Dutch government would include guilty parties on the abovementioned black list.

All undertakings naturally retained the right to choose whether or not to participate in the fast-track procedure and utilize the variety of incentives offered.

5.1 THE FAST-TRACK PROCEDURE

The fast-track procedure was open to all companies concerned who did not contest the Statements of Objections issued by the NMa. Once a company opts for the accelerated procedure, it agrees that a hearing on the merits of its individual case is no longer necessary and agrees to be represented by a joint legal representative. Companies may, however, put forward a written submission to the NMa regarding certain individual circumstances (relating to their financial position, for instance).

Companies remained at liberty to make use of the fast-track procedure, or to choose to defend their cases via the regular process. The intention behind the

64 Although this deadline was later extended - offering undertakings more opportunity to file for leniency with the NMa.

creation of the fast-track procedure was to save time and resources by, on the one hand, allowing cases to be handled much faster (increasing the volume of cases and the scope of the investigation); and on the other hand offering companies a diminished sanction (in return for not challenging the facts of the case as presented by the NMa).[65] Undertakings who took part in the fast-track procedure were offered a 15 percent reduction in the gross fine levied providing they complied with all the conditions of the procedure. The normal administrative procedure remained open to those who wish to contest the infringement and their alleged participation. The rights of defence were therefore preserved. [66] Out of the approximately 1400 companies involved, 90 percent (1250 companies) applied to make use of the fast-track process while 481 companies applied for leniency, of which 379 were accepted. In order to ensure that the fast-track procedure accomplished efficiencies for all involved, all participants were to be represented by one authorised sector representative. This attorney had exclusive access to the file and represented the participants at the hearings. This meant that during the fast-track procedure, no individual hearings were held, nor was individual access to the file permitted.[67]

In short, by opting for the fast-track procedure, undertakings agree to forego i) individual access to the file; ii) individual hearings; and ii) the opportunity to dispute the facts and conclusions contained in the Statement of Objections. Parties were naturally free to challenge the facts and conclusions as presented in the Statements of Objections at any time, however, in doing so, they would forego the possibility of a 15 percent reduction in fines.

The above aspects of the fast-track procedure were upheld by the District Court. The Dictrict Court stated that as parties were free to opt in, or out, of the procedure they were free to choose which type of defence they would lead. The companies were therefore under no obligation to incriminate themselves nor to waive their rights of defence in any other way.

65 For a discussion on the pros and cons regarding whether to opt for the fast track procedure, see "Keuze B&U voor reguliere of versnelde procedure is lasting overwegen", M. Essers and A. Boot (2005). See also http://www.nmanet.nl/engels/home/News_and_publications/Theme_files/Construction_case/Accelerated_Sanctions_Procedures_and_Special_Fining_Guidelines.asp.

66 In proceedings before the District Court of Rotterdam, the judge held that contrary to the parties' claim, the fine reduction of 15 percent, did not result in undue pressure being placed on undertakings to take part/remain in the fast-track procedure. However, this is currently being appealed at the Dutch Trade and Industry Appeal Tribunal.

67 "De bouwfraude: een tussenbalans", Jacco Hakfoort, Actualiteiten Mededingingsrecht, Nummer 9, November 2008, p. 208-211.

5.2 SPECIAL FINING GUIDELINES

As previously mentioned, the NMa developed specially tailored fining guidelines, for each of the sectors involved, in order to most efficiently and effectively clean up the industry and set it back on its feet. The accelerated fining procedure prescribed a method of fining specially adapted to stimulate company participation in the fast-track procedure. One aspect of these guidelines was the stipulation that the fines would be based on approximately 12 percent of the company's turnover from tenders in 2001.[68] Each fine was proportionate to the severity of the infringement and the sector involved. Thereafter, account was taken of other circumstances of the respective company, such as leniency and the financial situation of the undertaking concerned.[69]

In 2008 the District Court considered whether this aspect was reasonable. In its decision the court held that setting the fine on approximately 12 percent of the turnover (depending on the sector involved) in the 2001 calendar year, instead of the entire turnover generated during the period of the infringement, was neither unreasonable nor in violation of any law.[70]

5.3 OUTCOME

At the conclusion of these investigations, approximately 1400 of the companies who received a Statement of Objections applied for the fast-track procedure. A further 150 cases were dealt under the regular procedure, of which 60 were fined a total of 12,2 million euro. In its fining decisions, the NMa handed down decisions in 11 nationwide bid-rigging and market sharing cartels in 7 construction markets and sanctioned undertakings with a total of 240 million euro in fines.[71]

68 The actual percentage used varied per sector and was laid out in specific fining guidelines see: http://www.nmanet.nl/engels/home/News_and_publications/Theme_files/Construction_case/Special_Fining_Guidelines_.asp.

69 These fining guidelines are discussed on the English link to the NMa website at http://www.nmanet.nl/engels/home/News_and_publications/Theme_files/Construction_case/Accelerated_Sanctions_Procedures_and_Special_Fining_Guidelines.asp. The Dutch version of these guidelines may be found at http://www.nmanet.nl/nederlands/home/Actueel/Dossiers/Bouw/Index.asp.

70 For decisions in this sector, see http://www.nmanet.nl/nederlands/home/Actueel/Themadossiers/Bouw/GWWbesluitenoverzicht.asp.

71 These fines were significantly lowered as a result of appeals.

5.4 SIZE OF THE SECOND ROUND INVESTIGATION

The information in the table below provides an overview of the extent of the bid-rigging cartels uncovered by the NMa during these investigations.

Following the imposition of fines on 1300 companies, 100 of these appealed under the administrative system, and 50 to the District Court. This table does not include information on the cases currently pending in the courts.

Subsector	Leniency Applications	Fine imposed (€ million)	Number of companies: Fast Track	Number of companies: Regular Procedure
Civil Engineering & Infrastructure	113	€ 102	374	42
Installation	30	€ 44	174	19
Building and Housing	218	€ 76	657	77
Cable and Pipeline	22	€ 12	78	7
Remaining categories	45	€ 16	108	4
Total	**428**	**€ 250**	**1,391**	**149**

The following section provides a brief overview of some aspects of these appellate cases which relate specifically to the nature of the bid-rigging investigation.

6. STATE OF PLAY BEFORE THE DUTCH COURTS

The first construction case appeal was published in January 2008. To date, the District Court of Rotterdam has handed down approximately 45 decisions, although cases continue to be heard at the time of publishing this article. The agency has succeeded in more than 80 percent of cases heard before the District Court to date.

These first rulings relate to cases in the fast-track procedures in the civil engineering and infrastructure industries. Only two of the NMa's decisions have been (partly) overturned by the court. In 6 others, the level of the fine imposed was reduced. The remaining 37 cases have been ruled in the NMa's favour.[72]

72 These figures are subject to change, as these cases continue to be heard.

Outlined below is a brief description of the Court's findings with regard to whether undertakings who had originally taken part in the fast-track procedure ought to be permitted to challenge certain aspects of the case in a subsequent appeal.

In order to retain the benefit of the 15 percent discount received as a result of taking part in the fast-track procedure (where parties had not disputed the facts or the legal assessment), the judge held that, on appeal, these companies should not be allowed to question the existence of the system of bid-rigging nor their participation therein. This also held for a parent company where its subsidiary had not challenged its participation in such a system.

The court delineated its reasoning in this case, making it clear that undertakings who participated in the fast-track procedure, and wished to retain the reduction in their fine, would continue to be permitted to appeal the following two facts relating to the fining issues: (i) whether the basis of the fine has been set proportionally, and (ii) whether the level of the undertakings' involvement had been accurately judged.

7. LESSONS LEARNT

One of the earliest lessons learnt was the need to provide a structured means for leniency applicants to submit information. With over 300 leniency applicants, it quickly became necessary to streamline what type of, and how much, data ought to be delivered. In order to accomplish this, the NMa posted a form on its website stipulating the kinds of information required for parties to successfully qualify for leniency.[73]

Another valuable lesson learnt was that the use of specialized taskforces, as mentioned earlier in this article, can contribute significantly to effective case completion. These taskforces not only saved time and resources, they also allowed the remainder of the case handlers in the Antitrust Department and lawyers in the Legal Department, to continue investigating other sectors of the Dutch economy. Other benefits of these two highly specialized taskforces include the increased speed of the decision-making due to the specific knowledge each team had accumulated in each specific sector.

73 See http://www.nmanet.nl/nederlands/home/Actueel/Dossiers/Bouw/Index.asp "Formulier Melding van aanwijzingen voor mededingingsbeperkende afspraken bij de aanbesteding van bouwprojecten".

Another innovation in the handling of the construction cases was the establishment by the State of a compensatory fund. The goal was to prevent the escalation of unpaid civil damages claims. It was agreed that if undertakings contributed to this fund, the NMa would deduct a maximum of 10 percent of the fine, as long as this deduction did not result in the total of the fine to be paid falling below a certain pre-determined level. At the time of the construction cases, the NMa had little insight into this compensatory fund and how it worked. However, the cases gave the agency valuable insight into the concept of the compensatory fund, thereby providing an opportunity to develop this idea and apply it to later cases.

Another lesson learnt related to the need for new investigative methods in order to lessen the NMa's need to rely on leniency. One such method is to intensify the agency's contacts with other investigative authorities in order to benefit, where possible and appropriate, from information that they may already have gathered.[74]

A recent bid-rigging case, which was uncovered by maximising co-operation between the Department of Public Prosecutor and the competition authority, demonstrates that the construction industry is not yet clear of cartels. In this case, the NMa received transcripts of wire-taps the Public Prosecutor had utilized to uncover dealings in an offence unrelated to the antitrust agency's investigation.[75] These transcripts have led to a subsequent cartel investigation by the agency in Maastricht. The case proves that the NMa must remain vigilant in its monitoring and enforcement of antitrust law in the construction industry.

In order to capitalize on the successes the NMa has made through a targeted focus on the construction industry, the agency continues to promote vigorous competition in other sectors, by way of proactive advocacy.

8. CONCLUSION

The experiences of the NMa in the construction industry may be considered unique due to the number of companies investigated. It appears that many

74 Such as contacts with the tax authority and the Public Prosecutors office.

75 The NMa has no powers of its own to set wire-taps. Only the Public Prosecutor may place such taps and then only under authority of the Court for the purposes of a Public Prosecutor's investigation. In this case, the taps were placed in order to uncover a plot by construction companies to bribe civil servants.

other countries are also actively prosecuting cartels and, in particular bid-rigging activities, in this sector.[76]

In conclusion, although the agency is aware that the construction industry is not yet entirely free of cartels, it is optimistic that as a result of the clean-up of the construction industry, the attitude towards cartel-forming is gradually changing. This optimism is based on a survey sent to construction firms, property developers, government institutions and other interested third parties in order to determine the success of the NMa's clean up in the Dutch construction sector.[77] The conclusion of the survey was that although it remains too early to tell whether the culture has significantly changed, it is certainly obvious that the clean-up contributed to a positive change of attitude within the industry.

76 See Note by the Netherlands to the June 2008 OECD paper "Roundtable on Competition in the Construction Industry".

77 This survey was conducted by the consultancy bureau TNS NIPO and was published on the NMa website in 2008 (www.nmanet.nl).

Peter Klocker

FIFTY YEARS OF ANTI-CARTEL ENFORCEMENT IN GERMANY – DEVELOPING AND IMPROVING THE SYSTEM

1. INTRODUCTION

The Bundeskartellamt was established in 1958 and was entrusted with the enforcement of the German competition act, i.e. Act Against Restraints of Competition (ARC)[78], which entered into force in the same year. The course of competition law enforcement in Germany traces the changes of priorities attributed to certain kinds of competition law proceedings through the decades. The re-calibration of priorities and enforcement tools offers insights beyond the jurisdiction of Germany.

2. SETTING THE FOUNDATION

The original responsibilities of the Bundeskartellamt consisted of enforcing the ban on cartels and the control of abusive practices, while merger control was not yet in its portfolio.[79] Fighting hardcore cartels is a particular field in which the Bundeskartellamt has gained extensive experience. The basis of this was a clear vote of the legislature, already at the time of the enactment of the original ARC, for outlawing any horizontal agreements infringing competition save for certain well-defined exceptions.

However, this did not come about without struggle. The ban on cartels only came into the German ARC after a long and bitter debate against a strong industrial lobby. Even after its introduction, the companies' need for guidance on this subject was significant. From the start, competition advocacy was – in addition to anti-cartel enforcement – an important part of the Bundeskartellamt's work. The agency hosted meetings together with the competition authorities of the *Länder* (*Landeskartellbehörden*) and the Chambers of Commerce and Industry with the aim of conveying to the enterprises the limits of lawful coordination. These

78 Gesetz gegen Wetbewerbsbeschränkungen of 27th July 1958 (BGBl. I 1081).

79 Merger control was included in the governmental bill, however it was not made part of the ARC, when it was first enacted in 1958.

events were of particular significance in the early phase of the introduction of the competition regime, and then, again, after German reunification, when market participants in Eastern Germany faced a competition law regime for the first time.[80] But even beyond these exceptional periods, the Bundeskartellamt has remained well aware of the constant need for competition advocacy. This requires an ongoing effort to educate companies about the options and limits set by competition law, as well as driving home the importance of free competition in the political realm.

The ARC has been amended seven times since it became law in 1958. In 1973, the second amendment of the ARC expanded the application of the prohibition on cartels and introduced provisions on merger control.[81] Following this second amendment of the ARC, mergers meeting, or surpassing defined turnover thresholds had to be notified with the Bundeskartellamt for a competition assessment. Since then, the Bundeskartellamt has had the authority to prevent the creation or strengthening of dominant positions of companies through mergers. With the introduction of merger control into the ARC, merger control overshadowed fighting cartels. This was due to a number of factors, the most important being the time-sensitivity of merger control proceedings.[82] Nevertheless, the fight against cartels has always been an integral part of the Bundeskartellamt's daily work.

3. IMPROVING THE STRUCTURE

After the introduction of merger control, the number of notifications increased continuously.[83] The first years after the second amendment of the ARC were marked by the interpretation of indefinite legal concepts (*unbestimmte Rechtsbegriffe*), such as the "creation" and "strengthening" of dominant positions. The decision by the Federal Court of Justice in the case *GKN/ Sachs* is of particular relevance in this regard, as many questions of interpretation were addressed there.[84]

80 See Activity Report 1989/1990 BT-Drucksache 12/847, p. 7 f.

81 Law amending the ARC of 1973 (BGBl. I 1974, 869).

82 For further explanation see fn. 9.

83 In the first year after the introduction of merger control more than 150 cases were notified to the Bundeskartellamt: Activity Report 1974, BT-Drucksache 7/2791, p. 111 ff., Table 3. In 2008, 1675 mergers were notified with the Bundeskartellamt: Activity Report 2007/2008, BT-Drucksache 16/13500, p. 179.

84 Bundesgerichtshof, WuW/E BGH 1501 - Kfz-Kupplungen in which the Federal Court of Justice upheld the Decision by the Bundeskartellamt.

German reunification brought new challenges for the Bundeskartellamt. The privatisation of former East German state enterprises, often through acquisition by West German or foreign firms, led to a further increase in the number of merger cases. Within a year (from 1990 to 1991), the number of annual merger notifications rose from 1548 to 2007.[85] Due to the time-sensitive nature of merger review[86], the surge of notifications led to a certain focus on merger control during this exceptional period. External expansion through mergers took on specific significance for the economy, and thus captured the Bundeskartellamt's attention and manpower. Inevitably, other proceedings – such as cartel cases – received less attention in that period. However, the Bundeskartellamt was conscious of this shift in emphasis, and accordingly, reviewed its priorities in the early 2000s. This review led the Bundeskartellamt to recalibrate its priorities.

This is reflected by institutional changes which began in the early 2000s and have continued since then. The Bundeskartellamt reorganized its approach to cartel prosecution and established certain new structures which have allowed the agency to focus more – and more effectively – on combating cartels and the abuse of dominant positions. While the general principles of organisation of the Bundeskartellamt were recognised as a key factor for the success of the authority and were not questioned, some structural reforms have contributed to enhancing the effectiveness of the organisation. It is worth acknowledging that the bedrock of the Bundeskartellamt's structure and its key operating units are the Decision Divisions which investigate and decide cases.[87] They are, traditionally, structured along sectors of the economy, which means that a Decision Division deals with all competition cases – mergers, cartels, dominance issues – in those industries that are within its field of responsibility.

While the sectoral mode of organization of the competition authority has strong advantages for the Bundeskartellamt, it entails certain drawbacks as well. In particular, know-how and experience in the specifics of anti-cartel enforcement risk being diluted throughout the organisation. In recognition of this a special Unit

85 Activity Report 1991/ 1992, BT- Drucksache 12/5200, p. 163.

86 After receipt of the complete notification documents at the Bundeskartellamt the competent Decision Division has one month to examine the project. If the merger project proves unproblematic, the Decision Division clears it informally before the expiry of the one month time limit. The merger can then be put into effect. If the Decision Division considers further examination necessary, it will so inform the companies. This measure introduces the "main examination proceedings" and the time-limit for examining the merger project is extended. If the main proceedings have been initiated, the Decision Division has to decide the case within four months of the receipt of the complete notification.

87 Currently, the Bundeskartellamt has twelve Decision Divisions, two of which are exclusively competent for the prosecution of cartels.

for Combating Cartels (*Sonderkommission Kartellbekämpfung*) was set up in 2002, which collects and consolidates know-how and assists the Decision Divisions in the preparation, conduct and result analysis of investigations in cartel proceedings.

Furthermore, in amending the general principle according to which a Decision Division deals with all competition law infringements in a specific economic sector, two additional Decision Divisions were founded, in June 2005 and in October 2008, which focus exclusively on the prosecution of cartels. This does not replace the responsibility of the sectorally organized Decision Divisions for cartel prosecution, but rather complements it. This step also addresses very effectively the risk that time-sensitive proceedings – especially merger control proceedings – may take precedence over non-time-sensitive but equally crucial proceedings like cartel prosecution.

A complementary step to these organisational measures was the implementation of a number of enforcement tools. In March 2000, the Bundeskartellamt introduced its first leniency programme, which was subsequently reformed in 2006 and based on the ECN Model Leniency Programme[88]. It offers companies and individuals who are involved in a cartel and who decide to cooperate with the Bundeskartellamt in investigating and dismantling the cartel a waiver or reduction of up to 50 percent of the fine that would otherwise be imposed. To gain the benefits of the leniency programme, candidates have to cooperate fully with the Bundeskartellamt in the investigation at an early stage. The Bundeskartellamt also introduced a settlement policy, which improves efficiency by speeding up proceedings and avoiding lengthy challenges in court. Other policy tools defining the area of legal cooperation agreements include the so-called "de minimis notice"[89] and the notice on the possibilities of cooperation for small and medium-sized enterprises of 2007.[90] These give companies, which have to assess for themselves whether their cooperation agreements are exempt from the prohibition of cartels, guidance and more legal certainty.

Another enforcement tool was the implementation of new statutory provisions in 2005 with respect to how fines against companies and associations of undertakings

88 Activity Report 1999/2000, BT-Drucksache 14/6300, p. 43; Activity Report 2005/2006, BT-Drucksache 16/5710, p. 9.

89 The first "de-minimis notice" was published in 1980 as the "Bekanntmachung über die Nichtverfolgung von Kooperationsabreden mit geringer wettbewerbsbeschränkender Bedeutung", BAnz. Nr. 133 of 23 July 1980.
It was replaced by the current de minimis notice on 13th March 2007 http://www.bundeskartellamt.de/wEnglisch/download/pdf/Merkblaetter/0703_Bagatellbekanntmachung_e.pdf.

90 http://www.bundeskartellamt.de/wEnglisch/download/pdf/Merkblaetter/0711KMU_Merkblatt.pdf.

that have engaged in cartel activity are calculated. Prior to 2005, such enterprises could be fined up to 1 million DM (500.000 euros), and beyond this could face a penalty of up to three times the amount of excess profits they earned as a result of the anti-competitive conduct.[91] In practice this rule entailed two difficulties. First, it required the Bundeskartellamt to calculate the amount of excess profits – a time-consuming and resource-intensive activity. Second, the fines in practice were often not sufficiently high to produce the deterrent effect that prevents businesses from engaging in cartel activity in the first place. The new rules state that companies and associations of undertakings engaged in cartel activity can be fined up to 1 million euros, and beyond this could face a penalty of up to 10 percent of their overall turnover for the previous fiscal year depending on the gravity and the duration of the infringement.[92] In order to ensure transparency and a harmonised application of the fining provisions, the Bundeskartellamt published guidelines on the setting of fines against undertakings and associations of undertakings thereby limiting its margin of discretion.[93] The result is that fines can be significantly higher than under the former rules – thus increasing the deterrent effect – and the Bundeskartellamt no longer needs to undertake the laborious task of isolating and calculating excess profits.

Armed with these new tools, the Bundeskartellamt has continued targeting cartels in a wide range of sectors of the economy, most prominently and persistently in the construction materials sector, but also in other sectors, among them pharmaceuticals[94], luxury cosmetics[95], insurance,[96] and the paper trade.[97] However, it is the construction materials sector which has proven to be one of the most cartel-prone areas of the economy. It has provided the Bundeskartellamt with a constant stream of cartel cases.

To put the consistent work of the Bundeskartellamt with regard to anti-cartel enforcement into figures, in the period 2001/2002 the Bundeskartellamt conducted

91 See § 81(2) ARC (version in force prior to 2005).

92 See § 81(4) ARC.

93 Notice no. 38/2006 on the imposition of fines under Section 81 (4) sentence 2 of the German Act against Restraints of Competition (GWB) against undertakings and associations of undertakings - Guidelines on the setting of fines - of 15 September 2006: http://www.bundeskartellamt.de/wEnglisch/download/pdf/Bussgeldleitlinien-E.pdf.

94 Activity Report 2007/2008, BT-Drucksache 16/1350, p. 74 f.

95 Activity Report 2007/2008, BT-Drucksache 16/1350 p. 75.

96 Activity Report 2007/2008, BT-Drucksache 16/1350, p. 140 f.

97 Activity Report 2007/2008, BT-Drucksache 16/1350, p. 70.

eight national dawn raids in 149 companies and twenty private homes[98]; in the years of 2007 and 2008, the Bundeskartellamt carried out 35 dawn raids in 175 companies and 24 private homes.[99] The specific enforcement tools and measures to tackle cartels have proven to be very effective: all in all, the Bundeskartellamt received 212 leniency applications; of which eighty applications were submitted by undertakings and individuals in 2007 and 2008 alone.[100]

4. STRIKING A MULTITUDE OF BALANCES

Anti-cartel enforcement, in recent years, has not only relied on an increase in resources and on the adjustment of the organisational and operational framework. Rather, a series of novel tools was implemented. Together, they form an intricate system of cartel prosecution which combines and balances specific anti-cartel provisions and measures.

A system, by definition, consists of "a set of connected things or parts forming a complex whole."[101] The system at hand is made up of a number of important sub-systems, such as agency enforcement, comprising, inter alia, leniency programme and settlement, as well as judicial review and private enforcement, to name but a few. These sub-systems and their elements are mutually interdependent and influence each other by reinforcing or possibly counteracting each other. Therefore, there is an imminent need to strike a multitude of balances. In this respect, it is worth paying attention to the interactions of the sub-systems within agency enforcement (such as e.g. competition advocacy, the implementation of a leniency programme and the implementation of a settlement policy), but also beyond.

The Bundeskartellamt is active, even outside the strict area of enforcing the law, in ensuring that competition principles are not violated. With respect to competition advocacy, the Bundeskartellamt alerts the wider public as well as companies to the fact that cartel agreements are illegal and that the companies face – in the case of a violation – the consequences of such an offence. Furthermore, it is an objective of competition advocacy to generate an understanding among the public at large that cartels have negative overall economic effects and to highlight the

98 Activity Report 2001/2002, BT-Drucksache 15/1226, p. 43.
99 Activity Report 2007/ 2008, BT-Drucksache 16/13500, p. 32.
100 Activity Report 2007/ 2008, BT-Drucksache 16/13500, p. 32.
101 See: The New Oxford English Dictionary.

importance of prosecuting and punishing them. Competition advocacy is a vital tool for combating cartels, but it can only be effective if backed up by enforcement. Only if there are effective tools for prosecution and if they are used by the competition agencies, does advocacy receive the attention it needs to help firms steer clear of competition law infringements.

Another aspect that must be considered in designing an anti-cartel enforcement system is the relationship between a leniency programme and other agency policies. Launching such programmes can further the work of the competition agencies. However, its success also rests on a range of preconditions. There must also be a functioning system of prosecution that can achieve results absent such leniency. Only if there is a significant risk of detection and prosecution even without leniency applications, will the system, in the long run, be sufficiently credible for cartel offenders to step forward, reveal themselves and others and assist in the prosecution. Settlements can contribute to efficiency by accelerating proceedings and avoiding lengthy challenges in court. However, if settlement conditions are excessively generous, e.g. by reducing fines considerably, this may take the pressure off the cartel members to cooperate at an earlier stage, in the leniency phase. If the results which could be attained by a settlement even at a very late stage of the procedure are essentially equivalent to the results of a leniency application, the cartel members have little incentive to apply for leniency in the first place.

Similar considerations hold true for the relationship between judicial review and agency enforcement. Only if they work towards the same objective will the goal of effectively combating cartel agreements be attained. Thus, if competition agencies and courts are not in unison regarding the fundamental principles of anti-cartel enforcement, two negative consequences follow: on the one hand enforcement may be hampered, and on the other hand the deterrence function of cartel prosecution may erode.

Finally, private enforcement plays an important role in complementing the other tools of anti-cartel enforcement. Private enforcement denotes the application of competition law in civil disputes before national courts. This can take different forms, most prominently in the current international debate, the claiming of damages by those who have suffered a loss caused by an infringement of the antitrust rules. Private actions are widespread in Germany, and they have been part of the German competition law system from the start. Between 2004 and 2007 alone, there were more than one thousand private actions in Germany involving competition law[102]. These cases of private enforcement have given significant impulse to the development of competition law. Traditionally, the focus in these cases has been on obtaining a cease-and-desist order, and not so much on damages. In the German legal tradition, it is typically single firms who advance claims in court. In the past, collective actions were rare.

Private enforcement in cartel cases typically builds on agency cases that establish certain facts. Thus, if there is no agency case that brings a cartel out into the open, there is most likely no basis for private litigation. Hard-core cartel cases of the agencies, in turn, are frequently the result of leniency applications. Hence, a working leniency regime may lead to a hard-core cartel case, and subsequently to private enforcement. If, however, the potential leniency applicant, as an outcome of his or her internal cost and benefits analysis, considers the risk of extensive and costly private litigation to be too high, this would deter him or her from revealing the cartel and applying for leniency.

Leniency should hold the promise of legal certainty and a quick closure on the issue of cartel involvement for companies. This incentive may, however, be forsaken if cartel members must fear that their leniency application will backfire on them. Thus, if plaintiffs are given disproportionate incentives and means to take cartel members to court, as well as unduly favourable access to evidence, and the burden of proof is squarely placed on cartel members, chances are slim for them to achieve certainty or quick closure of the case. This, in turn, will mean that cartel members will neither file leniency applications nor enter into settlement agreements. In this respect it is of great significance that other measures – such as private enforcement – do not thwart the leniency programme and the settlement policy.

Against this background, it is important to keep in mind how sensitive the entire system is. The right balance between the various measures such as leniency applications and private enforcement must be found, as the wrong emphasis in either direction could tilt the scale.

Similar considerations have to be made with respect to the current discussion on criminalisation of cartel offences and the relation of this to enforcement practice, and especially the effectiveness of leniency programmes. Whereas,

102 Based on internal data of the Bundeskartellamt, deduced from the information filings by civil courts in Germany to the Bundeskartellamt.

in administrative proceedings, it is typically the competition authority that is solely in charge of conducting the proceedings, in criminal proceedings responsibility for handling a case will usually be in the hands of the public prosecutor. While a competition authority, in its administrative proceedings, may have discretion to pursue or drop charges, e.g. on the basis of a leniency programme, this is typically far more difficult in criminal proceedings. Therefore, if company managers or other individuals who have engaged in anti-competitive conduct need fear the possibility of a prison sentence, they may be discouraged from applying for leniency to the competition authorities.

The system's aspect of cartel prosecution is not limited to intra-agency and domestic interaction. Special attention should be given to effects deriving from the repercussions that enforcement action in neighbouring jurisdictions may have. This holds especially true in a closely integrated economic area like Europe.

Together, the national competition authorities within the EU and the European Commission form the European Competition Network (ECN), where members cooperate closely in the interest of protecting competition. The ECN provides a framework for cooperation between the European competition agencies in cases in which Articles 81 and 82 of the EC Treaty (respectively 101 and 102 of the Treaty on the Functioning of the European Union, TFEU) are applied and a basis for creating and fostering a common competition culture in Europe. However, one should keep in mind that the ECN establishes a network of partners with parallel competences.

This has special repercussions for the field of cartel prosecution. The non-hierarchical system of the ECN implies that an application for leniency to one competition authority is not to be considered as an application for leniency to another authority. With this in mind, the ECN Model Leniency Programme was established.[103] The purpose of this programme is to erect a common standard to ensure that participants in cartels are not discouraged, by the discrepancies between the existing leniency programmes within the ECN, from applying for leniency. This is not an easy and clear-cut solution to the problem of consistency among the cartel prosecution and leniency policies of different jurisdictions within Europe, but it is an important step towards eliminating contradictions that might jeopardize the enforcement system as a whole.

103 See: http://europa.eu/rapid/pressReleasesAction.do?reference=IP/06/1288&format=HTML&aged.

5. CONCLUSION

What are some of the insights that the experience of the Bundeskartellamt can offer? A lesson to be considered is that political and economic circumstances can impact competition policy in unforeseeable ways, and the competition enforcement system should remain flexible and nimble. This is illustrated by the process that followed German reunification, where German competition authorities not only had to deal with a surge in merger activitiy, but also where a competitive system was introduced into the new *Länder*. We see a current example today, where the still fragile financial system has prompted some stakeholders to downplay the importance of competition policy, or to suggest that certain aspects of it be placed on hold.

In a similar vein, competition authorities need to remain aware of what the most pressing competition issues are, and be prepared to recalibrate their priorities accordingly. While it was necessary for the Bundeskartellamt to devote a large share of its resources to merger control at certain periods, this also meant that fewer resources were available for combating cartels. This, in turn, necessitated a refocusing at a later stage, which the Bundeskartellamt did through organizational adjustments and the introduction of new enforcement tools.

When designing enforcement tools, e.g. in the field of cartel prosecution, there must be awareness of the fact that all of the tools, taken together, form a complex system. The constituent sub-systems and elements need to be complementary, and not work against one another. Thus, when a new instrument is introduced into competition policy – such as a leniency programme, or the possibility of private enforcement – it must be considered how this tool will interact with the existing enforcement system, and whether, overall, the system will be strengthened or weakened.

Bruno Lasserre

MAKING THE MOST OF THE FRENCH ANTI-CARTEL ENFORCEMENT PORTFOLIO[104]

1. INTRODUCTION: THE ECN FIVE YEARS ON

The European Competition Network (the "ECN") has just turned five years old. It is still a tender age. And yet, the pace at which it has grown and developed over this period is impressive. In fact, if I had been asked to take a look at antitrust enforcement five years ago, I am not sure that I would have ventured to speak about "making the most of our anti-cartel enforcement portfolio", as I will briefly try to do in the following pages. And if I had done so, at least in front of the French audience, a number of people might have wondered what I meant.

Why is that so? After all, the *Conseil de la concurrence* has been around for more than twenty years – twenty-two exactly – before being transformed, on 2nd March 2009, into a strengthened *Autorité de la concurrence* empowered to launch dawn raids, to handle merger control and to make market studies and sector enquiries, in addition to adjudicating antitrust cases, all that in full independence from the government. So there is no doubt that, in 2004, the *Conseil* already had a long story of issuing antitrust decisions, be it in relation to secret cartels and other horizontal or vertical agreements, or with respect to abuses of a dominant position.

Nonetheless, during its first fifteen years of existence, I do not think that it considered itself, for a number of reasons, as being an antitrust "enforcer" as such.

First of all, it is clear that, by and large, the *Conseil* viewed itself – and was seen by market players – as a body entrusted with the mission of applying competition law, much in the same way as a judge would do, in cases overwhelmingly brought to him by way of a complaint. It differs significantly from the function consisting in shaping and enforcing a competition policy.

Competition policy is, of course, based on the implementation of a set of rules, but it means something more than just applying these regulations.

104 This article is based on a speech delivered at the International Competition Law Forum (ICLF) organized by the Polish Office of Competition and Consumer Protection (UOKiK) on 15 and 16 April 2009 in Warszawa, Poland. The oral character of the speech has been retained.

The job of competition policy-makers does not stop with the interpretation and implementation of antitrust law. The ultimate goal is to guarantee that markets work competitively or, in other words that the free market economy that we have collectively chosen as our economic system operates to the benefit of consumers. So ideally, the way in which policy-makers interpret and implement competition rules should be guided by a set of pre-defined objectives, priorities and strategies, all carefully selected in order to best secure this result.

For the same reason, competition enforcement agencies should not remain confined to the handling of the individual cases that are brought to their attention by market players, because the sum of these individual requests does not necessarily coincide with the general interest that their mission commends them to promote. Complaints can give public enforcers a good signal that there exists a problem in a given sector, or simply bring useful information to their knowledge, but they can also detract them from focusing on issues that are crucial for consumers, and in any case overburden our limited resources. Therefore, competition agencies should be empowered not only to open their own investigations, but also to tackle other projects, including both broader interventions such as market studies and inquiries, as well as advocacy and compliance tools such as communication, guidance, etc.

Second, apart from the possibility of finding an infringement and imposing a fine, which is the minimum toolkit of any competition authority, the *Conseil* has long lacked an actual portfolio of anti-cartel enforcement instruments as such. It might come as a paradox that, contrary to many jurisdictions where collusion cracking is historically more developed than surveillance of unilateral conduct, French competition rules have traditionally provided for a toolkit far more adapted to single firm cases than to cartel cases in the large sense (i.e. including both secret conspiracies strictly speaking and other horizontal or vertical agreements). Most notably, the *Conseil* enjoys a long experience of enacting interim measures and imposing injunctions or remedies in abuse of dominance cases. This has proven very useful in shifting away from post-World War II monopolies and steering the French economy towards full competition, particularly in the 1990's and early 2000's. By contrast, although the *Conseil* has also been very active in the fight against cartels, it had, until 2001, no possibility of handling those cases otherwise than via fines.

Today, the *Autorité*, as well as the European Commission (the "Commission") and the other National Competition Authorities (the "NCAs") that form part of the ECN, and indeed other antitrust agencies in the world, are increasingly considered – and self-consciously view themselves – as competition "enforcers", that is as bodies commissioned not only to apply a given set of rules, but also to frame a policy intended, ultimately, to deter firms from breaching antitrust law and to induce them to put competition at the heart of their business, in a way that benefits consumers.

At the same time, an increasing number of competition agencies throughout the world have at their availability a broad set of utensils designed – and in fact perpetually complemented, adjusted and optimized – to help them achieve this goal. As a result, they devote increased attention to building strategies intended to maximize outcomes for consumers while minimizing costs, for instance by choosing which cases to pursue and which tools to implement.

In a nutshell, European competition authorities find themselves, only five years after coming into force of Regulation No 1/2003, in a world that differs significantly from the one they knew beforehand. The ECN has, if not revolutionized the way in which they think and act, at least opened their eyes and minds. It is with this backdrop in mind that I would like to devote a bit of attention to current anti-cartel activity and challenges, from two different viewpoints: the one of agencies and the one of consumers. In doing so I will draw at times on the French experience, with which I am well acquainted. Surely, however, some of what I will elaborate on will correspond to the experience of many other competition authorities in the world.

2. HOW TO BUILD TOMORROW'S SUCCESS ON TODAY'S ACHIEVEMENTS?

The enforcement portfolio available to competition agencies now comprises an impressive number of tools. Schematically, these instruments serve three purposes.

In order to detect potential cartel cases, authorities can count *inter alia* on complaints (from all market participants of course, but also from representative businesses or consumer associations, as well as from public bodies), on "type 1" leniency (that is, on first-coming firms that reveal the existence of a conspiracy by bringing the proof necessary to trigger an inspection or to ground a finding of infringement) and possibly also on sector inquiries, as evidenced by some of the investigations that fled from the European Commission's enquiry devoted to energy markets.

In order to build cases up, authorities can rely *inter alia* on "type 2" leniency (in other words, on second- or third-coming firms that adduce evidence bringing added value to the file), on dawn raids and on softer investigative techniques (e.g. requests for information, interviews, etc.). Finally, in order to adjudicate cases, the agencies can use *inter alia* fines, settlements and cease and desist orders.

Of course, all of these tools, which are now common to most European competition authorities, can be supplemented by other means when enforcement is not solely administrative, but also includes a criminal dimension – an issue which I will address at a later point.

I will not detail each of these tools individually, but will briefly mention how some of them could be further mobilized by competition authorities in the context of their continued effort to step up anti-cartel enforcement. I will look at this issue from the perspective of the two main avenues that are open to agencies for reaching their goal of keeping markets firmly on the path of efficiency and consumer welfare. As you know, our "stick and carrot" approach consists, on the one hand, in deterring firms from behaving anti-competitively and, on the other hand, encouraging them to behave pro-competitively.

2.1 REINFORCING THE BUILDING BLOCKS OF DETERRENCE

Deterrence is the most immediate objective of competition authorities. Firms that engage in cartel activity must end up, or at least know that they run the significant risk of winding up, paying a price which exceeds the benefit that they have made, or can expect to make by breaking the law. It is only if such objective at least approximated, that consumers will be better off. So, the firms whose practices are considered unlawful must be treated in a way that makes them unwilling to reiterate. At the same time it gives other companies a strong signal that engaging in conspiracy is not risk-free or risk-manageable. This is the classical distinction between "direct" or "individual" deterrence and "indirect" or "general" deterrence.

Obviously, the problem is that whichever form of deterrence you are thinking about, it can only be achieved if competition agencies are able to detect cartels and to amass the level of evidence that is needed in order to establish their existence, and thus to fine them. Economists estimate the level of uncovering of conspiracies as being relatively low. I have read figures running in the range of 15 to 20 percent. So, one of our key targets must be to bring this figure up to a satisfactory level. It is not necessary to rise it to a 100 percent – and this is hopeful, because such a challenge would be daunting. Simply, the goal is to reach a level that is high enough to make firms realize that the threat of detection is real and that, if exposure materializes, it will most probably lead to a substantial fine.

Large companies are better prepared and advised than ever to limit the chances of being caught via dawn raids. They got acquainted with our typical investigation techniques, and, by and large, have developed sufficient expertise to anticipate our moves, as an experienced chess master would do. For example, it was recently uncovered that some of the companies employ specialized consultants to organize the daily functioning of cartels and make sure to leave no trace behind. As they developed more sophisticated ways of securing secrecy, competition authorities had to revolutionize the tools in their hands, to be cleverer than the smart boy. How can we continue to move forward on these issues?

2.1.1 LENIENCY

As mentioned before, since I took office in the Summer of 2004, the *Conseil* has made it a core priority to intensify anti-cartel enforcement, in line with what has happened over the same period in many other jurisdictions.

Corporate leniency has tremendously helped in that respect. It is agreeable that it is the biggest competition "hit" of the past decade. The programs were virtually unheard of ten years ago on this side of the Atlantic, except in Brussels and perhaps in a couple of other places. Since then, a Model Leniency Program has been adopted by the ECN in September 2006, pursuant to a project co-chaired by the French *Conseil* and the UK Office of Fair Trading (OFT). Today, this immunity scheme has been imported by most NCAs which have built their antitrust policy on the basis of this common European framework. A recent report published by the ECN shows that the level of convergence achieved in that respect in just three years is impressive.

In France, corporate leniency had been introduced by way of legislation as early as 2001. However, this provision really started to come to life only once the *Conseil* had enacted amnesty guidelines in April 2007, immediately following the publication of the ECN scheme. Since that date, our program has proven increasingly attractive. Leniency seekers have fed a strong pipeline of cases, and it does not look like as though this is going to stop: in 2008, which is the last year for which a consolidated figure is available for the time being, the agency has received 18 applications from French and foreign companies, not counting summary applications that should end up being handled by a better-placed competition authority within the ECN. This equals all the requests received in the preceding years altogether.

Part of this success is due to the marker system, which provides applicants with a guarantee as to whether they are the first through the door, and to the *Autorité*'s practice of granting conditional leniency opinions very early in the process, which gives conspirators a full predictability as to the outcome of the case provided that they cooperate all the way through. Accordingly, no significant changes to our current leniency policy are foreseen in the near future.

Apart from being attractive, the French corporate leniency program has also proven very effective. It has enabled the agency to boost the detection of hardcore cartels and to significantly accelerate and facilitate the handling of such cases, thanks to the cooperation of applicants. Intense enforcement triggered afterwards has joined force with prosecution pursuant to *proprio motu* investigations, leading to an unprecedented number of high profile convictions, featuring landmark cases such as the *Mobile Phones* cartel (2005), the *Doors* and *Heating Systems* cartels (2006), *International Removers* cartels (2007) and the *Air Fuel* cartel (2008), as well as several major bid-rigging cases in the construction and public work industries. Of the landmark cases, two (the *Doors* and *International Removers* cases) are the result of "type 1" leniency applications.

A third case has recently joined them: the *Steel Trade* cartel (December 2008), in which fines totaled 575 million euro. The investigation once more illustrates that conspiracies are immensely detrimental to consumers as well as to the economy as a whole, by illegally depriving a vast mass of customers from the benefits attached to competition in terms of innovation, price and choice quality. In essence, the Authority found that between 1999 and 2004 the main players on the French steel wholesale trade market had colluded in order to fix prices and to carve up the entire country. During all those years, the thousands of small- and medium-sized enterprises that depend on them – ranging from building constructors to key makers – were deprived of the benefits of competition and charged with overprices amounting to hundreds of millions of euros. None of them was able to resist the very comprehensive and sophisticated schemes set up by the cartelists in order to make certain that nobody would slip through (e.g. national, regional, and local meetings, including ones through specialized professional trades that provided logistical support to the conspiracy; dissimulation through cover offers; refined monitoring and control mechanisms; sanctions in case of deviation, etc.).

None of this should happen again. This is why each cartel case spotted must be used as an opportunity, not only of putting an end to the practices at stake, but also of voicing a clear message that enforcers are uncompromisingly committed to strongly punishing firms that collude to artificially fix prices, share markets, or ration demand.

2.1.2 LOOKING BEYOND LENIENCY

However, the issue raised may be perceived twofold, as there are many things to do besides waiting for leniency applications to pour in if the goal is to bring in new cases and secure their outcome to the benefit of the consumers.

2.1.2.1 SETTLEMENTS

I will now devote a few observations to commitments, which are taking speed and must now live up to its promise. This modus operandi, set up in France in 2001 and much in the same way as the settlement package introduced at the European level in 2008, allows the *Autorité* to terminate cases by allowing firms to waive their right to contest the charges brought against them in exchange for a streamlined procedure and for a reduced fine. But the French Code of Commerce provides for an additional element of compliance. It allows companies that contemplate entering into a settlement with the agency to choose between two formulas: either they simply offer not to challenge the charges notified by the Investigation Services of the *Autorité,* in exchange to which they can expect a fine reduction, or they not only accept to waive their right to contest the objections, but also undertake to modify their future behavior on the market, for an additional financial sanction decrease.

The current experience of the *Autorité* suggests that this supplemental element of flexibility makes sense. There clearly are cartel cases (or bid-rigging ones) where commitments can bring added value, for instance by fostering greater antitrust compliance on part of the firms involved in the principles of competition law. Such pledges may take the form of "compliance programs" strictly speaking, that is of internal measures intended to make sure that insiders know competition rules, undertake to abide by them, report alleged violations to their superiors, etc. I will come back to this specific issue at a later point. Yet, the *Autorité*'s recent practice shows that there are cases where pledges can achieve conformity in a wider sense, for instance when they take the form of behavioral commitments governing the future interaction of the firm with its competitors. For example, a pledge taken in the steel trade case was of particular novelty. In this respect, one infringer committed to leave a professional association if its internal rules were not sufficiently modified to secure any possibility of future collusion between its members during the association's regular meetings. Of course, commitments do not have to be accepted only because they are offered by the parties and seem satisfactory and useful. Their added value has to be carefully weighed also against the burden that they could imply, notably in terms of monitoring. But the issue is worth considering.

On average, between one-fourth and one-third of all cartel cases adjudicated by the *Autorité* each year are now closed by way of a settlement. So, the agency has built sufficient practice to contemplate publishing guidance on the policy, in order to give companies and consumers a clearer view of what advantages they can gain from entering into a settlement, and how the process operates in practice.

But from a point of view of enforcers, it is in any case already evident that settlements can be very useful, provided that certain conditions are met in order to avoid drawbacks:

- you can start negotiating with one firm only, but you should target a settlement with all the companies involved in the case; otherwise, you may end up doing even more work than without an agreement;

- the settlement should be clear and unambiguous, and it should be finalized within a short deadline; otherwise it risks being used in a dilatory fashion;

- the discount granted to the parties in exchange for the waiver of the right to challenge the charges should be sufficiently attractive, but it should not jeopardize the attractiveness of leniency, which should remain number one objective;

- ideally, the parties should commit not to challenge the fine in court; the fact that this is not provided by the law does not necessarily prevent agencies from reaching an agreement with the firms concerned in that respect.

2.1.2.2 SECTOR INQUIRIES

Sector inquiries may serve a number of purposes. They may be performed in order for competition authorities to gather more abundant information on the situation on a given sector, to enter into a fact-intensive dialogue with market players and other stakeholders, to gain insight on the competitive issues that arise or could arise, and/or as a "screen" for potential individual breaches of the antitrust law. So they are not intended solely, or even mainly, for the purpose of triggering stand alone case-specific enforcement.

Depending on the objective or set of aims that lead the antitrust authority to launch a given sector inquiry, the unwinding of this kind of analysis has to be carefully approached. In some cases, it will be mainly cooperative (i.e. relying on information voluntarily submitted by stakeholders); in others, it will be more constraining (i.e. requiring stakeholders to provide information); and usually, it will contain a dose of cooperation as well as constraint.

The first action undertaken could well be the coupling of *ex officio* sector inquiries with dawn raids. For instance, the recent review of the pharmaceutical industry performed by the European Commission has led it to launch dawn raids, as provided for by Regulation No 1/2003. A final report has been issued and we now have to wait and see what action, if any, is taken by the Commission on the basis of the findings, before being able to measure the exact results and added value of the market analysis. What this means is that sector inquiries are long-term investments that do not necessarily yield immediate results. But a reading of the Commission's final report shows that the inquiry has enabled it to put together a more detailed picture of the current competitive landscape than would have been the case without these dawn raids, in terms both of intellectual understanding of how market strategies are devised and implemented, and of documentary evidence of what actually happens on the marketplace.

As for the *Autorité,* the modernization of the French competition enforcement framework that took place in 2008/2009 has given it a wide power to perform investigations and dawn raids, which can be undertaken either in the context of cases regarding an individual firm or the competitive situation of a given sector, as well as in the context of a market study.

These two examples illustrate that, although the rules and processes applicable to each European antitrust authority may differ to a significant extent, modern competition legislations strive to put the agencies in a position where they can, first, build their own cases and, second, build a multidimensional course of action at the same time. This can enable them to learn (a lot) more and a (little bit) more easily about the actual arrangements entered into by market players, be they either contracts, which are of course not secret cartels but may nonetheless be both previously unheard of and problematic for competition, or straightforward price-, market- or consumer-manipulating agreements.

2.1.2.3 BILATERAL COOPERATION

Another tool that could prove useful is bilateral cooperation between NCAs. It routinely occurs that agencies give a hand to the Commission during the investigative process. It is essential not to forget that Regulation No 1/2003 also sets up useful mechanisms for NCAs to help one another by joining forces during their own on-the-ground legal actions.

To date, there have been a few investigations where the *Autorité* has cooperated with other NCAs. In one noteworthy case, but for this cooperation, the French agency would not have been able to sanction some serious anticompetitive conducts artificially inflating flight fares for consumers. The matter involved some of the key players in the oil sector, who were believed to have colluded by fixing overcharges on the aircraft fuel market in the French overseas departments. Although the inspections that took place in France yielded no significant results, the agency was able, in the end, to prove the infringement thanks to a body of evidence gathered in the United Kingdom, as a result of the cooperation on the basis of Article 22 of Regulation No 1/2003. This allowed us to fine the firms concerned for a total of 41 million euros in December 2008.

The case was challenged before the Paris Court of Appeals, which confirmed all aspects of the decision, and specifically the implementation of Article 22. In particular, the way in which such a cooperation is controlled by national review benches was clarified. In essence, the French court can be called upon to judge both the legality of the initial request for assistance issued by the French NCA and the way in which the information obtained is subsequently used to ground the decisions, while the UK court can, if requested, review the actual authorization and carrying out the inspection on the British territory. In the present case, the Court of Appeals concluded that the French agency had rightfully requested the OFT's assistance and that the evidence obtained indeed grounded the findings as to the existence of an anticompetitive practice.

Of course, since the NCA's powers are greater under Regulation No 1/2003 when it applies European competition law than when it investigates solely based on the French Code of Commerce, companies will increasingly challenge the decisions on the ground that the practices at stake do not affect trade between the EU Member States. The broad interpretation of this notion by the Court of Justice, coupled with the NCAs' focus on cases that are liable to cause significant harm to competition and consumer welfare mean that this should not be an issue in cartel investigations. Still, it points to the fact that, if the objective is to achieve greater efficiency in terms of enforcement, all NCAs need to devote greater attention to the matter of how to secure further convergence of the rules and practices.

2.2 ADVOCATING A CLEAR ALTERNATIVE TO ANTICOMPETITIVE CONDUCT

Some audiences may be astonished to hear about advocacy in relation to conspiracies. But from our point of view, tools such as for instance compliance programs may also be part of the picture of anti-cartel enforcement. Of course, a degree of caution (and precaution) is needed. Turning up to the enforcer and promising not to do it again is not worthwhile. Simply undertaking, in the context of a settlement package, to start an e-learning program may not lead an enterprise very far either in terms of fine reduction. On the competition authority's side, it proves necessary to think twice before systematically imposing compliance programs without ensuring that it shall have the will or the means to monitor them.

As a general reminder, it should be first noted that commitments are not only useful ancillary complements to the settlement procedure. They are also the core element of an autonomous modus operandi which allows the *Autorité* to end cases prior to finding any infringement when companies come forward with constructive business solutions aimed at guaranteeing or restoring competition well before their behavior has caused significant consumer harm. The French Code of Commerce clarifies that this procedure is totally devoid of any incriminatory nature insofar as commitments are meant to put an end to competition concerns expressed by the antitrust agency based o its preliminary assessment of the case, and therefore well before any charge or objection would be notified to the firm(s) concerned.

This means that the agency's decision cannot be used by private plaintiffs in order to ground a claim for private damages. In fact, the decision normally limits itself to explaining that the *Autorité* had a number of anticompetitive concerns that were met by relevant, trustworthy and workable commitments offered by the firm affected, thus enabling the *Autorité* to close the case.

Given its nature and purpose, it is manifest that this procedure, taken as a whole, is not suited for cartel cases. In fact, they are specifically excluded from its scope, as recalled both by Regulation No 1/2003 and by the guidelines that the *Autorité* published in 2008 on antitrust commitments. This does not mean that pledges, in themselves, are not worth interest in the context of cartel cracking.

Indeed, our experience of the last three years shows that there are cases where the carrot can be a useful complement to the stick. As mentioned earlier, according to French law, antitrust settlements can include commitments, and this legal framework can be used in order to stimulate the launch of compliance programs, under strict conditions relating to their credibility and verifiability.

Of course, it is not difficult to imagine instances where such programs do not seem to be plausible, for example when the French authority is faced with a multi-recidivist firm that has breached previous compliance commitments. But this does not entail "throwing the baby with the bathwater." There are distinct cases where we can expect compliance pledges to be positive. In fact, between 2006 and 2008, almost twenty cartel settlements reached by the *Conseil* included extensive compliance commitments coupled with behavioral commitments. For instance, in a case involving companies in charge of industrial laundering, the *Conseil* accepted pledges from the parties to reorganize their business in a way that would prevent them from further collusion as well as pledges to launch extensive compliance programs, including whistle-blowing.

The French authority has now moved on to fitting these cases in a structured policy. In September 2008, an independent study commissioned on the topic of compliance was released. The aim was to measure its actual degree of development in France, its perceived benefits and costs, conditions of success and potential pitfalls, etc. The study was well received. We are now into the process of putting together a draft guidance document that will aim at setting out our views on compliance and the way in which it can bring a "plus" to cartel enforcement. If this advocacy activity can contribute to deterring a fraction of firms from engaging in conspiracies thanks to conformity, it will be worthwhile.

3. EMPOWERING CONSUMERS AND JUDGES

Now, let me take a step back and look not at public enforcement instruments, but at the wider anti-cartel portfolio available to all market participants. Our mission is to enhance consumer welfare by making markets work better. Consumers – in its economic sense, the term includes end users as well as other market players operating at an intermediate stage of the value chain – have the choice of coming to us or going to other public institutions. In many EU Member States, independent administrative agencies are at the heart of the competition enforcement process. However, it should be remembered that antitrust agencies are a part, fundamental, but by no means necessarily sufficient, of the portfolio of institutions and people in a position to help them assert their rights.

Let me have a brief look at other possibilities. We are dealing here with prospective issues, that is why the outline will be brief. Yet it will also clearly express my beliefs on criminalization and private enforcement.

3.1 CRIMINALIZATION OF ANTI-CARTEL ENFORCEMENT

The French *Conseil* was created following the decriminalization of French competition law in 1986. Since then, administrative enforcement has been at the heart of antitrust enforcement. The reform of the system that occurred in 2008/2009 has led the French Parliament and Government to give the *Autorité* a clean bill of health. This results in an improved legislation that provides the agency with greater powers and resources, and in a number of policy statements that distinctly support an active competition enforcement on the *Autorité's* part.

This does not mean that criminalization is ruled out. When I was heard by a special committee appointed to deal with further decriminalization of French business law, over a year and a half ago, I advocated just the contrary. To be exact, I stated that, as regards antitrust law, the issue was not to "decriminalize", but rather to move towards "more targeted and more effective criminalization" – i.e. to criminalize "better" rather than "less". This is because I believe that there are cases where a fine is just not sufficiently effective. In such instances, the perspective of a jail term and the moral stigma that it entails could be a valuable complement.

French competition law allows criminal judges to go down that road, although they still rarely do so in practice at the current stage. In my mind, making greater use of this tool entails two things: first, adapting it to contemporary challenges and, second, having a clear view on how to actually enforce it.

3.1.1 OPTIMIZING CRIMINAL LEGISLATION

French criminal antitrust enforcement, which is under the responsibility of criminal judges, is currently limited. The law provides that individuals who personally play a decisive part in the conception or operation of a corporate antitrust breach can be fined or jailed for a maximum of four years. But implementation is scarce.

As I hinted earlier on, that could change soon. The president of the Republic commissioned a report on the future of criminal business law, which was issued in January 2008 and which contains a number of interesting proposals on the antitrust front. Many of them are consistent with the suggestions that I made on behalf of the *Autorité* when I was heard by the members of the above-mentioned special committee on the future of criminal business law. In summary, they suggest a move towards a more targeted and efficient criminalization. For the time being, maximum fines are too low to ensure deterrence (75,000 euros). In addition, any type of antitrust infringement can currently give rise to criminal proceedings, including not only cartels and bid-rigging, as in many other jurisdictions, but also any type of vertical restraint or unilateral conduct, despite the complex issues to which they may give rise. This is worth being discussed. Are individuals who know from the start that they are acting unlawfully (as is the case when they enter into a cartel or participate in bid-rigging) and people who can honestly have doubts as to whether or not their behavior is illegal, to be treated exactly in the same way?

A draft bill is now being prepared by the French Ministry of Justice. Things will certainly take a bit of time, but taking this time is essential, because the issue is critical. One of the main suggestions is to set up a leniency program for individuals. It is a difficult matter, because criminal enforcement often comes after administrative enforcement. But individuals who take the decision of opting for corporate leniency and cooperating with the *Autorité* are often the same persons who could be prosecuted under criminal law once the authority has rendered its cartel decision. Today, they are put in a very paradoxical position: as corporate officers, they know that they can gain a lot from leniency, because it allows their firm to avoid a fine; but as individuals, they have much to lose, since it will trigger prosecution against them.

Let me say it clearly: effective anti-cartel enforcement cannot afford schizophrenia. It is critical to guarantee these people, from the very beginning, that they will also benefit from individual leniency if they cooperate with the *Autorité*, and state under which conditions they will benefit from this protection. If not, the effectiveness of the French leniency program will remain limited by this hurdle.

3.1.2 TURNING CRIMINAL LAW INTO ACTUAL POLICY

But having a piece of legislation is not enough. Guidance and signals on its implementation are necessary too. Today, when judges apply the provision on criminal antitrust enforcement, they often bundle a number of infringements together: competition law may be part of the package, but frequently other factors trigger the prosecution and ultimately the conviction. Often, it is bid-rigging or corruption. It would be helpful if the Ministry clarified its policy and if judges reasoned their decisions in a way that unequivocally indicates the relative weigh of competition law in their judgments.

Another point on which progress could be made is the actual conviction. Imposing a fine is one thing, but the perspective of a jail term is another. Things seem to be moving. In a recent judgment concerning a major bid-rigging case adjudicated by the *Conseil* in 2007, a court has ordered, for the first time in a few years, a suspended jail term. This is a good signal. It should not remain isolated.

But there are many other items worth considering. The specialization of criminal judges in economic law and competition law, which is also contemplated by the draft bill I mentioned earlier, is also a move that could help build momentum and experience.

3.2 PRIVATE ENFORCEMENT

My last point is for private enforcement. It is common knowledge that it is the second leg of competition law, besides public enforcement. Systems, much in the same way as human beings, must use both of their legs.

It was revealed by the press that the European Commission is finalizing a draft directive on private enforcement. This is excellent news, which will also stimulate the thinking at national level. I will not get into the details, which will no doubt give rise to intense discussion.

As national enforcer, I want to stress one specific point. As with human beings again, the two legs of our enforcement must be coordinated. Otherwise, standing up and walking will be risky. Allowing victims to claim damages when they have suffered from a cartel, as in the case for any other type of tort, is an extremely important element of trust in our system, which is governed by the rule of law and based on the imperative of liability for injuries caused to others. Simultaneously, it is crucial for competition enforcers to ensure that such claims are well coordinated with public enforcement, so that private interests do not clash with the public interest.

Finally, as is the case for criminal enforcement, having a piece of legislation will be a huge step forward, but by no means sufficient. Judges and consumers will need to empower themselves, by using all the tools that are available to them. All competition enforcers must help them, and can do a great deal through advocacy – for instance by calling on consumers to take action once a cartel has been found, as was done in the *Autorité's* press release relating to the decision in the steel trade cartel.

4. CONCLUSION

Effective competition enforcement is, at most, only halfway through the journey. The short picture that I have brushed above shows that a great deal has been done in five years, and we should be happy about it. But it also recalls that there is much more to be done in order to meet consumer expectations in the field of anti-cartel enforcement. We must remain dedicated and, above all, we must continue to work together.

Grzegorz Materna

COLLECTIVE MANAGEMENT OF RIGHTS – THE ROLE OF THE COMPETITION AUTHORITY AGAINST THE BACKGROUND OF COPYRIGHT LAW

1. INTRODUCTION

The President of the Office of Competition and Consumer Protection fulfils its task consisting in competition protection in line with the rules specified in the Act on competition and consumer protection ("Competition Act")[105] basically with respect to all economic operators ("undertakings") and in all sectors of economy[106]. This general rule is subject to restrictions. Due to the specific nature of some markets, sector-specific regulations are adopted, which may rectify the application of rules resulting from the Competition Act. As a result, there appears a question on the role and scope of the powers of the competition authority to influence the activities of undertakings operating on such markets.

This paper covers only a fraction of this broad topic, i.e. the role of the President of the Office of Competition and Consumer Protection as regards cases concerning the provision of services related to the collective management of copyright and related rights by collecting societies ("CSs").

The activity of CSs has been reviewed by the President of the Office of Competition and Consumer Protection as regards their compliance with the Competition Act. When using the instruments provided in the Act with respect to CSs, it is necessary to bear in mind that CSs in Poland carry out their activity on the basis of the Act on Copyright and Related Rights ("Copyright Act").[107]

Considering the role of the competition authority in collective management of rights in the context of the provisions of the Copyright Act, this paper will, in the first place, analyse whether and in what manner the provisions set out in the Competition Act define its relationship to other legal provisions significant

105 Act of 16 December 2007 on competition and consumer protection (Dz.U. No. 50, item 331 as amended).

106 D. Miąsik (in:) T. Skoczny, A. Jurkowska, D. Miąsik (ed.) *Ustawa o ochronie konkurencji i konsumentów. Komentarz*, Warszawa 2009, p. 81.

107 Act of 4 February 1994 on copyright and related rights (consolidated text Dz.U. of 2006 No. 90 item 631, as amended).

from the perspective of the CSs' activity. Next, this paper will classify antitrust cases concerning the collective management of rights on the basis of the existing case law. When analysing the case law, the paper will indicate which specific activities of the CSs were covered by the investigations carried out by the Polish competition authority (i.e. which activities of CSs were recognised by the President of the Office of Competition and Consumer Protection as falling within his powers and assessed from the point of view of their compliance with the Competition Act). On the basis of the classification adopted, I will analyse the Copyright Act to find some provisions that may exclude or restrict the jurisdiction of the President of the Office of Competition and Consumer Protection with respect to investigating specific categories of cases concerning CSs.

2. ROLE OF THE COMPETITION AUTHORITY IN CASES CONCERNING CSS IN THE LIGHT OF THE COMPETITION ACT

To establish the role of the competition authority in cases concerning CSs it is necessary to analyse the provisions included in Competition Act. From the perspective of the topic of this study, two provisions of the Act are especially significant, i.e. Article 2 and Article 3. The former defines the relationship between the restrictions of undertakings' activity set out in the Competition Act and the intellectual property rights. Whereas Article 3 determines the relationship between the restrictions provided for in the Act and other legal provisions, hence also the Copyright Act.

Article 2 of Competition Act sets forth the principle of inviolability of the existence of intellectual property rights and non-intervention of competition law into the area of the entitlements that follow from these rights[108]. Pursuant to Article 2(1), the Act *"is without prejudice to the rights vested pursuant to the provisions concerning protection of intellectual and industrial property rights, in particular the provisions on the protection of (...) copyright and rights related to copyright."*[109]

108 D. Miąsik (in:) T. Skoczny, A. Jurkowska, D. Miąsik (ed.) *Ustawa o ochronie konkurencji i konsumentów. Komentarz*, Warszawa 2009, p. 73.

109 When interpreting this provision the Supreme Court states that the Competition Act does not violate, in particular *"the economic rights tied to copyright, mainly the exclusive right to use the work and manage it in all areas of exploitation which is enjoyed by the author, as well as the right to remuneration for the use of the work (Article 17 of the Copyright Act)"*, and hence it does not violate the *"rights of the authors to receive royalty for broadcasting non-dramatic musical works and for using these works, the copyright to which is collectively managed by [CS] (…). The act also does not violate the rights of CSs, which are set out in the copyright, including the right to manage and protect the rights covered with a consent for collective management (Article 105(1) of the Copyright Act)."* See judgement of the Supreme Court of 2 April 2009 (III SK 19/08), unpublished.

The inviolability of the existence of intellectual property rights does not imply that competition protection law shall not apply in areas where intellectual property rights are exercised. According to Article 2(2), antitrust control is exerted over the scope of making use of intellectual property rights by these rights' exclusive holder[110]. In the light of this provision, the Competition Act applies to agreements concluded between undertakings: *"in particular licence agreements, as well as to other practices concerning exercising rights referred to in Paragraph 1 (...) where such agreements result in an unjustified limitation of freedom of business activity of the parties, or in a significant restriction of competition within the market."* Based in this wording and the case law of the Supreme Court, the powers of the President of the Office of Competition and Consumer Protection cover enforcing the prohibitions, defined in Competition Act, to carry out competition-restricting practices with respect to *"licence agreements and other agreements concerning the amount of remuneration received by the author or other entitled entity, because the amount of compensation for creative efforts or the financial risk associated with developing the work does not constitute the essence of copyright, and copyright law only awards the entitled entity the right to remuneration without reserving this entity the exclusive right to determine the amount of the remuneration."*[111]

The above discussion leads to a conclusion that in the light of Article 2, the issues associated with execution of intellectual property rights, in particular copyright and related rights, may be investigated from the point of view of the prohibition to apply competition-restricting practices set forth in the Competition Act. Also in practice, such cases were considered by the President of the Office of Competition and Consumer Protection. Let us take for example: i) a case concerning a licence agreement concerning a trademark and know-how related to the production and sales of yoghurt (it was discovered that the provisions of the agreement are an example of competition-restricting practices that consist in imposing onerous contract terms and conditions, allowing the party to gain unjustified profits[112]; ii) a case concerning undertakings that included a ten year non-competition clause in a contract for the sale and licensing of economic rights tied to copyright, rights to trademarks, know-how and other assets serving operate a publishing activity[113]. Also the activity carried out by the CSs has repeatedly been examined

110 See judgement of the Court of Competition and Consumer Protection of 21 January 1998 (XVII Ama 55/97), calendar of causes 1999/2/48.

111 Judgement of the Supreme Court of 2 April 2009 (III SK 19/08), unpublished.

112 See judgement of the Court of Competition and Consumer Protection of 21 January 1998 (XVII Ama 55/97), calendar of causes 1999/2/48.

113 Judgement of the Court of Competition and Consumer Protection of 29 May 2006 (XVII AmA 9/05), Official Journal of the Office of Competition and Consumer Protection 2006/4/58.

by the President of the Office of Competition and Consumer Protection, which constitutes an additional justification for devoting this paper to the topic.

While Article 2 refers to regulations related to intellectual property rights, Article 3 defines the relationship between the restrictions set forth in the Competition Act and other legal provisions. The Article provides that *"the act shall not apply to impediments to competition admitted by virtue of separate legal acts."* It is an expression of the general principle that all undertakings in all sectors of the economy[114] are subject to the competition authority's powers, which is limited only by specific regulations following from other acts.

According to the established case law, other legal acts may revoke the application of the Competition Act[115]:

- by directly exempting a particular type of activity from the Competition Act's application[116] stating unambiguously that e.g. *"the provisions on competition protection shall not apply to the activity governed by this act"*[117];
- by establishing a specific legal regime validating practices which at the same time meet conditions to being recognised as competition-restricting practices by violating the prohibitions set out in Article 6 or Article 9 of Competition Act[118];
- imposing on an undertaking an obligation to act according to an order of a public authority (regulatory authority), whereas in the absence of such order, the activity of the undertaking could be recognised as a competition-restricting practice[119].

114 D. Miąsik (in:) T. Skoczny, A. Jurkowska, D. Miąsik (ed.) op. cit., p. 81; C. Banasiński, *Równoległe stosowanie instrumentów prawa konkurencji i instrumentów regulacyjnych w Polsce*, (in:) C. Banasiński (ed.) *Prawo konkurencji – stan obecny oraz przewidywane kierunki zmian*, Warszawa 2006, p. 97.

115 Cf. also: G. Materna, *Stosowanie prawa ochrony konkurencji wobec organizacji zbiorowego zarządzania – granice ingerencji organu antymonopolowego*, paper for the conference "Prawo autorskie a prawo konkurencji", Faculty of Law and Administration at Adam Mickiewicz University in Poznań and Faculty of Law at the Poznan School of Social Sciences, Poznań, 03.06.2009 (a book containing post-conference materials is being prepared for publication).

116 Judgement of the Supreme Court of 19 October 2006 (III SK 15/06), OSNP 2007/21-22/337.

117 Such a statement is included, *inter alia,* in Article 2 of the Act of 20 April 2004 on organisation of the milk and dairy products market (consolidated text, Dz.U. of 2009 No. 11, item 65) and in Article 1(1) and (2) of the Act of 19 December 2003 on organisation of the fruit and vegetables market, hops market, tobacco market and dried fodder market (consolidated text, Dz.U. of 2008 No. 11, item 70, as amended).

118 Judgement of the Supreme Court of 19 October 2006 (III SK 15/06), OSNP 2007/21-22/337.

119 In the light of the case law excluding the application of the Competition Act may follow from an order issued by a public authority for the undertaking to act in a manner which might be recognised as a practice restricting competition from the perspective of the Competition Act. However, it should be emphasised that the sole fact of establishing in the provisions of

3. CLASSIFYING ANTITRUST CASES CONCERNING COLLECTIVE MANAGEMENT OF RIGHTS

The cases concerning collective management which were examined by the Polish competition authority[120] may be divided into the following categories: a) cases concerning the relationship between the CSs and the users of the rights they manage; b) cases concerning the relationship between the CSs and the persons who have entrusted the management of their rights to them; as well as c) cases concerning the relationships between the CSs themselves.

3.1 CASES CONCERNING THE RELATIONSHIP BETWEEN THE CSS AND THE USERS OF RIGHTS

So far, the cases in which the competition authority examined the activities undertaken by CSs towards the users of the rights managed by the CSs were related to imposing unfair prices and unfavourable conditions of awarding licences. These cases concerned:

- Termination of a licence agreement by the Association of Authors and Composers „ZAiKS" in order to force the licensee to accept the conditions imposed by ZAiKS and pay the disputed amount due[121]. In the judgement of 20 December 1995 (XVII Amr 49/95) the antitrust court overruled the decision of the competition authority, which recognised the above-described activity to be a competition-restricting practice;

- Collecting from the organisers of concerts and other events royalties in the amount of 8% of the gross income from ticket sales by ZAIKS[122]. In the judgement of 1 April 1998 (XVII Ama 35/97) the antitrust court confirmed the

law an entity with competence to influence the actions of undertakings in a given market sector does not by itself limit the possibility of the President of the Office of Competition and Consumer Protection to settle cases from these sectors on the basis of rules set out in the Competition Act. The Supreme Court stated that the Competition Act shall not be applied only when as a result of an authority's intervention the undertaking has no other possibility but to act in the manner imposed by this authority. Cf. Judgment of the Supreme Court of 19 October 2006 (III SK 15/06), OSNP 2007/21-22/337.

120 In order to see the discussion of the national antitrust case law in cases concerning collective management of copyright or related rights – G. Materna, *Praktyki ograniczające konkurencję organizacji zbiorowego zarządzania prawami autorskimi – przegląd orzecznictwa 2002-2006*, Glosa No. 4/2006, pp. 98-107; M. Kępiński, *Organizacje zbiorowego zarządzania prawami autorskimi lub prawami pokrewnymi* (in:) J. Barta (ed.), *System Prawa Prywatnego. Volume 13. Copyright. 2. edition*, Warszawa 2007, pp. 615-618.

121 Decision of the Antimonopoly Office of 26 January 1995, files sign DO-II-57/S/2/94/591.

122 Decision of the President of the Office of Competition and Consumer Protection of 6 December 1996, No. DO-II-57/S/1/94/25.

decision in which the competition authority stated that the described activity does not constitute an abuse of a dominant position;

- An application from a radio station requesting the competition authority to initiate antitrust proceedings against ZAiKS under the charge that ZAiKS imposed onerous terms and conditions in its the licence agreement, thus gaining unjustified profits[123]. In the judgement of 13 October 2000 (XVII Ama 11/00) the antitrust court dismissed the applicant's appeal against the decision in which the President of the Office of Competition and Consumer Protection refused to initiate competition proceedings in the case due to the expiry of the relevant prescriptive period;

- A music record contract whose conclusion was made subject to the licensee covering the costs of producing holograms. In this case, ZAiKS would also threaten to terminate licence agreements if the licensee did not sign an annex to the contract agreeing to cover the costs of the holograms in order to force the licensee to sign the annex to the record contract[124]. This was the first case in history of the Polish competition authority which ended in a final judgement stating that the CS abuses its dominant position[125];

- Collecting royalties for broadcasting non-dramatic musical works by ZAIKS on the basis of licence agreements with radio broadcasters ZAiKS in amount resulting from the table of royalties approved by the Copyright Committee on the basis of then effective Article 108(3) of the Copyright Act. So far, no final judgment has been made in the case. In 2002 the President of the Office of Competition and Consumer Protection ruled[126] that he is not the appropriate authority to assess the issue with respect to the prohibition competition-restricting practices. As a result of an appeal, the decision was overruled and the case was remanded to the President of the Office of Competition and Consumer Protection[127].

123 Decision of the President of the Office of Competition and Consumer Protection of 15 November 1999.

124 Decision of the President of the Office of Competition and Consumer Protection of 25 September 2002 No. DDI-82/2002.

125 Judgement of the Supreme Court of 20 June 2006 (III SK 8/06), OSNP 2007/13-14/208.

126 Decision of the President of the Office of Competition and Consumer Protection of 17 September 2002, No. DDI-77/2002.

127 Judgement of the Supreme Court of 2 April 2009 (III SK 19/08), unpublished.

3.2 CASES CONCERNING THE RELATIONSHIP BETWEEN CSS AND PERSONS WHOSE RIGHTS THEY MANAGE

The second category of cases featuring CSs which were examined by the President of the Office of Competition and Consumer Protection, were cases concerning the relationship between CSs and the persons whose rights they manage. The competition authority examined if the scope of rights delegated to CSs on their request and the length of the period after which an author or a performing artist could give up the services of a given CS was in conformity with competition law. The cases are described below:

- The first case was launched by the President of the Office of Competition and Consumer Protection on the request from the members of the band Brathanki and ended with a final and binding decision[128]. The case concerned the fact that ZAiKS made the collective management of copyright to musical works and to works composed of words and music dependant on being awarded the exclusive authorisation to manage the exploitation of these works in areas specified by ZAiKS. The competition authority ruled that the activity violated the prohibition of applying competition-restricting practices [129];

- In the second case, the President of the Office of Competition and Consumer Protection stated[130] that the rules of collective management of copyright to photographs applied by the Association of Polish Art Photographers violated the prohibition of making competition-restricting agreements. They limited the authors' freedom to entrust the CS with the collective management of their rights only with respect to selected areas of exploitation. The decision is final and binding;

- Also another decision of the President of the Office of Competition and Consumer Protection concerned the fact that CSs limited their clients' freedom to entrust the collective management of their rights with respect to selected areas of exploitation. In a decision that is now final and binding[131], the President

128 Decision of the President of the Office of Competition and Consumer Protection of 16 July 2004, No. RWA-21/2004.

129 As a result of failure to implement the decision No. RWA-21/2004 by ZAiKS within the set deadline the President of the Office of Competition and Consumer Protection issued on 24 June 2008 a decision No. RWA-19/2008, which imposed on ZAiKS a fine of 1 565 334 Polish zloty that constitutes an equivalent of 437 000 euro, i.e. 1 000 euro per each of the 437 days of delay in implementing the decision.

130 Decision of the President of the Office of Competition and Consumer Protection of 16 April 2007, No. RWA-10/2007.

131 Decision of the President of the Office of Competition and Consumer Protection of 15 February 2008, No. RWA-4/2008.

of the Office of Competition and Consumer Protection stated that the rules of collective management of rights to artistic performance of musical works and works composed of words and music applied by the Union of Performing Artists STOART violated the prohibition of making competition-restricting agreements, limiting the performing artists freedom to entrust STOART with the collective management of their rights only with respect to selected areas of exploitation;

- In another case, which also ended in a final and binding decision[132], the competition authority dealt both with the issue of the scope of rights delegated to CSs on their request, as well as the length of the period after which the entitled entity could give up the services of a given CS. The President of the Office of Competition and Consumer Protection stated that the Association of Artists Performing Musical Works and Musical Works with Lyrics SAWP in Warsaw violated the prohibition of making competition-restricting agreements by: a) determining rules of collective management of rights to artistic performances of musical works and works composed of words and music in a way that restricted the performing artists' freedom to entrust SAWP with the collective management of their rights only with respect to selected areas of exploitation; b) stipulating in their operational agreements with artists performing musical works and works composed of words and music that the collective management agreement may be terminated by the performing artist effective as of the end of the following year;

- So far, the last case concerning the relationship between CSs and the entitled persons (not finalized with a final and binding decision yea) was a case in which the President of the Office of Competition and Consumer Protection stated in a decision issued in July 2009[133] that ZAiKS hindered the formation of conditions necessary for the development of competition on the market of collective management of copyright to musical works and works composed of words and music by adopting in relations with its clients a standard *Declaration on assigning economic rights tied to copyright to collective management*, according to which the assignment of rights expires only after five years, regardless of when the termination notice is handed.

132 Decision of the President of the Office of Competition and Consumer Protection of 10 June 2009, No. RWA-6/2009.
133 Decision of the President of the Office of Competition and Consumer Protection of 21 July 2009, No. RWA-10/2009.

3.3 CASES CONCERNING RELATIONSHIPS BETWEEN INDIVIDUAL CSS

The final category of cases concerning the activities of CSs which were examined by the President of the Office of Competition and Consumer Protection centre around the relationships between the organisations themselves. It is the least numerous category and includes only two cases:

- The case in which ZAiKS and the Union of Audio-Video Producers (ZPAV) were accused of violating the prohibition of making competition-restricting agreements by establishing that ZAiKS will grant the license for mechanical copyright provided that the ZPAV-ZAiKS hologram be placed on each copy of the recording. In the decision of 2002[134] the President of the Office of Competition and Consumer Protection did recognise the described agreement as violating the prohibition of making competition-restricting agreements;

- The case of an agreement concluded by ZAiKS and the Association of Polish Filmmakers, which concerned fixing uniform rates of royalties collected from the commercial users for sales of audiovisual works on carriers for personal use. The President of the Office of Competition and Consumer Protection stated[135] that as a result of the agreement, ZAiKS and the Association of Polish Filmmakers restricted competition in the domestic markets of audiovisual works on carriers for personal use and in the market for collective management of copyright to audiovisual works, and violated the prohibition of making competition-restricting agreements, stipulated both in national and Community law.

4. ANALYSIS OF THE PROVISIONS OF COPYRIGHT LAW

The impact of the regulations of the Copyright Act on the powers of the President of the Office of Competition and Consumer Protection with respect to CSs' activity, should be analysed separately for each category of cases. At the beginning, it should be noted that the Copyright Act does not to include provisions that would unambiguously indicate that the lawmakers strived to exclude the issues regulated by the Copyright Act from competition review, including the issues related to the collective management of copyright and related rights. However, with

134 Decision of the President of the Office of Competition and Consumer Protection of 25 September 2002, No. DDI-82/2002.

135 Decision of the President of the Office of Competition and Consumer Protection of 29 August 2008, No. DOK-6/2008.

respect to specific activities of CSs, the Copyright Act includes both provisions which restrict the powers of the competition authority and provisions which not only do not restrict them but set forth additional mechanisms to protect the participants of the market against abuses of a dominant position by CSs.

4.1 CASES CONCERNING THE RELATIONSHIP BETWEEN THE CSS AND THE USERS OF THE RIGHTS THEY MANAGE

In the cases concerning the relationship between the CSs and the users of the rights they manage, considerations on the provisions of Copyright Act that may restrict the jurisdiction of the President of the Office of Competition and Consumer Protection, should begin with a reference to the now revoked Article 108(3) of this act[136]. It envisaged a procedure for approving the rates of royalties to be applied by the CSs by the Copyright Committee ("CC") [137]. Giving such powers to the CC raised doubts as regards the possibilities of controlling and assessing these rates by the competition authority on the basis of the Competition Act. The controversy was solved by the Supreme Court[138], which stated that the procedure for approving tables of royalties by the CC may legally restrict the relevant powers of the President of the Office of Competition and Consumer Protection.

The Supreme Court stated as long as the Article in question was effective, *"copyright law comprehensively regulated setting (with administrative methods) the remuneration for using works or artistic performances covered by collective management, and foresaw a judicial and administrative method of assessing the legality of decisions made in these cases, which justifies a conclusion that copyright law in this regard allows for restrictions of competition referred to in Article 3 of the act."* This implies that the rates of fees approved by the CC could not be assessed on the basis of the Competition Act, whereas, in the case fees that were not approved by the CC *"the licence fees imposed by the CS may be subject to control within the framework of competition proceedings."* Although Article 108(3) of the Copyright Act was revoked and, at the moment, CSs apply rates of royalties not approved by the CC, the stance of the Supreme Court in the discussed case is still valid from the perspective of law application practice.

136 This provision lost its legal validity following the judgement of the Constitutional Tribunal of 24 January 2006 (SK 40/04).

137 Article 108(3) of the Copyright Act stipulates that "a Committee comprising of six arbitrators and a chairman as a super arbitrator that are appointed by the minister competent for culture and national heritage protection from a group of arbitrators, approves or refuses to approve tables of remuneration for the use of works or artistic performances covered with collective management which are presented by collecting societies."

138 Judgement of the Supreme Court of 2 April 2009 (III SK 19/08).

Firstly, taking into account the ongoing legislative works which aim at restoring the CC's powers in a form which would be compliant with the judgement of the Constitutional Tribunal. Secondly, the judgment of the Supreme Court is also valid because the Court specified the powers of the competition authority in the present situation, when the CSs apply rates of royalties not approved by the CC. According to the Supreme Court *"if the legislator still has not determined the mode and rules of setting remunerations by the CC, the President of the Office of Competition and Consumer Protection is responsible for cases concerning abuses of a dominant position by CSs that consist in imposition onerous terms and conditions in licence agreements and collection of excessive royalties until an act restoring the state compliant with the Constitution enters into force."*

Other provisions of the Copyright Act that might be recognised as limiting the powers of the President of the Office of Competition and Consumer Protection with respect to cases featuring CSs are provisions that determine the supervisory powers of the Minister of Culture and National Heritage ("Culture Minister"). In the light of Article 104(2)(3) of the Copyright Act, the Culture Minister supervises the activity of the CSs. The minister's powers cover depriving a CS of it licence if it fails to duly perform its obligations as regards managing and protecting the copyright and related rights entrusted to it[139], if it violates the provisions of law associated with the licence granted (Article 104(5)(1) and (2). Consequently, the supervisory powers of the Culture Minister with respect to CSs are very extensive, as they enable the Culture Minister to influence all the activities undertaken by CS in relation to rights management, on pain of taking away their licence to operate. This may in turn influence the scope of powers of the competition authority. Bearing in mind Article 3 of the Competition Act, it should be noted that the President of the Office of Competition and Consumer Protection cannot take any formal steps grounded in the Competition Act against an activity imposed on a CS by the Culture Minister. Taking actions against a CS on the basis of the Competition Act in cases concerning activities following from an order by another authority equipped with powers concerning the CS might violate the Constitutional principle of trust in the State[140]. When considering the exclusion of the powers of the President of the Office of Competition and Consumer Protection one should bear in mind that the Culture Minister

139 A decision of the Culture Minister on granting or revoking an authorisation for an CS to operate has to be published in the Official Journal of the Republic of Poland "Monitor Polski" (Article 104(6) of Copyright Act).

140 Cf. Judgement of the Court of Competition and Consumer Protection of 20 May 2002 (XVII Ama 92/01), Official Journal of the Office of Competition and Consumer Protection 2002/3-4/171.

has rather supervisory than regulatory competencies over CSs and the provisions set out in the Copyright Act do not require the Culture Minister to consider the objectives defined in the Competition Act. Hence, it is impossible to exclude the power of the President of the Office of Competition and Consumer Protection review activities that were not imposed on CSs by the Culture Minister[141].

Other provisions of the Copyright Act that restrict the powers of the President of the Office of Competition and Consumer Protection include Article 20 and Article 20^1. These provisions set forth an obligation to pay fees to CSs by producers and importers of: 1) tape recorders, video recorders and other similar devices, 2) copiers, scanners and other similar devices making it possible to acquire a copy of a part or of the whole printed work, 3) empty carriers for recording works or other content covered by related rights, for personal use and utilising the devices listed in point 1 and 2 (Article 20 of the Copyright Act), as well as owners of reprographic devices who carry out business related to the reproduction of works for personal use or for third parties (Article 20^1(1) of the Copyright Act). The legislator also set out the rules of setting the fees. The fees' rates are specified in a regulation of the Culture Minister[142]. In this regard, the Copyright Act is *lex specialis* with respect to the Competition Act[143]. As a result, the President of the Office of Competition and Consumer Protection may not interfere with rates set this way, by way of launching competition proceedings against CSs.

Statutorily acceptable restrictions of competition also include the obligation set forth in the Copyright Act which requires CSs' intermediation in the case of fees for cablecasting (Article 21^1(1)) and with regard to the payment of sums due to co-authors of an audiovisual works or to performing artists for using audiovisual works in the scope defined in Article 70(2^1) of Copyright Act[144] (Article 70(3)).

141 Cf. A. Bolecki, *Problematyka równoległego stosowania prawa autorskiego i prawa antymonopolowego wobec organizacji zbiorowego zarządzania prawami autorskimi – spojrzenie krytyczne*, Przegląd Ustawodawstwa Gospodarczego No. 9/2009, p. 18.

142 Cf. Regulation of the Minister of Culture of 2 June 2003 on defining the categories of devices and media intended for recording works and fees imposed on producers and importers for sales of these devices and media (Dz.U. No. 105, item 991); Regulation of the Minister of Culture of 27 June 2003 on payment of fees by owners of reprographic devices (Dz.U. No. 132, item 1232).

143 A. Bolecki, *op. cit.*, p. 19.

144 According to Article 70(2^1) of the Copyright Act "co-authors of audiovisual works and performing artists are entitled to: 1) remuneration proportionate to the income generated from screening the audiovisual work in cinemas; 2) appropriate remuneration for lease of copies of audiovisual works and their public presentation; 3) appropriate remuneration for broadcasting the work on television or by other public means of making the work publicly available; 4) appropriate remuneration for reproduction of an audiovisual work on a media intended for personal use."

Apart from the above-mentioned cases of limiting the powers of the competition authority, the Copyright Act also includes provisions which manifest the legislator's intention to counteract abuses of a dominant position by CSs. This is the case, for example, of Article 106(2) which stipulates that *"A CS may not, without good reasons, refuse its consent for the use of works or artistic performances within the scope of its management."* As the Supreme Court[145] rightly stated, the *ratio legis* for this provision *"is not only the protection of the interests of authors and other persons delegating their rights to be managed by collecting societies, but it also preventing abuses of a dominant position by such organizations by refusing, without sufficient justification, to conclude license agreements with broadcasters."*

The contractors of CSs are also protected against abuses of their dominance by virtue of Article 110 of the Copyright Act. It sets forth a general guideline as to the manner of establishing the sums of remunerations claimed by CSs[146]. Article 21(1) of the Copyright Act should also be noted here because it stipulates that CSs are prohibited to demand from radio and television organisations to conclude agreements concerning broadcasting of published minor musical works, textual works and works composed of words and music if these organisations concluded a separate agreement with the entitled entity[147].

4.2 CASES CONCERNING THE RELATIONSHIP BETWEEN THE CSS AND THE PERSONS WHOSE RIGHTS THEY MANAGE

The above-mentioned provisions setting forth the supervisory powers of the Culture Minister with respect to CSs (Article 104 of the Copyright Act) may be recognised as the only provisions of the Copyright Act that may restrict the powers of the President of the Office of Competition and Consumer Protection as regards investigating, on the basis of the Competition Act, the relationships between the CS and the persons whose rights they manage.

Apart from that, the Copyright Act includes provisions which complement the competition protection implemented on the basis of the Competition Act. Article

145 Judgement of the Supreme Court of 2 April 2009 (III SK 19/08).

146 The cited provision stipulates that "the amount of remuneration claimed within the scope of collective management by collecting societies should take into account the amount of income generated by the use of works and artistic performances of the works, as well as the nature and scope of the use of these works and their artistic performances."

147 Article 21(1) of the Copyright Act stipulates that "radio and television organisations are allowed to broadcast published minor musical works, lyrical works and works composed of words and music basing exclusively on an agreement concluded with CSs, unless the radio and television organisation is entitled to broadcast ordered works on the basis of a separate agreement."

106(1) is of such nature. It states that a CS is obliged to equally treat the rights of its members and other entities that it represents with regard to the management of the above-mentioned rights or their protection. In this context, Article 106(3) should also be highlighted, as it stipulates that a CS may not, without good reasons, refuse to manage copyright or related rights.

From the perspective the role of competition law in cases concerning collective management of rights, Article 107 of the Copyright Act is of great significance. This is because it confirms the principle of a pluralist nature of the CSs[148]. This interpretation the Article was emphasised by the Court of Competition and Consumer Protection[149], which stated that the Copyright Act does not provide for a legal monopoly of a single CS only. On the contrary, it assumes that a number of such entities exist, as Article 107, *inter alia,* explicitly states that individual collecting societies may operate within the areas of exploitation of their own choice. The Court of Competition and Consumer Protection highlighted that *"base on the principle of »rational legislator« it should (...) be recognised that the provision included in the Act on copyright and related rights provides for the existence of many collecting societies, which may operate within the areas of exploitation of their own choice. It is up to the author to chose the CS he or she wants to cooperate with."*

4.3 CASES CONCERNING THE RELATIONSHIPS BETWEEN CSS THEMSELVES

Out of all the categories of cases so far examined by the competition authority, the Copyright Act has the least significant impact on the powers of the President of the Office of Competition and Consumer Protection with respect to cases concerning relationships between CSs themselves. As a general rule, the provisions of Copyright Act do not directly refer to these relationships. This implies that the Copyright Act does not restrict the application of the prohibition of competition-restricting practices in the case of agreements between CSs or the prohibition to abuse dominance by one CS against another.

148 Article 107 of the Copyright Act establishes that "if within a given field of use more than one CS is active, the competent organisation within the meaning of the act, is an organisation to which belongs the author or the performing artist, and if the author or the performing artist does not belong to any organisation or if the author or the performing artist failed to reveal its authorship – an organisation designated by the Copyright Committee."

149 Judgement of the Court of Competition and Consumer Protection of 9 January 2006 (XVII AmA 84/04).

5. CONCLUSION

Due to the presumption of the competition authority's jurisdiction in cases concerning counteracting competition-restricting practices which follows from the Competition Act, the powers of the President of the Office of Competition and Consumer Protection also cover the possibility to investigate activities of entities operating on the market of collective management of copyright and related rights. However, the President of the Office of Competition and Consumer Protection should take into account the provisions of the Copyright Act, since these may modify the scope of application of the rules of competition protection ensuing from the Competition Act, accepting the specific nature of the market.

Basis on an analysis of the Copyright Act, it should be concluded that there exists no basis to generally exclude the powers of the President of the Office of Competition and Consumer Protection with respect to investigating activities undertaken by the CSs from the point of view of the prohibition of competition-restricting practices set out in the Competition Act. However, the role of the President of the Office of Competition and Consumer Protection stops where the Copyright Act provides for a comprehensive regulation of the activities of the CSs by other public authorities and a method to assess the legality their decisions[150], as no objections should be raised against CSs for operating in the manner that was imposed on them by an authority that represents the State.

150 Cf. Judgment of the Supreme Court of 2 April 2009 (III SK 19/08), unpublished.

Elżbieta Modzelewska-Wąchal

CONSUMER PROTECTION IN THE POLISH COMPETITION ACT. HORIZONTAL ISSUES

1. GENERAL OBJECTIVES OF THE POLISH COMPETITION ACT

The Act of 16 February 2007 on competition and consumer protection[151] ("Competition Act") is the fourth consecutive act of law in Poland protecting competition as an institutional phenomenon and the third act to enter into force after the introduction of market economy. Contrary to the first competition acts, the current one is not a homogenous act, because it contains instruments typical for competition law, set out in the Treaty on the Functioning of the European Union (Articles 101 and 102 TFEU), as well as instruments serving directly and exclusively consumer interests.

The basic premise of the Competition Act expressed in its Article 1(1) should determine the conditions for the development and protection of competition. It does not, however, contain any regulations determining the conditions for the development of competition, but is an act that basically performs only one of the functions of competition policy, that is of protecting enterprises and consumers. This function is fulfilled by counteracting competition-restricting practices and practices infringing collective consumer interests, as well as anti-competitive mergers of undertakings and their associations, where such practices or mergers cause or may cause effects in Poland.

The Act contains a set of rules (orders or prohibitions) addressed at enterprises, which may be described as "the code of market behaviours". Complying with the code is one of the more important factors which guarantee the existence of effective and undistorted competition on the market.

The last twenty years when competition law has been effective in Poland (the first act being adopted already in 1987) strengthened the opinion that the situation when enterprises compete with each other is positive in every respect, because it leads to more efficient operation of businesses and to optimising the use of resources, creating the conditions for undisturbed trade, improved quality,

151 Dz.U. No 50, item 331, as amended.

faster technical development and a wider choice of products available to customers, including consumers, at lower prices. Competition imposes the necessity to care for consumers and their interests by offering them increasingly better products, additional services and new technologies[152], and also by ensuring that consumers can take advantage of the benefits brought about by strengthening competition.

Academics are disputing the objectives of competition policy. The traditional theory represented by the Harvard School and the efficiency theory promoted by the Chicago School are the two theories most widely debated. The Harvard School consistently argues that it is necessary to respect the laws protecting competition in order to guarantee the redistribution of income, small businesses' protection, control over the process of economic power concentration, consumer sovereignty and technical development. The Chicago School, in turn, considers the objective of competition policy to be consumer welfare, which is a result of economic behaviours of enterprises leading to allocative and productive efficiencies. According to the proponents of this school, having a large market share may be the source of economic efficiency, hence prosecuting dominant enterprises is acceptable only when their dominance does not contribute to efficiency.[153]

The Polish Competition Act in its legislative content implements the principles and assumptions of the traditional Harvard School, protecting competition as an instrument which supports entrepreneurship, protects consumer interests and counteracts abuses of market power.

2. CONSUMER WELFARE AS AN OBJECTIVE OF THE COMPETITION ACT

The Competition Act, as an instrument of implementing competition policy, should not serve to curb the behaviours of enterprises which fulfil the objectives of competition policy, that is behaviours causing, in particular, increased production or sales, lowering of prices, technical development or extending the market offer. Competition is restricted when the behaviour of enterprises leads or may lead to negative effects, such as decreased sales or production,

152 The judgement of the Supreme Court of the Republic of Poland of 19 October 2006 (III SK/15/06).

153 B. Majewska-Jurczyk, *Dominacja w polityce konkurencji Unii Europejskiej*, Wrocław 1998, p. 10-11.

limited choice for consumers, increase in prices or slower decrease in prices if compared to the decrease that could be expected in the conditions of undistorted competition. Such restrictions of competition should be subject to administrative intervention under the Competition Act. Behaviour of enterprises which does not serve consumer welfare and hence is contrary to the overall objectives of the Act, should then be eliminated.[154]

Along with protecting competition and the interests of businesses, consumer welfare is cited as one of the main direct objectives of the Competition Act, but it is also an indirect objective, to be achieved by efficient competition. In the case law of Community institutions, consumer welfare is also accepted as the overriding objective of competition law.[155]

3. LEGISLATIVE MEASURES OF CONSUMER PROTECTION

The Competition Act protects the interests of consumers in a two-fold manner: by counteracting restrictive practices and practices infringing collective consumer interests.

In terms of their effect, competition-restricting practices may be divided into:

- anti-competitive practices, exerting direct influence on the state or development of competition and on competition-related interests of other enterprises,

- exploitative abuses, the objective or effect of which is to infringe other than competition-related interests of the other market participants, including non-enterprises.

The division is not precise, however, because direct anti-competitive business behaviours tend to indirectly affect the interests of contractors and consumers, as restricting competition makes it difficult or even impossible for consumers to choose between market offers and contributes to enterprises' abusing their contractual advantage. In the case of anti-competitive practices, however,

154 Judgement of the Supreme Court of 19 October 2006 (III SK 15/06).

155 Judgement of the Court of First Instance no T-168/01 of 27 September 2006, in the case GlaxoSmithKline Services Unlimited v. the Commission. The case concerned the practice of using higher prices in the export of medicines to another Member State as a part of parallel trade, compared to prices used in domestic sales. This practice was considered as serving to maintain high prices of medicines.

this relationship is not direct, because, before we start talking about an infringement of consumer interests resulting from a new market situation, an anti-competitive effect has to occur first. This is different in the case of exploitative abuses, where the direct objective or effect of the behaviour of enterprises is the abuse of the advantage that they already have over contractors and consumers.

Therefore, only exploitative abuses directly harm consumer interests. Anti-competitive practices may harm them only as a result of lowered level of competition between enterprises.

Competition instruments do not, however, guarantee comprehensive protection of consumer interests. An important limitation is the premise that competition instruments may apply only to enterprises acting jointly (participating in agreements) or having a dominant market position. This way, the instrument protects consumers only partially, because it does not cover the cases of consumer interest infringements by non-dominant enterprises acting individually.

In such situations, counteracting practices infringing collective consumer interests complements counteracting anti-consumer competition-restricting practices in the consumer protection system. The introduction into the Polish Competition Act of the prohibition of practices infringing collective consumer interests was in line with the general trend to extend the legal guarantees of consumer protection, resulting from the fact that functioning of competition in the market does not sufficiently ensure the protection of weaker market players in their relations with professionals. Also, in certain sectors, namely those where network monopolies operate, market mechanisms do not function anymore.

The scope of consumer protection set forth by the provisions of the Competition Act and regulating the principles of counteracting practices which infringe collective consumer interests, is also not comprehensive. The prohibition covers only practices which violate collective consumer interest (not any interests), infringe the public interest and are illegal at the same time.

Contrary to competition-restricting practices, which are illegal *per se* as a result of being prohibited under Articles 6 or 9 of the Competition Act or Articles 101 and 102 of the Treaty on the Functioning of the European Union, the illegality of practices infringing collective consumer interests of is indirect: for a behaviour to be qualified as an illegal practice, it must constitute a breach of an order or prohibition following from legal provisions other than Article 24 of the Competition Act and which specifically makes this kind of behaviour unlawful. A legal basis equivalent to Article 24 must, therefore, exist to qualify actions or omissions of an enterprise as practices infringing collective consumer interests. The following may serve as the legal basis:

- Article 385^1 §1 of the Civil Code if the practice consists in applying abusive contract terms listed in the Register of Prohibited Clauses,
- Act of 13 April 1993 on combating unfair competition[156] defining actions which infringe consumer interests, e.g. unfair advertising (Article 16),
- Act of 23 August 2007 on counteracting unfair market practices[157],
- any other provisions imposing on enterprises specific obligations in their relations with consumers.

Article 9 of the Competition Act prohibiting market dominators to abuse their dominant position, including in their relations with consumers, may also serve as the legal basis here.

According to Article 25 of the Competition Act, taking action to protect collective consumer interests by the President of the Office of Competition and Consumer Protection does not exclude the possibility for other authorised bodies or individual consumers to take action aimed at protecting their interests on the basis of other legal acts.

The difference between the powers of the President of the Office ensuing from Article 24 and further articles of the Competition Act and the rights of consumers and other entities enforced based on the other consumer protection acts, does not lie in the difference in the behaviour of enterprises but the scope of their conduct. Consumer interests may be protected on the basis of Competition Act where the practices of enterprises affect collective interests, whereas other acts make it possible to counteract the same practices even

156 Dz.U. of 2003, No 153, item 1503 as amended.
157 Dz.U. No 171, item 1206.

if the conduct infringed the interests of a single individual consumer only. Collective consumer interests are considered to be threatened when the behaviour of an enterprise is addressed at unspecified consumers, singled out from other consumers according to some criterion.[158] A behaviour of an enterprise which infringes interests of one or several consumers, even if unlawful, is not a behaviour infringing collective consumer rights, as defined in Article 24 of the Competition Act[159], because what distinguishes the protection measures provided for in the Competition Act from the measures ensuing from other acts, is the premise of infringing collective rather than individual consumer interests.

4. CONCURRENCE OF CONSUMER PROTECTION LEGISLATION

The system of consumer protection covers both the instruments provided for in the Competition Act and those established under other legal provisions. However, these measures are not independent, in some cases it is possible that they may converge. The convergence may occur:

- between the provisions of the Competition Act prohibiting competition-restricting practices and its provisions prohibiting practices infringing collective consumer interests,

- between the provisions of the Competition Act prohibiting competition-restricting practices and the provisions of other acts,

- between the provisions of the Competition Act prohibiting practices infringing collective consumer interests and the provisions of other acts.

The convergence of the legal provisions listed in point 1 may occur in particular when an enterprise dominating the relevant market undertakes actions towards consumers which may be considered a manifestation of the abuse of its dominant position (and hence are a practice prohibited under Article 9 of the Competition Act), while at the same time breaching the provisions regulating the obligations of enterprises towards weaker market participants. In such cases, the President of the Office of Competition and Consumer Protection

158 Judgment of the Supreme Court of 5 June 2007 (III SK 7/07).

159 Judgement of the Court of Competition and Consumer Protection of 10 May 2004. Ama 45/2003 LexPolonica no 392167.

may choose the basis for qualifying the practice as illegal: he or she may either use sanctions associated with "anti-competitive" practices or for "consumer-related" practices. Under the existing law, the sanctions used against both of these categories of practices are equally acute, which results in a situation where using either of these instruments to counteract a practice is equally effective (if the effectiveness of law is measured by the type and acuteness of the sanctions imposed). Therefore, from the point of view of the enterprise and consumers concerned the choice either of the legal bases with respect to the consumer-related practices penalised under the Competition Act is of no importance as they perform the same function.

The acuteness of the sanction may be even greater if, benefiting from the convergence of laws, the authority applies both of these legal bases at the same time. The Office is authorised to do it under the Competition Act, especially that in both cases the protection of consumer interests is performed in the public interest. Then, the law allows for doubling the sanctions, e.g. imposing a higher fine. The decision on what sanctions to apply in such cases should be taken with consideration for the basic function that sanctions should perform, namely the preventive and repressive function.

There exist no legal obstacles to the President of the Office of Competition and Consumer Protection acting on the basis of Article 24 of the Competition Act in the case of convergence of the provisions of this Act and other acts protecting consumers. Moreover, proceeding in this way is even desirable, because applying administrative sanctions guarantees greater effectiveness of consumer protection than applying civil law redress mechanisms available to aggrieved persons under private law.

The provisions of the Competition Act forbidding practices infringing collective consumer interests converge with other acts protecting competition only where an enterprise's practice corresponds to the scope of separate legal provisions, infringing individual interests of consumers, while at the same time being addressed *ad incertam personam*, harms (at least potentially) an indefinite number of people, consequently leading to a situation where anyone may be aggrieved by the practice.

In the remaining cases it is acceptable to use only the sanctions provided for in provisions separate from the provisions of the Competition Act. These are, however, civil law remedies and they require that consumers, entities representing their interests, enterprises take action by themselves. Civil law remedies are in principle not as acute as administrative sanctions, which is justified by the lesser significance of civil law infringements.

5. CONCLUSION

The current system of consumer protection is coherent and comprehensive. The legal instruments foreseen in the system are adjusted to the nature of the detrimental practices employed enterprises. The Competition Act plays a special role in this system. The instruments that the Act provides are tailored to combating the most harmful anti-consumer practices: the practices of enterprises operating on markets where competition is restricted (the prohibition of competition-restricting practices harming consumer interests) or practices infringing collective consumer interests, and hence having a larger impact than those directed at individual consumers. Overall, the Competition Act adopted a highly repressive system of sanctions, whose aim is both to prevent and to repress. The effectiveness of the Competition Act as an instrument combating anti-consumer practices will depend on the sanctioning policy implemented by the President of the Office of Competition and Consumer Protection, which should both be balanced and ensuring, at the same time, effective application of law.

Mercedes Pedraz Calvo

COMPETITION AUTHORITIES' POWER OF INVESTIGATION AND RESPECT OF FUNDAMENTAL RIGHT: INVIOLABILITY OF DOMICILE

1. INTRODUCTION

Within the scope of the fundamental right to inviolability of domicile, judges and tribunals have worked intensively on this concept, how and when a warrant must be requested and provided, who may or may not enter the natural or legal person's residence and be present while the search is being conducted.

The use of computers has created a new range of problems in this field: how to deal with the enormous amount of information stored there. Can competition authorities take each piece saved on the domicile holder's computer? If so, can they lawfully read and gain knowledge of everything? And again, if this is the case, can they use that information to prosecute the domicile's holder or other undertakings for infringements previously unknown?

The purpose of this comment is to share with other judges, lawyers and scholars specializing in competition law some cases resolved by the Spanish Audiencia Nacional, where the inspection of private persons' and enterprises' domiciles by the antitrust authorities officials was the main issue.

The inviolability of domicile is a basic constitutional right enshrined in Article 18.2 of the Spanish Constitution. It implies that the entry into a domicile is "legal" only in three situations:
– with consent of a holder,
– with judicial authorization,
– in case of a flagrant offence, without either of the above.

This is a right that, with nuances in its formulation, is enshrined in all the declarations of human rights, Universal Declaration of Human Rights (Article 12), the Convention on Civil and Political Rights (Article 17.1), and the Rome Convention on Fundamental Rights and Freedoms (Article 8.1).

The Spanish Constitutional Court stated in decision no. 129/1990 that according to Article 18.2 of the Constitution no entry into a domicile may be made without the holder's consent or judicial authorization, except in cases of flagrant offences. Inviolability of domicile is a basic right of every person, established to ensure the privacy of this limited area that the individual chooses, characterized by being exempt or immune to invasions or external aggressions of others or of the "public authority."

To implement the fundamental right, the law has established a double conditioning to the entry and search of the premises: either the administrative authority obtains explicit consent of the owner, or a warrant to do so, issued by a judge. The Constitutional Court stated that what Article 18.2 of the Constitution essentially bans is household search, because it is the essential attack on the constitutionally protected right, for which entry is not more than formality or instrumental means.

The Constitutional Court also points out that comparing the two titles enabling an administrative authority to enter residence, i.e. consent or court permission, the former is "weaker" than the latter, since a public agency can penetrate domicile with or without the holder's approval when a judge has issued an authorization to do so.

Continuing with the reasoning, the Constitutional Court recalls that there are no unlimited rights in our legal regime and that restrictions are either founded on the Constitution itself, in respect of other human rights, or based on constitutionally protected principles.[160]

Two consequences of this constitutional jurisprudence are established: the first rule is inviolability of the domicile, the fundamental right of the person; the second imperative is that to enter residence, the authorities must have either the holder's consent, or a judicial authorization.

2. THE JUDGE'S POSITION

In judgment 144/87 the Spanish Constitutional Court examines the position of the judge issuing a warrant for the administrative authority to enter a residence. It concluded that the judge is a guarantor of the fundamental right to inviolability

160 See: Spanish Constitutional Court decisions: 11/1981, 2/1982 and 110/1984.

of domicile, and so, must firstly implement the administrative decision, ensuring that the entry is requisite. And moreover, that this decision has been taken by the competent agency in the use of its legal powers. Secondly, the judge must ensure that invasion of privacy does not result in other limitations of fundamental rights of occupants, and is strictly necessary to execute the administrative decision.

The Spanish Constitutional Court categorically indicates that a judicial warrant cannot be understood as automatic. In other words, the judge is not deprived of his/her capacity to examine adequacy of the administrative action in regard to the purpose to be achieved.[161] The judge can examine, review and refuse to allow a warrant.

If the judge decides to give a warrant to enter a domicile, this decision must be explained: motivation constitutes an essential part of the judgment and becomes the means to verify if the judicial action has operated as a guarantee to the exceptionality of interference in the basic right and of "proportionality of restriction of any fundamental right".[162]

The warrant issued by a judge must be motivated, and the Spanish Constitutional Court considers that the reasoning must include:[163]

a. existence of a necessity to enter and search domicile related to protection of a legitimate constitutional principle (i.e. search for documents conducted by tax officials must be justifiable by the obligation of citizens to pay taxes),

b. suitability of the measure to achieve the intended purpose,

c. and, in particular, the concrete conditions related to this warrant: particularities proving that what the authorities are looking for may not be obtained by other means, less onerous to fundamental rights.

The warrant must also include concrete circumstances referring to that case, i.e.:

a. circumstances related to location, i.e. address of domicile to be entered and searched,

161 Decision 137/1985.
162 Decision 171/1999.
163 Decision 147/2001.

b. conditions concerning time, i.e. date and duration of the search, and,

c. if possible, identification of the holder of premises to be entered and searched, as well as relationship of this proprietor with the law infringement investigated.

To complete this list of requirements, the European Convention on Human Rights has established that a warrant must include reference to the number of officials authorized to enter and search the domicile.

Another important issue examined by the Spanish Constitutional Court and one especially relevant to competition authorities prosecuting cartels, is whether asking the owner's permission is necessary before addressing the judge and obtaining the warrant.[164] According to the Court, the latter constitutes an alternative to the owner's consent. Thus, the judicial authorization is legally identical to the approval of the domicile's holder.

3. DOMICILE: THE CONSTITUTIONAL CONCEPT

The Spanish Constitution does not include any description or concept of domicile, while there are definitions in other rules akin to the Civil Code, Criminal Code or Taxes Regulations. According to the National Constitutional Court[165] home is the place where the natural person resides without being necessarily subject to social uses and conventions, enjoying utmost freedom.

The abovementioned definition does not refer directly to legal persons, but the Constitutional Court stated that companies also have the right to inviolability of domicile. The difference lies in the scope of the rights[166] that extends only to the physical place indispensable to carry out business operations without interference from outside, where the undertaking develops its entrepreneurial activities without hindrance, from where the entity is directed, where documents are kept, or other location where the company's activity is held and kept apart from the knowledge of third parties.

164 Decision 129/1990.

165 Decisions 22/1984 and 50/1995.

166 Decision 69/1999.

4. THE COMMISSION'S POWERS OF INSPECTION IN REGULATION 1/2003

Regulation 1/2003 in its explanatory statement states as follows:

"The Commission should also be empowered to undertake such inspections as are necessary to detect any agreement, decision or concerted practice prohibited by article 81 of the Treaty, or any abuse of a dominant position prohibited by article 82 of the Treaty. The competition authorities of the Member States should cooperate actively in the exercise of these powers."

Two articles of the Regulation establish the rules on the Commission inspection powers – Articles 20 and 21. Article 20 stipulates that the Commission officials may conduct inspections and therefore have the right:

"(a) to enter any premises, land and means of transport of undertakings and associations of undertakings;

(b) to examine the books and other records related to the business, irrespective of the medium on which they are stored;

(c) to take or obtain in any form copies of or extracts from such books or records;

(d) to seal any business premises and books or records for the period and to the extent necessary for the inspection;

(e) to ask any representative or member of staff of the undertaking or association of undertakings for explanations on facts or documents relating to the subject-matter and purpose of the inspection and to record the answers."

This article also rules that to conduct the inspections, the Commission officials must have and present *"a written authorization specifying the subject matter and purpose of the inspection."*

In paragraph 4, Article 20 determines that *"The decision shall specify the subject matter and purpose of the inspection, appoint the date on which it is to begin (…)"*. The assistance of the police or of an equivalent enforcement authority to enable the Commission officials to conduct their inspection is also incorporated into the provisions of paragraph 6 of Article 20, as well as an authorization by the judge or court issued "according to national rules."

Article 21 of Regulation 1/2003 concerns the inspection of other premises, including the homes of directors, managers, and other members of the undertakings and associations of the staff thereof. Again, Article 21 stipulates that "The decision shall specify the subject matter and purpose of the inspection, appoint the date on which it is to begin and indicate the right to have the decision reviewed by the Court of Justice. It shall in particular state the reasons that have led the Commission to conclude that a suspicion in the sense of paragraph 1 exists."

5. WHAT ARE THE OBLIGATIONS OF THE COMPANIES WHOSE DOMICILES ARE SEARCHED?

Companies whose premises are searched have to accept the inspection whenever it is ordered by a decision. As mentioned above, the decision must indicate its subject and purpose, the date when it will take place, fines for infringement, and the right to appeal.

According to Regulation 1/2003, a judicial warrant should be requested whenever the authority considers it necessary and when the search of premises must be carried out with assistance of the police (or the equivalent security forces) and the law of the Member State does not allow such support without a warrant.

Both a decision and warrant must indicate certain precise facts, namely: the subject, object and purpose of the inspection, date to be performed, grounds for suspecting the infringement, and the right of appeal against each of the above.

A judge asked to authorize the inspection must verify authenticity of a decision and consider whether measures intended are not arbitrary or disproportionate in relation to the object of an inspection. To grant or refuse a warrant, a judge must take the following aspects into consideration: the basis of the request, seriousness of the alleged infringement and the company's participation in the breach, and reasonable probability that books and records relating to the subject matter of the inspection are kept in the premises affected.

A judge cannot question the necessity for administrative authorities to conduct an inspection of the company premises or demand access to the Commission's records. In case of having doubts, he or she may ask for explanations from the Commission, or the antitrust authority about the element(s) aforementioned deemed necessary to assess the proportionality of the intended search.

The legality of the Commission's decision is subject to review by the European Court of Justice exclusively. The Roquette Frères decision (22-10-2002) established and explained the extension of a national judge's supervision (one responsible for authorizing an entry and search of domicile in an investigation ordered by the Commission according to Regulation 17/62). The Court also examined thoroughly, what must be done when the judge is not satisfied with the information provided by the Commission.

The Court resolved that if a request for assistance is made, a national judge responsible for issuing a warrant must verify whether a measure intended is not arbitrary, that there are reasonable grounds for suspicion of a breach of the antitrust rules, and that such an action is necessary. The Commission (or the national authority) must provide all the information necessary to ensure that the judge may supervise the request. Therefore, the request for a warrant must include the following:

a. essential characteristics and nature of the suspected offence and an indication of the relevant market,

b. alleged involvement of the legal person's domicile in the suspected offence must be explained,

c. factual grounds for suspicion that the offence has been committed,

d. indication, as accurate as possible, of evidence sought and the powers conferred to officials in search of such proof,

e. in cases where the action is taken on a preventative basis, so as to avoid the opposition of the undertaking concerned, details allowing the judge to confirm that establishing the facts of offence would be difficult or impossible should an entry not be warranted.

A national judge cannot demand access to the contents of the Commission's dossier, even when the suspicions are based on them. If a national judge considers that the information given by the Commission is not sufficient, he or she may not reject the request; instead, he or she must ask the Commission, or the national authority making the request, to provide him/her with sufficient clarifications to exercise supervision.

6. SPANISH ANTITRUST LAW PROVISIONS

The Spanish Competition Law, 15/2007 in Section Two of Title IV (Procedures) Chapter I (Common provisions) the first provision (Article 39) establishes "Duties of collaboration and information):

"*1. All natural or legal persons and the organs and bodies of any Public Administrations are subject to the duty of collaboration with the National Competition Commission and are obliged to provide, at the request of the latter and within the deadline, all kinds of data and information that they may have and that may be necessary for the application of this Act. This deadline shall be 10 days, unless given the nature of the request or the circumstances of the case a different justified deadline is set.*

2. *Collaboration, ex officio or at the request of the National Competition Commission, shall not imply the status of interested party in the corresponding proceedings*."

It also contains a provision related to this issue: Article 40 "Powers of inspection"[167]. According to Article 40 paragraph 2, the Antitrust Commission officials have "*the following powers of inspection*"*:*

"*a) to enter any premises, land and means of transport of the undertakings and associations of undertakings and the private homes of the entrepreneurs, managers and other members of staff of the undertakings,*

b) to verify the books and other records relating to the business activity, irrespective of the medium on which they are stored,

c) to take or obtain in any form copies of or extracts from such books or records,

d) to retain the books or documents mentioned in letter b) for a maximum period of 10 days,

e) to seal all business premises, books or records and other business assets for the period and to the extent necessary for the inspection,

167 All paragraphs in italics of the English version of the Spanish Antitrust Law are taken from the Antitrust Authority's official web site.

f) to ask any representative or member of staff of the undertaking or association of undertakings for explanations on facts or documents related to the subject-matter and purpose of the inspection and record the answers."

This rule also states that whenever the Antitrust Commission officials intend to enter a domicile (paragraph 2.a) and to seal the premises (paragraph 2.e), they must either obtain the affected party's permission or a warrant issued by the judge (as we have seen, this is a constitutional obligation).

Regarding the undertakings' obligations, Article 40, paragraphs 3 and 4, stipulates as follows:

"3. The undertakings and associations of undertakings are obliged to submit to the inspections that the Director of Investigation has authorized.

4. If the undertaking or association of undertakings opposes an inspection ordered by the Director of Investigation or exists a risk of such opposition, they must request the corresponding judicial authorization when this involves restriction of fundamental rights from the Administrative Court, which shall rule within a maximum period of 48 hours."

In the previous Antitrust Regulation (16/1989), Article 32 stated that undertakings are obliged to help the antitrust authorities by providing whatever information and data they request (necessary for competition law enforcement). In addition, while exercising functions of an investigation and inspection, the antitrust agency might need to perform a domicile search and warrant authorizing them to do so must be given by a judge.

The Spanish Supreme Court has stated that if, while the administrative or police authorities are investigating a domicile, other documents or objects showing the possible existence of other crimes or administrative infractions appear, only the judge has the authority to decide: first, if those objects or documents are related to the matter investigated, and second, if the warrant should therefore be extended to allow the officials in charge to take and carry away those findings. As we shall see later on, it is a matter of debate among Spanish jurists whether a search would or would not be void when documents (objects, emails, letters) falling outside the precise object of the warrant issued by the judge are taken and used to prosecute the owner, that is whether they have or have not been taken in violation of a fundamental right.

In any case, to ensure maximum respect of the domicile holder rights, both administrative and judicial decisions (the first ordering an entry and search, the second authorizing it) must clearly indicate the crime or law infringement they are investigating, as well as actions to be carried out once they are inside the domicile.

Both an administrative decision and judicial warrant must indicate the following:

a. name of domicile holder, the natural or legal person who must bear the consequences of entry and search,

b. address of the domicile,

c. crime or administrative violation being prosecuted.

Both an administrative decision and judicial warrant must be notified to the holder, a person living there, or an individual who legally or factually represents him/her. The usual means of notification is giving the holder or his/her representative a copy of the order. Only a holder and officials authorized by the law in an administrative decision and/or the judicial warrant may participate in the action.

Some rules have been clarified in criminal law cases, namely:

a. objects, documents, books or computers must be made available,

b. useless inspections should be avoided,

c. objects, documents, books, etc. may be taken or copied,

d. search must end when the authorization expires.

The consequences of an illicit entry into a domicile have also been settled in criminal law cases, namely evidence obtained in violation of fundamental rights is void.

7. SOME CASES AND DECISIONS

The Audiencia Nacional is the country's tribunal competent to revise decisions issued by the Spanish Competition Authority. To date, only three of the S.C.A. rulings have been appealed by the parties.

The Audiencia Nacional ruled on 29th September 1997 in the case where an association of undertakings representing 80 percent of the market in Spain issued a press statement calling for a revision of fees charged. They also published bulletins quoting prices ostensibly lower than these published in trade press.

The referenced association claimed that proof obtained through an inspection of their premises by the competition authorities was illegal because the officials were investigating only the press release and an interview on that topic, whereas during the inspection they also collected other data, including the aforementioned bulletins.

The Audiencia ruled that the inspection carried out by the antitrust officials was not unlawful. Although a decision to enter a domicile must establish the basic facts being investigated, if in the course of search other elements unknown to the authorities and "intimately linked with those investigated" are found, they may be examined. The decision pointed out that in this particular case, the antitrust officials were investigating a collective indication regarding costs of services and the new data obtained during the inspection proved different means applied by the association to achieve the same goal - an agreement on prices and other commercial conditions.

For this reason, the search was considered legal because being aware of the investigation, the domicile holder was present during the inspection and was able to present his/her arguments both during the search and afterwards in the course of the administrative procedure.

This ruling was contested in the Supreme Court, which rejected the appeal by issuance of a decision on 17th March 2003. On the question of domicile inspections, the Spanish Supreme Court stated that once the officials are inside a residence or premises, the law limits their search to the object previously determined, but when the holder exhibits other documents without being obliged to do so, or when examining those papers previously determined another infringement is discovered, there is no legal obstacle to prosecute this breach and to consider the evidence a valid means of proof.

On 18th May 1999 the Audiencia Nacional ruled in a case where an undertaking disputed the order issued by the antitrust authority for the inspection of its premises. The Court rejected the claim stating that the inspection was performed with the consent of the person concerned, properly assisted by a legal advisor and that a copy of the decision was delivered to the association holder of the domicile.

After a close examination of the order, the Court considered the document duly included:

a. identification of civil servants authorized to perform the search,

b. search objects: documents, data, communication means, activities related to distribution of goods, commercial strategy, including projects, programs, and other actions leading to acquisition of commercial authorized warehouses,

c. investigation object: documents, data, communication means, contracts related to distribution of explosives, and explosives.

The Court considered the investigation order to be duly motivated.

In the very recent decision of 30th September 2009, in a special procedure for the protection of fundamental rights, the Audiencia Nacional stated that the constitutional right to inviolability of domicile had been infringed by the antitrust authority. In this case, documents not included in the warrant were collected and later examined by antitrust officials.

Both the decision and warrant (the search was performed in two different cities) indicated that the inspection's object was to look for proof of suspected antitrust infringement in the area of professional hairdressing. While performing the search and coping computer data, some documents unrelated to the professional hairdressing commercial activities of the domicile holder were found.

The Audiencia Nacional stated as follows: domicile search constitutes a limitation of the fundamental right and inspecting a residence or premises is subject to restrictions.

The main limitation is the infringement being investigated: facts being investigated are reference to decide whether a search has been carried out legally or not. In that case the Court decided that the antitrust authority had acted against the undertaking's constitutional right because the officials copied and took away documents and data unrelated to the specific object of the decision and the warrant. Consequently, those documents and data should be returned to the undertaking.

8. CONCLUSION

It is difficult to interpret the scope of the constitutional right to inviolability of domicile in the circumstances, when documents are stored on computers. Antitrust authorities must investigate to fulfill their task and to point the committed infringements. Evidence is very often hidden in the depths of complicated computerized data, therefore, antitrust authorities must enter the undertakings' premises and explore their computers. Those computers contain large amounts of confidential information, keep lots of data and secrets, not only commercial, scientific or financial, but also personal, or protected by legal privilege.

A balance between a domicile holder's right to guard his/her privacy and competition authority's obligations to obtain and scrutinize personal data which conceals an antitrust infringement must be reached. Judges must decide case by case how to ensure the protection of the constitutional right while assuring that competition authorities carry out their responsibility to shield the interests of consumers and undertakings.

Marta Sendrowicz

PARALLEL TRADE AND THE LIMITS TO ADMISSIBLE ACTIVITY OF DOMINANT PHARMACEUTICALS COMPANIES IN THE CASE LAW OF THE COURT OF JUSTICE OF THE EUROPEAN UNION

I would like to dedicate this article to the memory of Professor Eugeniusz Piontek. When writing the paper, I missed the Professor's wisdom and insightful approach to this topic, which was one of his keenest interests.

1. INTRODUCTION

The dynamics of relations between enterprises is becoming, in the contemporary legal context, a real challenge for competition protection authorities and judicial bodies. This may be observed in many sectors of the economy, where interesting and difficult issues concerning the application of the European competition law constantly delineate new areas for investigation. They are subsequently examined by competition protection authorities, which apply methodologies developed within earlier cases analysed on the basis of Article 81 or 82 of the Treaty establishing the European Community (EC Treaty) (now Article 101 of the EC Treaty and Article 102 of the Treaty on the Functioning of the European Union – TFEU) by the European Commission and European courts. The question is: Is it possible to formulate and successfully justify a statement that the rules of the European competition law provide universal solutions to all matters which need to be examined on their basis and all that we need to do is simply apply them to the particular factual context investigated? This paper analyses the problem in light of a particular type of relations occurring between undertakings operating at various levels of the broadly understood market for the supply of medicinal products[168]. The essence of these relations lies in the continuous confrontation between the fundamental principle of free movement of goods in the Common Market, triggering the phenomenon referred to as parallel trade[169],

168 J.W. Myhre, *The pharmaceutical sector – Article 81 EC and Article 82 EC – Imperfect tools for an imperfect market?*, (in:) M. Johansson, N. Wahl, U. Bernitz (eds.), *Liber amicorum in honour of Sven Norberg: a European for all seasons*, Brussels 2006.

169 "The principle that the consumer should be able to buy goods from the cheapest source anywhere in the Community leads in particular to the need to protect trading intermediaries who buy from manufacturers to sell on to consumers, Parallel traders typically buy goods in low-priced areas of the Community and export them cheaply to higher priced areas,

and limitations to what is admissible in the operations of dominant medicinal products suppliers, who oppose this phenomenon for justified reasons. From the legal point of view, this confrontation becomes especially interesting when it is caused by actions undertaken by entities possessing a dominant position in the relevant markets defined for the purposes of particular antitrust cases[170]. Such activities have become a reason for deliberations by the Court of Justice of the European Union (Court of Justice) in the cases of *Sot. Lélos kai Sia EE and Others v GlaxoSmithKline AEVE Farmakeftikon Proïonton* (case *Sot. Lélos kai Sia*)[171].

2. DISPUTE ON VALUES IN THE CONTEXT OF FACTS IN THE JOINED CASES OF SOT. LÉLOS KAI SIA EE AND OTHERS V GLAXOSMITHKLINE AEVE FARMAKEFTIKON PROIONTON

Due to the fact that the issue presented before the Court of Justice is of universal nature for to the pharmaceutical sector, and the practical importance of the ruling for entities participating in the trade in medicinal products, since 2005 the discussed cases (including also the case of *Syfait,* referred to below[172]), have involved a wide group of legal scholars in the European debate on delimiting in the European competition law what is admissible with respect to actions of medicinal product suppliers possessing a dominant position[173]. Participation in that discussion is

thus making it impossible for the higher prices to be maintained.", see C. Bellamy, G. Child, European Community Law of Competition, ed. by P. Roth, V. Rose, Oxford University Press 2008, p. 42.

170 In relation to unilateral actions undertaken by pharmaceutical suppliers not holding a dominant position, due to which the parallel market is limited as a result of refusing to supply medicinal products, the Court of Justice expressed its opinions in the judgment of 6 January 2004 in cases C-2/01 and 3/01, Bayer v Commission, ECR [2004] 23. Issues connected with limiting parallel trade with medicinal products which stems from an agreement of a supplier with wholesalers and which introduced a distinction between prices imposed by wholesalers applied in selling medicinal products to pharmacies or hospitals within the territory of a particular state (whose costs of purchase are subject to reimbursement) and higher prices imposed on export of medicinal products to other Member States, were also assessed by the Court of First Instance (the Court within the meaning of the Treaty on the Functioning of the European Union) in the its judgment of 27 September 2006 in case T-168/01 GlaxoSmithKline v Commission, ECR [2006] II-2969, and the Court of Justice in its judgment of 6 October 2009 in relation to appeals against the judgment in question (not published yet).

171 Judgment of 16 September 2008, Joint Cases C-468/06 to C-478/06, ECR [2008] I-7139.

172 Case C-53/03 Synetairismos Farmakopoion Aitolias & Akarnanias (Syfait) v. Glaxosmithkline Plc, ECR [2005] I-4909.

173 See C. Koenig, C. Engelmann, *Parallel trade restrictions in the pharmaceuticals sector on the test stand of Art. 82 EC. commentary on the opinion of Advocate General Jacobs in the case Syfait/GlaxoSmithKline*, European Competition Law Review 2005, 26(6), 338-348; D. McCann, *Syfait v GlaxoSmithKline: Article 82 and parallel trade of pharmaceuticals*, European Competition Law Review 2005, 26(7), 373-374; G. Robert, S. Ridley, Parallel *trade in the pharmaceutical sector: scourge or benefit?,* European Competition Law Review 2006, 27(2), 91-95; A. Dawes, *Neither head nor tail: the confused application of EC competition law to the pharmaceutical sector*, European Competition Law Review 2006, 27(5), 269-278; R. Eccles, *Parallel exports in the pharmaceuticals sector: taking nothing for granted*, European Competition Law Review 2007, 28(2), 134-142; A. Coscelli, G. Edwards, A. Overd, *Parallel trade in pharmaceuticals: more harm than good?*, European Competition Law Review 2008, 29(8), 490-492; C. Desogus, *Parallel trade and pharmaceutical R&D: the pitfalls of the rule of reason*, European Competition Law Review 2008, 29(11), 649-665; P. Turner-Kerr, *Finally a bit of clarity for pharmaceutical companies; but uncertainties remain: judgement of the ECJ in Sot Lelos kai Sia EE v GlaxoSmithKline AEVE*, European Competition Law Review 2009, 30(2),

advisable, although one can certainly worry that taking a stance here might make one feel, as Advocate General D. R.-J. Colomer put it, *"like Avellaneda writing the second part of somebody else's novel, and, like that author, [one] could be criticised for this"*[174]. At the beginning, it is justified, however, to outline facts on the basis of which the second part of somebody else's novel is now being written.

In November 2000, a Greek company belonging to the GlaxoSmithKline group, GlaxoSmithKline AEVE Farmekeftikon Proïonton (GSK AEVE), implemented a new system of sales concerning a group of GlaxoSmithKline's medicinal products by providing direct supplies of selected products to domestic hospitals and pharmacies. Before the new model was implemented, the products were sold to hospitals and pharmacies by independent wholesalers (suing in the case referred to below), who, due to implementation of the new system, were refused by GSK AEVE the supply of the medicines concerned since the company itself took over the task of distributing these products within the domestic market.

What needs to be emphasised is that the group of products covered with the new sales system included a product representing a relevant market on which the Greek supplier had a dominant position.

In 2001, the principles of the new sales system were modified by GSK AEVE. The company decided to resume selling the medicinal products concerned to the wholesalers, yet in limited amounts. The mechanism of setting the limits determined by GSK AEVE assumed meeting the national demand for the products and estimated the risk of fluctuations in domestic demand at the level of 18%. GSK AEVE consulted this mechanism with the Greek competition protection authority (*Epitropi Antagonismou*).

The modified sales strategy became a cause of many complaints being submitted to the Greek competition protection authority by wholesalers, their associations as well as pharmacists' associations. They claimed that the discussed policy, introduced and then modified by GSK AEVE, was a manifestation an abuse of a dominant position within the meaning of the current Article 102 TFEU and

57-60; X. Groussot, T. T. Nguyen, T. Minssen, *The rule of reason under Article 82 after Sot .Lelos Kai Sia*, Lund University, 2009; T. Graf, *Dominant companies may not refuse ordinary orders with the aim of restricting parallel trade: the ECJ judgement in GlaxoSmithKline AEVE*, European Competition Law Review 2009, 30(4), 194-197.

174 Opinion of Advocate General Damas Ruiz-Jarabo Colomer delivered on 1 April 2008; point 3; available at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:62006C0468:EN:HTML.

the relevant provisions of the Greek antitrust law. This induced the Greek competition protection authority to launch antitrust proceedings against the supplier. In the course of this case, the Greek competition protection authority asked the Court a number of questions concerning the interpretation of the abovementioned article (*Syfait* case). They were not answered, however, due to the fact that the Court of Justice did not recognise its jurisdiction with respect to issuing the preliminary ruling, although on the other hand, they provided the valuable and important opinion presented by Advocate General F. Jacobs[175].

The investigations conducted by the Greek competition protection authority coincided with civil proceedings before the court of first instance in Athens (*Polymeles Protodikeio Athinon*), initiated by the wholesalers involved in the antitrust case. They claimed that the refusal to supply which resulted from the new sales system introduced by GSK AEVE in November 2000 was a manifestation of an abuse of a dominant position. Therefore, the suing wholesalers demanded, first of all, that GSK AEVE be ordered to supply to them the medical products concerned in amounts equal to the average monthly supplies taking place between 1 February and 31 October 2000. Second of all, they requested to be paid a compensation for the losses and missed profits due to the implementation of the sales system in question[176].

The court of first instance in Athens dismissed the wholesalers' claims stating that the refusal to supply was not unjustified and was not an abuse of dominance by the supplier. The claimants appealed against the judgements to the appeal court in Athens (*Efeteio Athinon*). This court, having received no response from the Court of Justice concerning the prejudicial questions asked in the case *Syfait*, repeated them in this case, seeking clarification of the following issues:

"1. Where the refusal of an undertaking holding a dominant position to meet fully the orders sent to it by pharmaceuticals wholesaler is due to its intention to limit their export activity and, thereby, the harm caused to it by parallel trade, does the refusal constitute per se an abuse within the meaning of Article 82 EC? Is the answer to this question affected by the fact that the parallel trade is

175 Opinion of Advocate General Francis Jacobs delivered on 28 October 2004; available at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:62003C0053:EN:HTML.

176 Some claims aimed at obliging GSK AEVE to perform supplies of the size corresponding to the amount of average monthly supplies of particular medicinal products, performer by GSK AEVE within the same period, increased by a specific percentage.

particularly profitable for the wholesalers because of the different prices, resulting from State intervention, in the Member States of the European Union; that is to say, by the fact that pure conditions of competition do not prevail in the pharmaceuticals market, but a regime which is governed to a large extent by State intervention? Is it ultimately the duty of a national competition authority to apply Community competition rules in the same way to markets which function competitively and those in which competition is distorted by State intervention?

2. If the Court holds that a limitation in parallel trade, for the reasons set out above, does not constitute an abusive practice in each case where it is engaged in by an undertaking holding a dominant position, how is possible abuse to be assessed?

In particular:

(a) Does the percentage by which normal domestic consumption is exceeded and/or the loss suffered by an undertaking holding a dominant position compared with its total turnover and total profits constitute appropriate criteria? If so, how is the level of that percentage and the level of that loss determined (the latter as a percentage of turnover and total profits), above which the conduct in question may be abusive?

(b) Is an approach entailing the balancing of interests appropriate, and, if so, what are the interests to be compared?

In particular:

(i) is the answer affected by the fact that the ultimate consumer/patient derives limited financial advantage from the parallel trade; and

(ii) is account to be taken, and to what extent, of the interests of social insurance bodies in cheaper medicinal products?

(c What other criteria and approaches are considered appropriate in the present case?"[177].

177 *Sot .Lelos Kai Sia* (n 171, above) para. 23.

These preliminary matters addressed in the context of the cases *Sot. Lélos kai Sia* may be considered from several perspectives.

Following the stance of the Court of Justice, one may consider the issue in dispute being the subject of domestic proceedings, only within the framework of competition law and limit it to the assessment of "whether there is an abuse of a dominant position contrary to Article 102 TFEU if a pharmaceuticals company occupying such a position on the national market for certain medicinal products refuses to meet orders sent to it by wholesalers on account of the fact that those wholesalers are involved in parallel exports of those products to other Member States."[178] The case may also be treated, however, as a complex system problem in the context of which the Court of Justice faced *de facto* the task of assessing the hierarchy of two competing values, on the one hand – free competition manifesting itself in unlimited parallel trade in the territory of the EU, which is historically grounded in the Court of Justice's case law[179], on the other hand – the protection of domestic patients' interests, which a supplier of medicinal products is obliged to ensure by meeting relevant orders from wholesalers supplying pharmacies and hospitals in a particular Member State, according to Directive 2001/83 on the Community code relating to medicinal products for human use (Directive 2001/83)[180].

3. REFUSAL TO MEET AN ORDER BY A DOMINANT SUPPLIER OF MEDICINAL PRODUCTS IN RELATION TO THE CONCEPT OF THE ABUSE OF A DOMINANT POSITION *PER SE*, ACCORDING TO THE COURT OF JUSTICE

The considerations of the Court of Justice, differently than the opinion of Advocate General F. Jacobs in the case *Syfait,* focused in particular on the first question – i.e. assessing "the refusal of an undertaking holding a dominant position to fully meet orders sent to it by pharmaceutical wholesalers that is due to its intention

178 *Sot .Lelos Kai Sia* (n 5, above) para. 28.

179 When applying Article 81 EC, the Court of Justice had several occasions to question agreements that had as their object the partitioning of the Common Market (in particular by limiting or hindering parallel trace within the European market). See Cases 96/82 to 102/82, 104/82, 105/82, 108/82 and 110/82 IAZ International Belgium and others v Commission [1983] ECR 3369, paras. 23-27; C-306/96 Javico [1998] ECR I-1983, paras. 13-14; C-551/03 P General Motors v Commission [2006] ECR I-3173, paras. 67-69.

180 Directive 2001/83/EC of the European Parliament and of the Council of 6 November 2001 on the Community code relating to medicinal products for human use (OJ L 311, p. 67), amended with the Directive 2004/27/EC of the European Parliament and Council of 31 March 2004 (OJ L 136, p. 34).

to limit their export activity *and* (author's emphasis), thereby, the harm caused to it by parallel trade"[181].

It can seem surprising that the Court of Justice constructed its argument using well-known concepts of competition law, starting, first of all, with the statement that "the refusal by an undertaking occupying a dominant position on the market of a given product to meet the orders of an existing customer constitutes abuse of that dominant position under Article 82 EC where, without any objective justification, that conduct is liable to eliminate a trading party as a competitor"[182]. The Court of Justice reminded also that it stems from settled case-law that "an undertaking in a dominant position for the purpose of marketing a product – which cashes in on the reputation of a brand name known to and valued by consumers – cannot stop supplying a long-standing customer who abides by regular commercial practice, if the orders placed by that customer are in no way out of the ordinary."[183]

Therefore, "in order to determine whether the refusal by a pharmaceuticals company to supply medicinal products to such *wholesalers* (i.e. existing customers – author's emphasis) indeed falls within the prohibition laid down in Article 82 EC, in particular at point (b) of the second paragraph of that article, it must be examined whether, as GSK AEVE maintains, there are objective considerations based on which such a practice cannot be regarded as an abuse of the dominant position occupied by that undertaking."[184] Such a method of assessing the case should also be adopted, in the Court of Justice's opinion, if refusing to meet orders concerns clients performing parallel exports of medicinal products to Member States where prices for medicines are higher[185].

181 In doctrine, this quite selective approach of the Court of Justice to the scope of initial issues addressed by the court of appeal in Athens was criticised. See e.g. X. Groussot, T. T. Nguyen, T. Minssen, *The rule … op. cit.*, p. 16-17; P. Turner-Kerr, *Finally … op. cit.*, p. 59-60; T. Graf, *Dominant companies … op. cit.*, p. 196-197. As a matter of fact it is difficult to avoid at least a comparison between the thoroughness and complexity of conclusions included in opinions of Advocates General F. Jacobs and D. R.-J. Colomer in relation to questions formulated by the domestic court, including the question about the criteria determining that there are objective reasons of refusing to meet wholesalers' orders, which were left unanswered by the Court of Justice.

182 *Sot .Lelos Kai Sia* (n 171, above) para. 34, in which the Court of Justice referred to: Cases 6/73 and 7/73 Istituto Chemioterapico Italiano and Commercial Solvents v Commission, [1974] ECR 223, para. 25; Case 27/76 United Brands and United Brands Continental v Commission, [1978] ECR 207, para. 183.

183 *Sot .Lelos Kai Sia* (n 171, above) para. 49, where the Court of Justice quoted para. 182 of the judgment in case United Brands and United Brands Continental v Commission.

184 *Sot .Lelos Kai Sia* (n 171, above) para. 39, where the Court of Justice recalled para. 184 of the judgment in case United Brands and United Brands Continental v Commission and recalled para. 69 of the judgment in Case C-95/04 P British Airways v Commission, [2007] ECR I-2331.

185 *Sot .Lelos Kai Sia* (n 171, above) para. 51.

The Court of Justice searched for objective reasons for *prima facie* abuses of the prohibition set forth in Article 102 TFEU, examining mainly the impact of State price and supply regulation in the national pharmaceuticals sector, leaving unanswered the national court's questions about other factors allowing to identify the existence of an objective justification for refusing to supply. These issues were addressed by Advocate General F. Jacobs in his opinion in *Syfait* case. He discussed such significant issues as, for example, the economic side of the innovativeness if the pharmaceutical industry, or the impact of parallel trade on consumers and buyers in a given Member State. Therefore, one may feel not entirely satisfied with the depth of the analysis in the discussed judgement, considering the importance of the topic that was examined by the Court of Justice[186].

In relation to the impact of State price and supply regulation in the national pharmaceuticals sector, the Court of Justice observed that in the case of enterprises operating in the territory of Member States where sale prices of medicines (or reimbursement of medicines) are regulated by public bodies, "when assessing (…) whether the refusal of a pharmaceuticals company to supply medicines to wholesalers involved in parallel exports constitutes abuse, it cannot be ignored that such State intervention is one of the factors liable to create opportunities for parallel trade"[187]. The Court of Justice emphasised clearly, however, that the degree of price regulation in the pharmaceuticals sector does not generally preclude the European competition law from applying in the context of cases of this type[188]. On the other hand, however, differences in national price regulations should not lead to a situation when dominant medicines suppliers in a Member State with low prices of medicinal products cannot undertake reasonable and proportionate actions aimed at protecting their own commercial interests[189]. The Court of Justice considered that this is the case when a dominant medicine supplier refuses to meet abnormal orders from wholesalers whose aim is to obtain supplies of products intended mainly for parallel export[190]. At the same time, the Court of Justice entrusted Member States with specifying the volume of an abnormal order and emphasised that this kind of calculation should be performed taking into consideration the *needs* [author's emphasis] of the domestic market

186 See n 181.
187 *Sot. Lélos kai Sia* (n 171, above) para. 67.
188 *Sot. Lélos kai Sia* (n 171, above) para. 67.
189 *Sot. Lélos kai Sia* (n 171, above) para. 69.
190 *Sot. Lélos kai Sia* (n 171, above) para. 71.

and the previous business relations between the dominant supplier and wholesalers[191].

It is probably difficult to understand the argumentation given by the Court of Justice as something other than a recognition of the rule of reason in the process of assessing specific kinds of enterprises' conducts under Article 102 TFEU and as challenging the validity of applying the concept of *per se* abuses of a dominant position – which, indeed, is controversial taking into account the abovementioned Treaty provision[192]. What is important, while constructing the rule of reason in the discussed case, the Court of Justice referred methodologically to the rule of reason developed in the case law concerning assessing actions of Member States that had resulted in limitations of the fundamental freedoms stipulated in the Treaty[193], including the principle of free movement of goods, which is also an issue in the cases *Sot. Lélos kai Sia.* The rule of reason seems acceptable in cases concerning abuses of a dominant position also in light of the opinion of Advocate General D. R.-J. Colomer[194]. It is worth recalling here that deducing the rule of reason on the basis of the facts in question was approached for the first time by Advocate General F. Jacobs in his opinion in the case *Syfait*[195]. He pointed to three basic reasons justifying such

191 In cases *Sot. Lélos kai Sia,* para. 77, the Court of Justice concluded: "Article 82 EC must be interpreted as meaning that an undertaking occupying a dominant position on the relevant market for medicinal products which, in order to put a stop to parallel exports carried out by certain wholesalers from one Member State to other Member States, refuses to meet ordinary orders from those wholesalers, is abusing its dominant position. It is for the national court to ascertain whether the orders are ordinary in the light of both the size of those orders in relation to the requirements of the market in the first Member State and the previous business relations between that undertaking and the wholesalers concerned."

192 See more: C. Bellamy, G. Child, *European Community Law of Competition…op. cit*., p. 950 et seq.; R. Whish, Competition Law, Oxford University Press 2009, p. 196 et seq.; T. Skoczny, (in:) *Ustawa o ochronie konkurencji i konsumentów. Komentarz.*, ed. by T. Skoczny, Warszawa 2009, p. 619 et seq.; K. Kohutek, M. Sieradzka, (in:) *Ustawa o ochronie konkurencji i konsumentów. Komentarz.*, Warszawa 2008, p. 349 et seq.

193 Among others, Cases 120/78 Rewe-Zentral AG v Bundesmonopolverwaltung für Branntwein, [1979] ECR 649; Case C-55/94 Reinhard Gebhard v Consiglio dell'Ordine degli Avvocati e Procuratori di Milano, [1995] ECR I-4165 and Case C-415/93 Union Royale Belge des Sociétés de Football Association ASBL v Jean-Marc Bosman, Royal club liégeois SA v Jean-Marc Bosman and Others as well as Union des Associations Européennes de football (UEFA) v Jean-Marc Bosman, ECR [1995].

194 According to the Opinion of Advocate General D. R.-J. Colomer: "1) Article 82 EC does not provide a basis for attributing conduct which is abusive per se to undertakings in a dominant position, even when the circumstances of the case show that there is intent and an anti-competitive effect caused by that conduct. 2) The refusal of an undertaking holding a dominant position to meet fully the orders sent to it by pharmaceutical wholesalers by reason of its intention to limit their export activity and, thereby, the harm caused to it by parallel trade constitutes an abuse within the meaning of Article 82 EC. However, the undertaking may produce the relevant evidence in order to justify its behaviour objectively, in particular: (i) matters relating to market regulation which constrain it to behave in this manner, given that it is not within its power to change such regulation, disregarding, in the present case, the setting of prices for medicinal products and the obligation to maintain reserves in order to supply patients, (ii) proof that its only purpose was to protect its legitimate business interests, which do not include, in the present case, the impact on incentives to innovate; (iii) the economic benefits of the conduct in question."

195 The opinion of Advocate General was not unequivocally received in literature. See C. Koenig, C. Engelmann, *Parallel trade … op. cit.*., p. 341 et seq.

a position. Firstly, dominant entities have the obligation to supply only in special circumstances. Secondly, there are justified reasons to prove that this obligation does not exist. Thirdly, refusing to supply should be assessed in terms of the special economic and regulatory conditions which are relevant in a given case[196]. Advocate General F. Jacobs underlined also that he regards the conclusion reached in his opinion "as highly specific to the pharmaceutical industry in its current condition (namely existing at the moment of issuing the opinion – author's notice) and to the particular type of conduct at issue in the present proceedings"[197]. Although, while according to Advocate F. Jacobs, it "is highly unlikely that any other sector would exhibit the characteristics which [would lead] to conclude that a restriction of supply in order to limit parallel trade is defensible in relation to pharmaceutical products"[198], the judgment of the Court of Justice did not include a similar restriction.

The position of the Court of Justice, although developed mainly from the point of view of competition law, should be also considered in a broader context, taking into account the legal framework provided in Directive 2001/83[199], which should have been implemented into domestic legal systems by 30 October 2005. Pursuant to Article 81 of this Directive, medicinal products suppliers' obligation to provide medicines to pharmacies and other entities entitled to supply the domestic market in medicinal products should be performed *so that the needs of patients in the Member State in question are covered* (author's emphasis)[200]. The same article of Directive 2001/83 imposes on Member States the obligation to ensure that: "the arrangements for implementing this Article [are], moreover, justified on grounds of public health protection and be proportionate in relation to the objective of such protection, in compliance with the Treaty rules, particularly those concerning the free movement of goods and competition", which are clearly manifested in the phenomenon of parallel trade. Is it possible, therefore, to formulate a conclusion that the dispute which is the essence of the case *Sot. Lélos kai Sia* also lies immanently in the

196 X. Groussot, T. T. Nguyen, T. Minssen, *The rule … op. cit., p.* 13.

197 Opinion of Advocate General F. Jacobs (n 175, above) point 101.

198 Opinion of Advocate General F. Jacobs (n 175, above) point 102.

199 It was broader referred to by Advocate General F. Jacobs in point 82 et sec. of the opinion (n 175, above).

200 According to Article 81 of Directive 2001/83: "The holder of a marketing authorisation for a medicinal product and the distributors of the said medicinal product actually placed on the market in a Member State shall, within the limits of their responsibilities, ensure appropriate and continued supplies of that medicinal product to pharmacies and persons authorised to supply medicinal products so that the needs of patients in the Member State in question are covered."

European sector regulations determining the legal frameworks applied to the pharmaceuticals sector? *Prima facie,* Article 81 of Directive 2001/83 can be interpreted, in relation to the obligation to supply medicinal products, as weighing, on the one hand, the legally protected interests of patients in a given Member State and, on the other, free movement of goods and unlimited competition. Confronting these values at the regulatory level is not appropriate, though. Paragraph 4 of Preamble to Directive 2001/83, clearly states that "The main purpose of any regulation on the manufacture and distribution of medicinal products for human use should be to safeguard public health." Therefore, the values put on that other side of the scale are not the most important ones protected by the Directive 2001/83.

The above argument – which from the systemic point of view is the most coherent with the judgment of the Court of Justice in the cases *Sot. Lélos kai Sia* – should also be taken into account when assessing the limits to permitted activity by dominant medicinal products suppliers towards wholesalers exercising their right (limited though, as the Court of Justice ruled) to stimulate parallel trade in medicinal products in the territory of the EU.

Bohdan Wyżnikiewicz

BUSINESS CYCLES AND UNLAWFUL AGREEMENTS

1. INTRODUCTION

Economic growth occurring in the conditions of strong globalisation processes leads to tighter competition both on domestic markets and on the international arena. Strong competition for markets and customers inclines some enterprises to conclude unlawful agreements, which usually take the form of price fixing. There is a hypothesis, or more likely a supposition, backed up by numerous observations by national antitrust authorities that the enterprises' inclination to take on such agreements grows at a time of economic crises[201]. Such considerations will pose as the main topic of this paper. They will primarily encompass theoretical discussion, since empirical examination of the above-mentioned hypothesis requires data covering several dozen of years and spanning a few full business cycles, which in the Polish context is not possible.

2. BUSINESS CYCLES

Market economy evolves in cycles, which means that periods of quicker or slower economic growth, or absolute decline of production levels take place one after the other. There are many causes of the uneven growth rate. Most important of them include: seasonal nature of economic phenomena, resulting e.g. from the changing seasons of the year, circumstantial factors and so-called business cycles. Business cycle is the fluctuation of production levels against the long-term growth trend. These cycles fall into four subsequent phases, whose duration and amplitude is varying and difficult to anticipate. These are, respectively: recession, recovery, expansion and contraction.

Recession translates into a decline in economic activity measured by a set of macroeconomic indicators, among which the most important one is Gross Domestic Product (GDP), referred to in simplified terms as national income. For us to talk about recession, the decline in the economic activity should spread over at least two subsequent quarters. It is a frequent criterion allowing

201 Such opinions were expressed by Presidents of the antitrust authorities of Germany, Austria and the Netherlands during the International Competition Law Forum organised by UOKiK on 16 April 2009 in Warszawa.

us to say that recession has taken place, although no unequivocal definitions exist in that regard in the theory of economics. In a business cycle, recession is followed by recovery, i.e. a period in which economic growth is observed, production and employment increase and the incomes of both enterprises and the population rise. Recovery evolves into expansion, when economic growth is remains high for a period of a few to a couple dozen of quarters. If the economic growth rate reaches a very high level, then we may speak of economic overheating. The last phase of a typical business cycle is gradual contraction, which later evolves again into recession.

Recently the concept of gross domestic product as the measure of economic growth is being questioned. The criticism results, in my opinion, from a certain misunderstanding. People who are only lightly involved in economic issues, such as journalists or politicians, would like the GDP to measure more than the statistical output of business activity, despite the fact that this is the only purpose for which it was devised.

In economic practice, business cycles are not regular and tend to deviate from the above model. If the expansion phase is followed by contraction, such a situation does not have to end in a recession. Quite often, instead of recession, a period of economic slowdown follows. Slowdown consists in the economy showing a lower growth rate than in the recovery period, but no recession, i.e. a period of negative economic growth, takes place. The observation of business cycles in the United States allowed researchers to conclude that their duration in the 20th century gradually extended and, towards the end of the millennium, reached 12 years[202].

The fact that the economy has entered the phase of recession or that such phase has ended is known only after some time – usually at least one month, more often several months. This is a result of the fact that estimating the GDP by the national statistical services is an arduous and time-consuming process.

During recession, the levels of production decline as a result of lower consumption demand and subsequent decreasing investment demand. Recession translates also into lower consumer incomes, growing unemployment, as well as decreasing business revenues.

202 The American National Bureau of Economic Research provides data on business cycles' duration in the United States of America since 1857: http://www.nber.org/cycles/cyclesmain.html.

In most countries recession is now more frequently caused by external than internal factors. It results from globalisation, which in this case means the so-called synchronisation of business cycles, i.e. their similar course in different countries. Signs of such synchronisation are visible in integrating economic groupings such as the European Union.

3. ENTERPRISE BEHAVIOURS AT THE TIME OF RECESSION

When the economy enters the phase of recession, called a crisis by some experts, enterprises are the first ones to notice. We need to realise, however, that they experience it in a totally different way. It usually depends on the sector of the economy where they operate, but also on their geographical location. Enterprises in some sectors are more sensitive to recession, others are less.

A sector's sensitivity to the phenomenon of recession depends on many factors and may have different intensity in the course of subsequent recessions. In general, recession is much stronger felt in sectors producing higher-end commodities, i.e. luxury goods. On the other hand, sectors producing essential goods, or lower-end products, with low price flexibility of demand are less susceptible to crises. Another factor is the dependence on bank loans. If lending policies are stricter, i.e. when financial institutions introduce higher requirements towards borrowers, many enterprises are not able to obtain loans or loans are granted to them at much less favourable conditions than to other entities.

Sectors sensitive to market changes develop quicker than others in periods of recovery and expansion, but suffer much greater losses than the rest of the economy during contraction and recession.

The reasons behind the changes in the economic situation, in particular occurrences of recession, may be different, which means that the impact of such fluctuations on the economic situation of individual sectors will also vary for exactly the same reasons. If the contraction results from external factors, then it mostly affects those sectors which focus on export and those which are strongly connected with the exporting sectors. But if recession is caused by domestic factors, then the situation is quite opposite – the recession affects mostly those companies which produce mainly for the domestic market.

Within one sector some enterprises may remain unaffected by recession if they have been well managed in the long term. Good management here means creating an effective growth strategy and consequent implementation thereof, along with an appropriate and early preparation for the possible occurrence of a recession or crisis.

Most common effects of recession in undertakings include mainly declines of the production levels, lower profits or losses, layoffs, freezing ongoing investments, indebtedness as well as loss of some outlets, etc. Most undertakings which suffer from the effects of a crisis see the source of their difficulties rather in external factors than problems originating internally in their organisations. The typical reaction to difficulties which threaten the existence of companies is their entering the grey areas of the economy, in other words, avoiding taxes by under-representing their turnover in the accounting documents, tax returns and statistical reports.

Such escape strategy is possible in small and medium-sized enterprises on dispersed markets due to a large number of suppliers and recipients. For large and very large enterprises operating in markets characterised by a small number of producers and a limited number of recipients, „running away" from the effects of recession is not possible. Some large enterprises may, however, be inclined to apply unlawful practices, including the conclusion of price fixing agreements. We need to remember, though, that recession or crisis-related processes are only one, not necessarily the most important, reason for employing unlawful practices.

4. THE GLOBAL FINANCIAL AND ECONOMIC CRISIS IN 2008–2009

Since the second half of 2008, global economy remains in a deep financial crisis, which in most economically developed countries contributed to recession. Generally speaking, the reason for such developments was the inappropriate monetary policy of the Federal Reserve and the lending policies of the banks which provided services to the real estate market in the United States, which led to speculative overheating of that market. The global capital markets slump, and a crisis of consumer confidence in the banking sector followed, which resulted in a long freeze of the inter-bank market, and in the end a drastic decrease in the crediting activities of banks.

The world's most developed economies found themselves in recession. Only a few managed to maintain a positive economic growth rate. Poland as the only European Union Member State was among the few countries which managed not to suffer from recession. According to the estimates of the International Monetary Fund, the global GDP growth rate in the world's most important economies and in Poland is the following:

Table 1 GDP growth rate (percentage) in the global economy, in developed countries, in the European Union and in Poland in 2007-2010 and forecast for 2009-2010

	2007	2008	2009	2010
Globally	5.2	3.0	-1.1	3.1
Developed countries	2.7	0.6	-3.4	1.3
European Union	3.1	1.0	-4.2	0.5
Poland	6.8	4.9	1.0	2.2

Source: World Economic Outlook, October 2009, International Monetary Fund

It may be assumed that the occurrence of recession in most countries of the world influenced the increase in the number of cartels created globally. Information in this regard will be available in a few quarters of the year.

5. CARTELS AND BUSINESS CYCLES

In economically developed countries, cartels are defined as unlawful agreements referring to price levels or other conditions of market transactions, concluded secretly between enterprises (producers) to improve the conditions in which they operate. Such activities practically eliminate competitive mechanisms. Cartels most often occur in a relatively small group of market sectors, such as telecommunications, construction, building materials production, production of house appliances, transport; most often in oligopolies. In sectors characterised by oligopoly structure, recession often leads to market limitations and bankruptcies. In such sectors strong and long cycles may occur, regardless of business cycles observed at the macroeconomic level. The construction sector and the building materials industry, both linked closely together, constitute an example of a market which is particularly sensitive to such fluctuations.

An empirical assessment of the impact of business cycles on the enterprises' susceptibility to concluding illegal agreements is quite difficult in the Polish context. This is due to several reasons.

First, information concerning the conclusion of cartel agreements may come only from the the Office of Competition and Consumer Protection, and not from independent observations or estimations. The Office publishes this kind of information at a point which is completely unrelated to the moment at which a given agreement was concluded. It seems impossible to determine unequivocally when an agreement of this kind could have in fact been concluded. Usually preparations or negotiations relating to collusions last for several months. Business cycle phases, on the other hand, last for a few months to several years. We need also to face the fact that not all collusions are detected by the antitrust authority. Thus, it is impossible to specify exactly at which point of a business cycle a given agreement was made. The moment can only be roughly estimated.

Second, since the beginning of the political transformation, only one full business cycle was observed in Poland, namely in 1991–2001. Currently Poland is in its second cycle, which has not reached the recession phase yet. Currently, only an economic slowdown can be observed, which most probably will transform into recession with time. The period of observation is thus too short to establish any regularities.

An alternative method of examining the inter-dependence between the inclination to conclude unlawful price-fixing agreements by Polish undertakings and the business cycle could involve an empirical examination of enterprises suspected of concluding such collusive agreements. These surveys would have to be conducted indirectly and must be completely independent from the operations of the antitrust authority. Some techniques developed for the analysis of the grey zone in the economy ought to be used. Such analysis should also provide for the identification of other factors inclining enterprises to conclude unlawful agreements.

6. FOREIGN EXPERIENCES

My further considerations will be based on the theoretical analyses provided in literature, usually supported by calculations based on theoretical models and taking account of approaches applied in game theory. Thus, conclusions are rather hypotheses than confirmed facts or behaviours. Researchers are mostly interested in examining the inclination to create cartels in the expansion and recession phases of a business cycle. Literature is not particularly vast in this respect; it is in fact limited to a few items cited by authors analysing illegal collusions in the context of business cycles.

Many economists accept the popular hypothesis formulated in the early 1980s by Rotemberg and Saloner[203] and confirmed by Haltiwanger and Harrington[204] in the early 1990s, stating that business cycles, or to be more precise, the fluctuations in demand, make it more difficult to conclude unlawful collusions. Corporate behaviours are analysed in terms of game theory, indicating optimal solutions for enterprises creating an oligopoly. Model calculations indicate that in the recovery phase of a business cycle oligopoly participants show an inclination to compete with each other. Collusions are more often concluded when the volume of future demand is certain.

In the opinion of the above mentioned authors, a situation where the future revenues of cartel participants are known happens when the economy is doing well, while economic contraction translates into uncertainty regarding future profits, leading many cartels to simply disintegrate. The authors conclude also that price fixing agreements are more profitable in the recovery phase than at the time of recession. This follows from the fact that potential fines imposed if collusion is detected by antitrust authorities are the same, regardless of the business cycle. Paying the fine after a period of high profits is much less burdensome than during a period of low profits or losses suffered during recession.

Based on theoretical analyses, also Ivaldi et al[205] reached a similar conclusion stating that demand fluctuations make it more difficult to enter into collusions. They analysed the behaviours of undertakings against demand fluctuations in general, not necessarily related to business cycles. They believe that collusions occur less often when these fluctuations are accidental and more often if they are predictable, mainly as a result of the natural sequence of the seasons.

Bagwell and Staiger[206] attempted at a generalisation of the Haltiwanger and Harrington's approach by building models with stochastic (random) distribution of demand fluctuations within a business cycle. They concluded that collusions are of cyclical nature and their frequency depends on the rate at which demand grows and the expected duration of the expansion phase of the business cycle.

203 J. Rotemberg, G. Saloner, *A Supergame-Theoretic Model of Business Cycles and Price Wars During Booms*, NBER Working Paper Series 1412, August 1984.

204 J. Haltiwanger, J. Harrington, *The impact of cyclical demand movements on collusive behavior*, RAND Journal of Economics, 1991, Vol 22, no. 1.

205 M. Ivaldi, B. Jullien, P. Rey, P. Seabright, J. Tirole, *The Economics of Tacit Collusion*, Final Report for DG Competition, European Commission, March 2003.

206 K. Bagwell, R. Staiger, *Collusion over the business cycle*, RAND Journal of Economics, 1997, Vol. 28.

Examining companies at risk of bankruptcy during recession, Canadian researcher Eswaran[207] observed that when threatened, companies tend rather to terminate collusive agreements than to conclude them. In such circumstances, participants of such agreements strongly rely on competition and perceive it as their chance to overcome difficulties. Eswaran believes that only if there is a cartel participant whose costs are low, the established division of the market can be maintained. This is achieved by the members of the oligopoly dividing the market in a way that is adjusted to the conditions occurring during the recession.

Foreign economic literature concerning the relation between conclusion of collusive agreements and business cycles concentrates on theoretical model considerations. The barriers to the research presented above and methodological limitations largely explain the absence of empirical research in this regard.

7. CONCLUSION

The review of theoretical economic literature allows to formulate a hypothesis that undertakings more often and to a greater extent enter into collusions in the expansion phase, rather than at the time of recession. Theoretical conclusions contradict opinions often expressed by foreign antitrust authorities. Multi-annual observations of the phenomenon of illegal collusions described in theoretical papers cited here suggest that periods of recession contribute to the creation of collusions. Similar conclusions may be drawn from the above-mentioned behaviours of undertakings during recession.

Despite the difficulties in conducting empirical research which would identify which phases of a business cycle are favourable for concluding price fixing agreements, such examinations should be conducted using indirect methods and in-depth case studies. Empirical research should rather be aimed at verifying theoretical hypotheses rather than at creating new ones. Research based on a sample covering as many undertakings from various European Union states as possible should also be considered. Such analyses would be easier, since the ongoing processes of integration lead to greater synchronisation of the business cycles in EU Member States.

207 M. Eswaren, *Cartel unity over the business cycle*, Canadian Journal of Economics, vol. XXX, Nr 1, August 1997.

Chapter II

MERGER CONTROL

Jan Krzysztof Bielecki

SELECTED ASPECTS OF COMPETITION AND CONSUMER PROTECTION IN BANK MERGERS

In this paper, I would like to illustrate the problem of competition and consumer protection in bank mergers with a description of the case of a merger between Bank Pekao S.A. and a spun-off part of Bank BPH SA. This transaction was an unprecedented one in the history of bank mergers in Poland; its completion was a deviation from the traditional models of bank mergers. It is worth a comment also for the reason that, in my opinion, a transaction of this kind will not happen again. Its conditions had been specified in an agreement concluded by the Ministry of Treasury (MSP) with UniCredito Italiano S.p.A. (UniCredit, UCI), the majority shareholder of both banks. Next, the Banking Act[208] was amended under the urgent procedure, providing for a division of banks operating as joint stock companies, as specified in Article 529 (1)(4) of the Commercial Companies Code[209].

The agreement between MSP and UCI was preceded by a widely publicized battle against the decision of the European Commission of 18 October 2005. The Commission stated that the notified merger as a result of which Italian UCI would acquire control over German Bayerische Hypo-und Vereinsbank (HVB), falls within the scope of the Council Regulation (EC) on the control of concentrations between undertakings (Regulation)[210], i.e. has a Community dimension, and thus falls under the jurisdiction of the Commission. The Commission also stated that the merger "does not raise serious doubts as to its compatibility with the common market and the EEA Agreement"[211].

208 Article 124c of the Banking Act, added under Article 1(3) of the Act of 18 October 2006 (Dz.U. 2006, No. 190, item 1401) stipulates:
"Article 124c. 1. Banks in the form of joint stock company may be divided exclusively in the way defined in Article 529(1)(4) of the Commercial Companies Code, with the proviso that the part of assets of the bank being divided shall be transferred to the joint stock company which is a domestic bank or a credit institution.
2. Division of the bank referred to in (1) shall require the authorisation of the Commission for Banking Supervision. The Commission for Banking Supervision shall refuse to issue such an authorisation if the division may turn out to be detrimental to the sound and prudent management of the bank being divided or the banks to which the assets of the bank being divided are transferred or if the division may cause substantial loss for the national economy or for the important interest of the State."

209 Article 529(1)(4) of the Commercial Companies Code (Dz.U. 2000, No. 94, item 1037) provides for "a division of a joint stock company by a transfer of a part of the company being divided onto the existing company or a newly established company (a spin-off)".

210 Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings (the EC Merger Regulation).

211 Point (1) and (2) of the Commission Decision of 18 October 2005, SG-Greffe(2005) D/205803.

Let us look back at the origins of the transaction. On 12 June 2005, UniCredit and HVB announced that the UCI Board of Directors as well as the HVB Management Board and Supervisory Board approved the agreement on business combination of HVB and UniCredit. The transaction was to consist of three voluntary share-for-share offers by UniCredit for HVB, Bank Auistria (a subsidiary of HVB) and Bank BPH SA (a subsidiary of Bank Austria). The offers were to be approved by relevant local authorities. The transaction was to be completed under the condition that the shareholders agree to raise the capital of UniCredit and all the necessary clearances be obtained from the regulatory authorities. Simultaneously to the merger announcement, UniCredit's management informed of the company's intention to introduce their shares, previously listed on the Milan stock exchange, for trading on the main market of the Frankfurt Stock Exchange and the Warsaw Stock Exchange.

On 13 September 2005, the European Commission was notified of the proposed merger in compliance with Article 4 of the abovementioned Regulation on the control of concentrations of undertakings, in order to for the Commission to assess the compatibility of the transaction with the common market. The Regulation applies to significant structural changes, whose impact on the market goes beyond the national borders of any one Member State, which is tantamount to the merger possessing a Community dimension[212].

The Regulation specifies both general rules and detailed procedures for the assessment of a notification of a proposed merger. As a general rule, transactions which have a Community dimension should be reviewed exclusively at the Community level[213]. Unless it is otherwise stipulated in the Regulation, Member States must not apply national competition legislation to mergers with a Community dimension. It regulates in detail the rules governing the referral

212 A merger with a Community dimension should be deemed to exist where the aggregate turnover of the undertakings concerned exceeds given thresholds (point (10) of the preamble to the Regulation). Basic thresholds are specified in articles (1) and (2) of the Regulation:
"A concentration has a Community dimension where:
(a) the combined aggregate worldwide turnover of all the undertakings concerned is more than 5 000 million; and
(b) the aggregate Community-wide turnover of each of at least two of the undertakings concerned is more than EUR 250 million,
unless each of the undertakings concerned achieves more than two-thirds of its aggregate Community-wide turnover within one and the same Member State."
The Regulation also provides for cases whereby a merger has a Community dimension despite the fact that undertakings do not achieve the abovementioned basic thresholds.
According to point (32) of the preamble, concentrations which, by reason of the limited market share of the undertakings concerned, are not liable to impede effective competition may be presumed to be compatible with the common market.

213 Point (8) of the preamble to the Regulation.

of mergers from the Commission to Member States and from Member States to the Commission. The main purpose of these solutions is to introduce an effective "corrective mechanism": these rules are designed to protect the competition interests of Member States in an adequate manner.

The merger of UniCredit and HVB fulfilled all the criteria specified for a merger with a Community dimension, which falls within the exclusive jurisdiction of the European Commission. Having assessed the notification, the Commission issued the abovementioned decision of 18 October 2005 confirming the merger's Community dimension. Considering the impact of the transaction on the markets of individual Member States, the European Commission stated that the impact of the proposed merger would be the greatest in Poland, because it would combine the second and the third largest banks in the market and create the leading player in terms of assets (21 percent of all banking assets)[214].

The notification, in the part related to the Polish market, was assessed with regard to the impact of the merger (i.e. the proposed merger of Bank Pekao S.A. and Bank BPH SA) on individual market segments: retail banking, including distribution of investment funds (mutual funds), corporate banking, factoring, financial services market, investment banking, assets management, payment clearing services and distribution of banking products.

The Commission stated that with regard to retail banking, despite the fact that the proposed transaction would increase the combined market share of both entities, there would still be strong competition from other banks, and thus the proposed merger does not raise doubts as to its compatibility with the common market. As regards retail services, the merged bank would become the leader with regard to investment accounts and the distribution of mutual funds. Nonetheless, the combined share would not affect the situation in the industry and would not create an opportunity to increase prices. The decisive fact was that both banks would not control distribution to the extent sufficient to influence the access of rival funds to the market, and there were no barriers to entry for any new EU fund managers; in addition, the market would retain its significant growth potential. [215]

214 Point (54) of the Commission Decision.

215 Results of the analysis of the retail banking market and the distribution of mutual funds are specified in points (56) - (67) of the Commission Decision.

With respect to corporate banking, the only market segment where the combined share would exceed 30 percent would be real estate project financing. The share would have been much smaller if the financing provided in Poland by foreign banks and financial institutions had been taken into account. The Commission declared that the proposed transaction would not significantly impede effective competition in corporate banking services. [216]

The analysis of the situation in other market segments led the Commission to conclude that the transaction would be without incremental effect on competition and prices. [217] With regard to the distribution network, the European Commission declared that "the combination of the branch networks of the parties will not lead to a significant reduction of choice in individual regions of the country. The market investigation has confirmed that at the level of each of the Polish voivodeships (regions), competition from branches of all the main rival banks would remain strong. In addition, there are more than 600 cooperative banks serving local areas throughout the country."[218]

Having conducted the procedure, the Commission decided not to oppose the notified merger and to declare it compatible with the common market and with the EEA Agreement.

More than two months after the Commission's decision, its legitimacy and legal validity was challenged by the Polish government. A discussion began that went on for a few months. At the same time, merger processes in other European countries, where the banks owned by UniCredit and HVB had been present, were well under way. In Poland, UniCredit was still waiting for a clearance from the Commission for Banking Supervision[219] to execute its voting rights following from its shares of Bank BPH SA (the application for clearance had been filed at the end of July 2005).

The Minister of Treasury objected to the proposed merger, referring to the privatisation agreement. The announcement from MSP of 23 December 2005 stated: "The Minister of the Treasury sent a letter to Mr. Alessandro Profumo, the CEO of UniCredito Group (strategic investor in Pekao S.A.) requesting that

216 Results of the analysis of the corporate banking market are specified in points (68) - (72) of the Commission Decision.

217 Results of the analysis of other market segments are specified in points (73) - (83) of the Commission Decision.

218 Point (85) of the Commission Decision.

219 These powers were transferred to the Polish Financial Supervision Authority as of 1 January 2008.

a state consistent with the provisions of the Pekao S.A. privatisation agreement be restored within one month. UniCredito Group committed in the agreement not to invest, including investing through other entities, in shares of companies which compete against Pekao S.A. in Poland. BPH is a company which competes against Pekao S.A."[220]

The position of UniCredit with regard to the interpretation of the provisions of the privatisation agreement was significantly different from the Minister's. The clause that had raised doubts was aimed to protect Pekao against competition from UniCredit in Poland, and thus not to weaken this bank. Meanwhile, the merger with Bank BPH SA would mean strengthening, not weakening Pekao; besides, the clause had lost its validity after Poland's accession to the European Union.

In January 2006, after the period of one month specified in the letter to UniCredit had expired, the Ministry of Treasury sent UCI a final written request "that a state consistent with the provisions of the Pekao S.A. privatisation agreement be restored" by means of sale of all shares of Bank BPH SA within the period of three months. Simultaneously, at the beginning of February 2006, the Minister of Treasury filed a complaint with the European Court of Justice claiming that the Commission, when assessing the effect of the merger on the situation in Poland, wrongly defined some product markets and the impact of the transaction on the state of competition. In official announcements and discussions in the media, politicians of the ruling coalition and government officials who spoke out against the merger highlighted predominantly the fact that, as a result of the merger, the state-controlled PKO BP bank would lose its position as a leader, market concentration would increase and, as a consequence, competition would be weaker.

How would the actual concentration ratios have shaped? After the merger, the market share of the five largest banks would have gone up five percentage points and would have reached 54 percent. That meant that it still would have been below the European average. In some EU states, the share of the three largest banks was much bigger at that time (almost 60 percent in Portugal and the Czech Republic). It is worth adding that on the most concentrated markets, i.e.

220 An announcement by the Spokesperson for the Minister of Treasury published on the Ministry's website on 23 December 2005.

in the Netherlands, Belgium and Finland, the share of the five largest banks exceeded 80 percent.

The business project of merging two banks that had the same majority shareholder as a result of a transnational merger, became the subject of a heated debate in Poland, which focused around interpretations of the national interest. The questioning of the appropriateness of the 1990s privatisation processes in the Polish banking sector started once again. The corollary of the political storm was the parliamentary "banking" inquiry commission, set up by *Sejm* in March 2006. A judgement of the Polish Constitutional Tribunal put an end to it in the autumn of 2006. Those who keep a close eye on the public life surely remember the heat and tension of those days; rational arguments would not reach the public without difficulty.

It was in such a climate that the dispute between the Polish government and the European Commission began. The Commission was represented by Neelie Kroes, European Commissioner for Competition, and Charlie McCreevy, European Commissioner for the Internal Market and Services. The Directorate General for Competition accused Poland of a breach of Article 26 of the Treaty establishing the European Community ("EC Treaty"), which granted the Commission the exclusive right to decide on mergers and takeovers in the EU. Commissioner McCreevy accused the Polish government of a breach of Article 43 of the EC Treaty, which guarantees the freedom of establishment and Article 56, which guarantees the freedom of capital movements between EU States. According to the European Commission experts, the disputed clause in the privatisation agreement cited by the Polish government, lost its legal validity on the day of Poland's accession to the European Union due to its incompatibility with the EC Treaty.

Thus, Poland was facing two procedures: one before the European Court of Justice initiated by Charlie McCreevy, European Commissioner for the Internal Market and Services, for a breach of the principle of freedom of capital movements, and the other, before a Polish court, as a result of an action taken by European Commissioner Neelie Kroes for obstructing the Commission's competition policy decision. The Polish application to the Court against the decision of the European Commission did not stand much chance, especially that Poland had not made use of the opportunity to influence the Commission's decision envisaged in the relevant procedures, i.e. the right of each party concerned to submit comments within 10 working days of the publication of the information on the notification of a proposed merger in the Official Journal of the European Union[221], and the right to request, within 15 working days of the date of receipt of the copy of the notification, that part of the case be referred to the competent authority of the Member State[222], along with the right to appeal against the decision within two months. In the end, the European Court of Justice did not pronounce a judgment in the case. Although as far as the key issue raised by the Minister of Treasury was concerned, i.e. a breach of the provisions of the privatisation agreement, the parties (MSP and UniCredit) held to their positions, it became clear over the next few weeks that to wait for the dispute to be resolved in court would be, from the business point of view, a waste of valuable time.

In the second half of March 2006, negotiations began with the aim of resolving the dispute. The result was an agreement between MSP and UCI signed on 19 April 2006. Two weeks earlier, on 5 April, when the agreement was initialled, the Commission for Banking Supervision issued a clearance for UniCredit to execute its voting rights following from the shares of Bank BPH S.A it possessed. The agreement was hedged with many obligations for UCI, concerning both the policy to be applied towards Bank BPH SA until it merges with Bank Pekao S.A., as well as the policy to be implemented towards the bank which was to emerge as a result of the merger. The method of carrying out the transaction was specified in a secret agreement between MSP and UniCredit.

The government considered the agreement with UniCredit to be its great success. After it had been initialled, MSP informed in its announcement of 5 April 2006 that "the agreement will guarantee that Bank BPH SA remains an independent market player. UniCredit will sell 200 branches and related banking services operating under the BPH brand to an independent third party through an international, competitive and transparent process. Unsold assets will be incorporated to Pekao." The announcement also stated that "the agreement resolves all disputes concerning privatisation agreements between UniCredit and MSP."[223]

The method of the merger was made dependent on amending the Banking Act, within six months of signing the agreement, so that it would provide

221 Point (4) of the previous notification of a proposed merger (COMP/M.3894 – UniCredito/HVB), published in the Official Journal of the European Union of 23 September 2005.

222 Article (9) of the Regulation.

223 An announcement by the Spokesperson for the Minister of Treasury published on the Ministry's website on 5 April 2006.

for the possibility to divide a bank operating as a joint-stock company. The amendments were passed under extraordinary (urgent) procedure. They came into force on 19 October 2006, leading to the merger being carried out after a prior division of Bank BPH SA under Article 529(1)(4) of the Commercial Companies Code, i.e. through the spin-off and transfer of separated assets to Bank Pekao S.A. If the amendments had not been passed, and if they had not entered into force on time, first, the two banks would have merged, and then a "mini-BPH" would have been offered for sale to an independent investor.

The National Bank of Poland (NBP) and the Polish Bank Association (ZBP) expressed objections to introducing the possibility to divide banks during the legislative works on the amendments to the Banking Act. In the view of both institutions, allowing such divisions could potentially open up the possibility for banks registered in the EU to freely divide their companies in Poland and transfer the most valuable assets to their own branches, which would not be subject to Polish banking supervision. As a consequence, the national system of deposit guarantees would have to provide protection for depositors of banks whose best quality assets had been cut off.[224]

It is hard to evaluate in practice to what extent the risk against which NBP had warned was real. Lawyers are of the opinion that it is not in every case that dividing a nationwide bank and transferring part of its assets to a credit institution would be possible, in the light of both EU regulations and the regulations of individual Member States.[225]

In the context of the experiences following from the merger of Bank Pekao S.A. and the separated part of Bank BPH SA, one may conclude that dividing banks does pose a serious risk: the risk of affecting consumer interests. It is linked with the risk of breaching bank secrecy and data protection regulations. It is not always possible to smoothly combine meeting the procedural requirements set forth by the law and providing customers with information in due time. The National Bank of Poland pointed this out during the legislative process. In his speech, J. Pruski, First Vice President of NBP, stated: "In the assessment of NBP, the draft

224 An address by J. Pruski, NBP First Vice-President, and K. Pietraszkiewicz, ZBP President during a session of the Sejm Commission for Public Finance, Biuletyn Biura Komisji Sejmowych No. 1153/V/V, and an address by J. Pruski during a plenary sitting of the Sejm on 17 October 2006.

225 R. Zdzieborski, *Podział transgraniczny banku krajowego działającego w formie spółki akcyjnej - zagadnienia wybrane*, Prawo Bankowe No. 12 (112), December 2006.

requires a comprehensive analysis as regards the conditions ensuring that a bank which is to be divided will keep the legally protected secrets, in particular bank secrets, comprising information about bank customers. Such analysis should be carried out with regard to the actual possibility of completing all the stages of the procedure of dividing a bank under the Commercial Companies Code while complying with the obligation to keep the secrecy of legally protected information."[226]

We knew when we began the preparations for the transaction that the operation would be difficult. Although Bank Pekao S.A. had some experience from the 1998 merger with three regional commercial banks, which had become part of Pekao S.A. Group two years earlier, those experiences could be used only to some extent, since the two processes were fundamentally different from each other. The 1996 decision to establish Pekao S.A. Group was administrative in character; it was taken as part of the implementation of a government privatisation programme and consolidation of the banking sector. Not only had the merger of the four banks already been cleared, but even had a "patronage" of state authorities and was the first, pioneer attempt to carry out a large-scale consolidation in the Polish banking sector. At that time, the lack of unified operation base was a serious risk factor. Four different IT systems had been operating in the four banks, the advancement of the technologies was different as well and their hardware platforms were dissimilar. For the business priorities of the integration to be feasible, it was necessary to build an integrated telecommunications network, which would provide customers with access to a unified offer through the combined distribution networks. Despite the complexity and the scale of the process, the operation was a success. Beginning from 1 January 1999, four, until then independent, banks started operations as one: the new Bank Pekao S.A.

In the case of the envisaged transaction, carried out as a consequence of a transnational merger approved by the European Commission, the intention of both banks' majority shareholder encountered a strong opposition on behalf of the Polish government, and the merger was completed owing to a compromise, as a result of which the Banking Act was amended for this particular case, allowing to divide banks operating as joint stock companies under the procedure specified in the Commercial Companies Code. Using the example of this transaction, it can be concluded with full responsibility that deviating from the traditional

226 An address by J. Pruski, NBP First Vice-President during a plenary sitting of the Sejm on 17 October 2006.

model of conditional merger (merger followed by the sale of selected assets in order to limit market concentration) and adopting the divide then merge formula resulted in a multiplication of legal risks, operational risk, and the complexity of the process itself, as well as a significant increase of the costs.

Due to the data protection regulations in force, in particular the provisions of the Banking Act concerning bank secrecy, the operational integration, i.e. the data migration from BPH computer systems to Pekao systems could not begin before the day of the legal division of Bank BPH SA. The process had to take into account all sorts of legal problems and complex technological determinants. In order to effectively carry out the migration of data from BPH's computer systems to those of Pekao and to limit the legal and operational risks, both banks concluded a general agreement specifying the rules of cooperation and the division of responsibility.

To limit the risk and ensure uninterrupted service not only for customers being transferred from Bank BPH SA but also for the millions of existing Pekao customers, the migration was carried out as a roll-out, i.e. through a gradual (in groups of branches) transfer of customer data and their accounts from BPH's systems to Pekao's systems. The transfer of information was designed in a way that would ensure stability and a high quality of operations of the IT environment of both banks.

For the operational integration to be appropriately prepared and completed, it was critical that to lay down the rules of the banks' cooperation in the transition period, i.e. from the day of the registration of the division of Bank BPH SA in court (legal merger) until the end of the transfer, as during that period the customers who were being transferred were handled with the use of the operational platform of BPH.

Under the general agreement, the banks had undertaken to provide specified services to each other within the scope of their activity. These issues were later specified in detailed outsourcing contracts, including contracts on providing IT support services, on providing customer service operations, on providing data archive storage and access services, on providing data access services for reporting purposes. Conducting the operation in a way that would be safe and compliant with the regulations required also the introduction of a system of protection so that, under the outsourcing contracts, the access of employees to customer data from the other bank would be made possible without breaching bank secrecy regulations. Special controlling teams were set up in both companies and scrutiny procedures adopted to ensure that IT systems were used properly and in compliance with the contracts concluded, and that the application of the systems was properly supervised.

Restrictions resulting from the need to obey bank secrecy regulations had a direct impact on the methods of communicating with the clients of the branches that were being taken over. Dividing Bank BPH SA by spinning-off part of its assets under Article 529(1)(4) of the Commercial Companies Code meant that by taking over the separated part of the assets, based on general legal succession, Bank Pekao S.A. took over the rights and obligations of Bank BPH S.A. which were assigned to it under the Spin-off Plan. Therefore, there was no need to transfer individual assets and individual obligations and to get the creditors' consent for the change of the debtor. With respect to the agreements concluded with the customers and business partners, this meant that on the day of the spin-off, from the legal point of view, only a change of a contracting party took place: Bank Pekao S.A. replaced Bank BPH S.A.

Due to legal restrictions, Bank Pekao gained access to the database of transferred clients and access to the agreements concluded with them only after the spin-off had been registered, because only then did it have the right to obtain information protected by bank secrecy. It was only then that we could start communicating with transferred customers individually. Prior to that, meticulously planned information activities had been carried out, first with information about the intended integration of the banks, then about the development of the integration process, being communicated to the public in the form of updates published in the press and other media, as well as during quarterly press conferences. As it was impossible to reach the transferred customers directly before the day of the spin-off, letters containing content agreed on by both banks were signed and distributed by Bank BPH S.A.

During the whole process, we took the utmost care to ensure that the integration, both on the formal and the operational platform, would progress in compliance with the relevant regulations, in a transparent way, respecting the rights and interests of customers. The process was accompanied by continuously strong interest of the media looking for hot topics and often exaggerating instances of errors. Considering the complexity of the process, resulting mostly from legal aspects, those errors constituted acceptable operational risk, and their scale, considering the size of the operations, was relatively small.

This was confirmed in the explanatory investigation, initiated in April 2008 by the Office of Competition and Consumer Protection (UOKiK). UOKiK's announcement of 21 April 2008 stated that "It transpires from the complaints filed with the Office that there might have been a case of providing unreliable information to existing customers of Bank BPH S.A. about the consequences of the ongoing transaction and their transfer to Bank Pekao S.A.". Having completed the investigation, UOKiK announced on 3 November 2008 that "on the basis of the evidence collected, the President of the Office found no irregularities taking place in the course of the merger of the two financial institutions that would justify instituting proceedings concerning an infringement of collective consumer interest".

The transaction showed that not every joint stock company may be subjected to the same transformations. A bank is an institution of public trust, its customers being specially protected under the law. You cannot put banks in one line with other companies arguing that they can be treated in the same way as steelworks, airlines or construction companies, as the authors of the amendments to the Banking Act did.

The risk of breaching the law when dividing and merging banks is high. It was only owing to an incredibly accurately planned and carried out process that we managed to avoid many problems which could lead to a complete failure of the operation and an infringement of customer interests on a great scale. One can speak of a big success, even more so because we could not support ourselves with anybody's experience, nor test the designed solutions in advance. One can only hope that it was the first, and at the same time the last operation of this kind on the Polish market. Apart from arguments voiced three years ago against introducing the described amendments to the Banking Act, also the experiences gained during the merger of Bank Pekao S.A. and a separated part of Bank BPH S.A. proves that the possibility to divide banks should be ruled out and the legal status existing before 19 October 2006 be restored.

*Jacques Bourgeois and Cormac O'Daly**

HARD TIMES: EMPLOYMENT ISSUES IN EU MERGER CONTROL

1. INTRODUCTION

This contribution aims to highlight a somewhat neglected area of study in EU merger control, namely the reference in the EC Merger Regulation (the "Merger Regulation") to the fundamental objectives of the Treaty establishing the European Community ("EC") and the Treaty on European Union.[227] One of these fundamental objectives is a high level of employment, yet the Commission's decisional practice has not openly squared this objective with what it considers to be a purely competition-based test for assessing a transaction's legality. Nor are we aware of extensive scholarly research on this issue, at least in the areas of mergers; the interaction of competition and other EU policy objectives has been studied.[228]

The orthodox view of EU merger control is that the Commission must base its assessment of whether a merger is compatible with the internal market on exclusively competition grounds.[229] Nonetheless, since its entry into force, the Merger Regulation has also contained the references to other goals pursued by the European Community. Rejecting these goals' relevance in the Commission's analysis of mergers, Sir Leon Brittan, the Competition Commissioner at the time of the introduction of the Merger Regulation, wrote as follows:

> *"Furthermore, the [Merger] Regulation provides a series of factors of which the Commission shall take account in making its analysis. The interplay between these various factors and between them and the dominant position test itself has already*

* The views expressed are personal to the authors who bear sole responsibility for errors.

227 The subject was raised at the Commission and IBA's jointly hosted conference on the reform of the EU's merger control system in 2003. See: Loughran, Competition Policy Newsletter, Number 1-Spring 2003, at page 81. The subject has also arisen in European Parliament resolutions – see, for example http://www.europarl.europa.eu regarding the ABB-Alstom merger.

228 For background, see, for example, Ehlermann and Laudati ed., European Competition Law Annual 1997: The Objectives of Competition Policy, Hart Publishing, 1998; Mische, Nicht-wettbewerbliche Faktoren in der europäischen Fusionskontrolle, Nomos Verlagsgesellschaft, 2002.

229 This of course assumes that these grounds can be identified and are not themselves controversial. While beyond the compass of this paper, this is not necessarily straightforward with, for example, conflicting views on what competition policy ought itself to be.

> *given rise to comment.* ***Let there be no doubt: the fundamental analysis to be carried out by the Commission is whether the merger impedes competition.*** *(…) In other words, as is always the case in competition policy our concern will be whether the merged entity could raise prices, discriminate unfairly or restrict output with impunity or in a way which would not be possible in normal competitive conditions. The factors listed in Article 2 of the Regulation provide assistance to the Commission in making that analysis."*[230] (emphasis added)

Following this theme, a leading textbook also states, "EU merger control is based on purely competition criteria to the exclusion of social or industrial policy considerations".[231]

Thus there would appear to be a dichotomy between competition considerations, on the one hand, and social and industrial ones on the other. Moreover, this dichotomy reportedly was a reason for the – eventually successful – move to have Article 3(g) EC removed by the Treaty of Lisbon.[232]

This contribution challenges whether such a clear delineation can be made between competition and "other" factors in merger analysis. We maintain that given the wording of the EU's founding treaties and the Merger Regulation, the Commission cannot simply – at least – ostensibly ignore the relevance of such other factors. Analysis of such other factors may, we recognize, be difficult to accommodate in the Commission's current framework and procedure for assessing mergers but this alone should not prevent their being analysed in appropriate cases. What constitutes an appropriate case is, of course, a different – and difficult – question as is the level of impact on employment that the Commission would be expected to take into account. The answer to these questions is beyond the scope of this paper. But we would submit that the number of cases in which the Commission would have to take account of employment issues will be very few and exceptional, although in the current political and economic climate, the issue may arise more than it has in the past.

230 Sir Leon Brittan, QC, "The Law and Policy of Merger Control in the EEC", 15 EL Rev, (1990) 351, at page 352.

231 EU Competition Law, Volume II, Mergers and Acquisitions, Drauz and Jones ed., Claeys and Casteels, 2006, at page 262; See also Immenga/Körber in Immenga/Mestmäcker ed., EG-Wettbewerbsrecht, Verlag C. H. Beck, 2007, Art. 2 (1) of Regulation 139/2004, para. 211.

232 See EU deal drops 'free competition' at http://news.bbc.co.uk/2/hi/business/6229300.stm, reporting on tensions between social and competition objectives in intergovernmental discussions on The Treaty of Lisbon.

We begin by examining the relevant provisions of the Treaty establishing the European Community and the Treaty on European Union. Then we comment briefly on how employment and other non-competition goals have influenced the interpretation of what is now Article 101 of the Treaty on the Functioning of the European Union (TFEU). Turning more specifically to mergers, Section 4 examines the text of the Merger Regulation, Section 5 comments on the only time this issue has reached the European Courts before we wrap up our conclusions in Section 6.

2. THE TREATY PROVISIONS

While the main provisions on competition law were in Articles 81 to 86 EC, other articles of the Treaty establishing the European Community must also be recalled.[233]

Article 2 EC provided as follows:

> "*The Community shall have as its task, by establishing a common market and an economic and monetary union and by implementing common policies or activities referred to in Articles 3 and 4, to promote throughout the Community a harmonious, balanced and sustainable development of economic activities, a high level of employment and of social protection, equality between men and women, sustainable and non-inflationary growth, a high degree of competitiveness and convergence of economic performance, a high level of protection and improvement of the quality of the environment, the raising of the standard of living and quality of life, and economic and social cohesion and solidarity among Member States.*"

The aforementioned Article 3(g) stated that "the activities of the Community" shall include "a system ensuring that competition in the internal market is not distorted". The Treaty of Lisbon deletes Article 3(g). The Protocol on the Internal Market and Competition, however, provides that the internal market "includes a system ensuring that competition is not distorted". Overall, although this has been debated, the Treaty of Lisbon's entry into force does not therefore change the central role of competition policy in the EU.[234]

233 This section mainly refers to the treaties pre their amendment by the Treaty of Lisbon. This retrospective review of the EU's founding treaties is necessary as these are the versions of the treaties referred to in the Merger Regulation.

234 See comments of the former Director General of the Legal Service of the European Commission, Michel Petite, in "La place du droit de la concurrence dans le futur ordre juridique communautaire", in Concurrences N°1 – 2008, at page 17.

Article 3(i) EC also numbered among the Community's activities "the promotion of coordination between employment policies of the Member States with a view to enhancing their effectiveness by developing a coordinated strategy for employment".

Employment was the subject of a separate title in the Treaty. While the relevant articles did not grant the Community substantive legislative powers in this area, Article 127(2) EC stipulated that "The objective of a high level of employment shall be taken into consideration in the formulation and implementation of Community policies and activities".

Article 2 of the Treaty on European Union also referred to promoting a "high level of employment".

The Treaty of Lisbon amends some of these provisions. The aim of having a high level (or even "full") employment is, however, retained in Articles 3(2), 5(2) and 9, and Titles IX and X of the TFEU and in Article 3(3) of the Treaty on European Union.

While the EU does not have the same competences in the area of employment as in other fields – such as competition – it does set itself the goal of a high level of employment as one of its aims and, under Article 147(2) TFEU, this objective must always be taken into account, whenever the EU is implementing its policies and activities. Given all of this, it is difficult to conclude that any area of EU policy, including merger control, can be oblivious to the consequences of a decision, or other act, on employment.

3. ARTICLE 101 TFEU (FORMERLY ARTICLE 81 EC)

Before examining mergers specifically, it should be recalled that the relevance of employment, and other interests referred to in what have been termed the "policy-linking clauses",[235] in the Treaty have been considered quite extensively under Article 101 TFEU.

235 See C. Townley, "Is Anything more Important than Consumer Welfare (in Article 81 EC)?: reflections of a Community lawyer", (2007-2008) 10 Cambridge Yearbook of European Legal Studies 345, at page 352. This article reviews alternative analytical methods that the Commission and Courts have deployed when taking account of non-competition objectives under Article 81 EC. See also, by the same author, Article 81 EC and Public Policy, Hart Publishing, 2009. In addition, see Monti, "Article 81 EC and Public Policy", CML Rev 39, 1057, which provides a comprehensive review of cases in which the Commission had taken public policy considerations into account under Article 81 EC. Written when discussions regarding the decentralization of Article 81(3) EC were taking place, the author advocates redrafting Article 81(3) EC and inserting an Article 81(4) to make the granting of an exemption from Article 81(1) EC more justiciable, see page 1099.

Article 101 TFEU's bifurcated structure traditionally has involved a balancing exercise under which *prima facie* restrictions on competition under Article 101(1) TFEU are examined to see if they qualify for an exemption or exception under Article 101(3) TFEU. The Commission's *Guidelines on the Application of Article 81(3) [now 101(3)] of the Treaty* specify that, while Article 101(3)'s four conditions are both cumulative and exhaustive, "Goals pursued by other Treaty provisions can be taken into account to the extent that they can be subsumed under the four conditions of Article 81(3)".[236] Even though the Guidelines recognize that other Treaty objectives may be relevant to the availability of an exception under Article 101(3) TFEU, they consider that this will only occur in exceptional cases.

On a number of prominent occasions the Commission, or Courts, have ruled that what would be regarded as non-competition considerations, are relevant in deciding whether or not a practice infringes Article 101 TFEU. Sometimes this has been done by finding that an agreement does not fall within Article 101(1); other times the agreement has been found to satisfy the conditions of Article 101(3).[237]

As early as in 1977, in *Metro I*, when the European Court of Justice was considering the legality of a selective distribution system, it stated that "(…) the establishment of supply forecasts for a reasonable period constitutes a stabilizing factor with regard to the provision of employment which, since it improves the general conditions of production, especially when market conditions are unfavourable, comes within the framework of the objectives to which reference may be had pursuant to Article 85(3)".[238]

In *Metro II*, the same court considered the importance of "safeguarding of objectives of a different nature" to competition and stated that provided any restrictions on competition were proportionate to the attainment of these different objectives, account could be taken thereof under Article 85(3) EC".[239]

236 Guidelines on the application of Article 81(3) of the Treaty, [2004] OJ C 101/97, 27.4.2004, at paragraph 42. This may be an overly narrow reading of Article 81(3) EC – see Bourgeois and Bocken, "Guidelines on the Application of Article 81(3) of the EC Treaty or How to Restrict a Restriction", Legal Issues of Economic Integration, Kluwer Law International 2005, Vol. 32, Issue 2, 111, at page 120.

237 For other prominent examples, see cases such as Laurent Piau, COMP/37.124 and Case C-519/04P, Meca-Medina v Commission, [2006] ECR I-6991 concerning taking account of regulations regarding sport as a wider social good to be considered under Article 101 TFEU and Townley and Monti supra.

238 Case 26/76, Metro SB v Commission, [1977] ECR 1875, at paragraph 43.

239 Case 75/84, Metro SB v Commission, [1986] ECR 3021, at paragraph 65.

More recently in *Wouters*, a preliminary reference from a Dutch Court, the Court of Justice found that Dutch bar rules that prohibited interdisciplinary partnerships did not infringe Article 101(1) TFEU when their positive effects – such as providing guarantees of integrity and experience to consumers of legal services – were balanced against the negative and anti-competitive effect of being "liable to limit production and technical development".[240] For the Court the "overall context" of the bar association's decision and its objectives had to be taken into account and the "consequential effects restrictive of competition [were] inherent in the pursuit of those objectives".[241]

As for the Commission, among other cases, it has taken wider social reasons into account under Article 101(3) TFEU when considering agreed output restrictions in so-called "crisis cartels" (i.e. when an industry is experiencing particularly difficulty times).[242]

Thus there is little doubt that – at least on some occasions – non-competition goals have influenced the interpretation of Article 101 TFEU. Whether there should be any difference for merger review might, in the first place, depend on the text of the Merger Regulation, to which we now turn.

4. THE EC MERGER REGULATION

The substantive test for the compatibility of a merger with the internal market is in Articles 2(2) and 2(3) of Regulation 139/2004, which stipulate that the Commission must authorize transactions unless they "significantly impede effective competition in the common market or in a substantial part of it" (the SIEC test). On the face of it, this establishes a wholly competition-based test but other parts of the Merger Regulation are, at the least, more ambiguous on this point.

Recital 4, for example, provides that corporate reorganizations "are to be welcomed to the extent that they are (…) capable of (…) improving the conditions of growth and raising the standard of living in the Community". More significantly perhaps,

240 Case C-309/99, Wouters v Algemene Raad van de Nederlandsche Orde van Advocaten, [2002] ECR I-1577.

241 At paragraph 97. For a discussion, see Whish, Competition Law, 6th ed., Oxford 2009 at page 126 et seq.

242 See, for example, Motta, Competition Policy Theory and Practice, Cambridge University Press, 2004 at page 15 and Roth and Rose ed., Bellamy and Child European Community Law of Competition, 6th ed., Oxford 2008 at page 338. See by analogy Case 240/83, Association de défense des brûleurs d'huiles usagées, [1985] ECR 531, at paragraph 12 where the Court of Justice stated that the principle of freedom of trade is "subject to certain limits justified by the objectives of general interest pursued by the Community provided that the rights in question are not substantively impaired".

Recital 23 states that the Commission "must place its appraisal [of a merger's compatibility with the internal market] within the general framework of the achievement of the fundamental objectives referred to in Article 2 of the Treaty establishing the European Community and Article 2 of the Treaty on European Union". Recital 45 states that "This Regulation in no way detracts from the collective rights of employees, as recognized in the undertakings concerned, notably with regard to any obligation to inform or consult their recognized representatives under Community and national law". Article 18(4) accordingly provides that, *inter alia*, recognized representatives of employees have a right to be heard if the Commission holds a hearing as part of its investigation into a merger's legality. Unless the Commission is supposed to take these views into account later in its merger analysis, it is difficult to see what purpose this article would serve.

Most significantly, the very text of Article 2(1) states that the Commission is to appraise transactions both "in accordance with the objectives of this Regulation" and with "the following provisions", which include Article 2(2) and 2(3)'s SIEC test. So while Articles 2(2) and 2(3) set out what appears to be a pure competition-based test, and while these articles are phrased in mandatory terms ("shall be declared (...)"), the Commission is also bound, under Article 2(1), to take account of the Regulation's objectives, which, given the mention there of in the recitals, also include the objectives of Article 2 of both the Treaty establishing the European Community and the Treaty on European Union. Therefore, under the very text of the Merger Regulation, read in harmony with the founding treaties, employment is a factor that the Commission it seems must consider when analyzing a merger's legality under EU law.

5. CASE LAW – VITTEL AND PIERVAL

The recitals and articles of the Merger Regulation discussed in the preceding section were central to two substantively identical cases before the European Court of First Instance. Both the *Comité Central d'Entreprise de la Société Anonyme Vittel*[243] and *Comité Central d'Entreprise de la Société Générale des Grandes Sources*[244] cases concerned trade union challenges to the Commission's clearance of the *Nestlé/ Perrier* merger. The Commission's decision was subject to a number of conditions including the divestment of certain plants and brands. The trade unions argued

243 Case T-12/93, Comité Central d'Entreprise de la Société Anonyme Vittel and others v Commission, [1995] ECR II-2147.

244 Case T-96/92, Comité Central d'Entreprise de la Société Générale des Grandes Sources and others v Commission, [1995] ECR II-1213.

that the Commission had failed to consult them properly and thereby violated the Merger Regulation by failing to take employees' rights into consideration.

The Commission argued that former Recital 13 (now Recital 23 but its text has been amended somewhat) did not impose any obligation to examine a merger's impact on employment. The Court, while ultimately holding that the applicants only had *locus standi* to challenge respect of their procedural guarantees during the administrative procedure, did not agree and stated as follows:

> "*(…) the primacy given to the establishment of a system of free competition may in certain cases be reconciled, in the context of the assessment of whether a concentration is compatible with the common market, with the taking into consideration of the social effects of that operation if they are liable to affect adversely the social objectives referred to in Article 2 of the Treaty.* The Commission may therefore have to *ascertain whether the concentration is liable to have consequences, even if only indirectly, for the position of the employees in the undertakings in question, such as to affect the level or conditions of employment in the Community or a substantial part of it.*"[245] (emphasis added)

The Court continued that "Article 2(1)(b) of Regulation No 4064/89 requires the Commission to draw up an *economic balance for the concentration in question*, which *may, in some circumstances, entail considerations of a social nature*" (emphasis added).[246] In the Court's view, the then 13th recital confirmed this conclusion – that the "Commission may therefore have to" take account of impact on employment – as did Article 18(4), which "manifests an intention to ensure that the collective interests of those employees are taken into consideration in the administrative procedure".[247]

As to when the entitlement to take account of wider objectives might arise, the Court stated this would happen "in certain cases" but provided no greater detail than that this could occur if the proposed merger was "to affect adversely the social objectives referred to in Article 2 of the Treaty" or "such as to affect the level or conditions of employment in the Community or a substantial part of it". Perhaps realizing the enormous sensitivity of the potential intrusion of wider policy issues into merger control, the Court did not go further. Arnull therefore comments on the judgments as follows:

245 Case T-12/93, paragraph 38.
246 Case T-12/93, paragraph 39.
247 *Ibid.*

"The CFI does not specify when it will be appropriate for the Commission to take into account the social effects of a concentration. Its rulings allow the policy pursued by the Commission to be influenced by the political complexion of the Commissioner responsible for competition and that of the college of Commissioners. Such an outcome is hardly conducive to the legal certainty which undertakings are entitled to expect."[248]

We could not but concur that if merger control is to involve consideration of wider policy goals, these ought to be set out in a transparent manner to provide legal certainty to merging companies. Moreover, one fears that the Commission already sometimes takes account of other policy considerations, which exacerbates the sense of lack of legal certainty. The reality is that whatever DG COMP's approach to transactions, the most controversial merger decisions are ultimately debated, discussed and adopted by the college of Commissioners (or if not by the college of Commissioners itself, at least by members of the Commissioners' cabinets or private offices), which may be more open to considering wider non-competition objectives.[249] As has been noted, "Despite regular official protestations to the contrary, it is apparent that broader social and economic issues such as employment, "national champions" and other industrial policy factors influence the final Commission decision in some cases, although it is admittedly difficult to assess to what extent such factors are outcome determinative and in which cases".[250]

This all said, it would be wrong to consider that even pure competition-policy based merger assessment has always proved entirely predictable. Cook and Kerse, for example, caution that "[I]t has to be recognized that many of the key factors in the appraisal decision are incapable of precise measurement or prediction and there may be not one but many finely balanced judgments to be made in carrying out the appraisal process before reaching a final decision".[251] Nonetheless, through the increased number of published decisions, the greater experience

248 Arnull, Case Law, CML Rev. 33 (1996), 319, at page 328.

249 For discussion on this, see Jones and Sufrin, EC Competition Law Text, Cases and Materials, 2nd ed., Oxford, 2004, at page 975 where the authors speculate that other policies may have been central to the Commission's decisions in, among other cases, Aérospatiale-Alenia/de Havilland, MSG/Media Services GmbH and Mannesmann/Vallourec/Ilva.

250 Hawk and Huser, European Community merger control: a practitioner's guide, Kluwer Law International, 1996, at page 213. The authors speculate that the Commission's clearance in the Kali+Salz case was at least partly motivated by employment issues. See also Völcker in Immenga/Mestmäcker ed., EG-Wettbewerbsrecht,. Verlag C. H. Beck, 2007, Internationales Wettbewerbsrecht, Wettbewerbsrecht und seine internationale Durchsetzung: Kartellbehörden in Drittstaaten und ihre Beziehungen zur EG-Kommission am Beispiel des EG-US-Kartellrechtsabkommens, paragraph 40.

251 Cook and Kerse, EC Merger Control, 4th ed. Sweet & Maxwell, 2005, at page 270.

of regulators and external counsel, the publication of guidance documents and notices, legal certainty in mergers is steadily improving. Similar steps, such as the publication of a Commission Notice concerning when employment might be considered as a factor in merger analysis, could be envisaged to clarify the role of other policy objectives in merger control.

6. CONCLUSION

This contribution does not call for impact on employment to become central to the Commission's merger control analysis. Used incorrectly, it could be a cloak for protectionism, preservation of the *status quo* and ultimately deny consumers the benefits of innovation and dynamic market evolution. Defending competition has served Europe well as the primary goal of EU merger control. As former Director General at DG Competition, Alexander Schaub has cautioned, competition policy should not be "burdened with too long a list of objectives".[252] The same goes for merger control.

This contribution's modest aim was to demonstrate that the Commission cannot dismiss the relevance of a transaction's impact on employment in all cases. To do this runs counter to the wording of the treaties and the Merger Regulation. We would therefore submit that in cases where, per the Court of Justice in *Vittel*, a deal will have a significant, positive or negative, impact on employment – be this at Member State or exceptionally potentially at Community level – this must be taken into account along with the competition-based arguments. This conclusion should not be regarded as controversial,[253] as Cook and Kerse comment, "[I]t is understandable that when a case is finely balanced, the Commission will look to wider EC objectives recognized in the Recitals to the Regulation".[254]

There may well be a tension between a competition policy perspective and arguments based on the impact on employment. In some cases the Commission, having properly weighed everything up in a transparent manner, may reject the effect on employment in favour of countervailing "pure" competition arguments that promote wider consumer welfare. However, in other decisions, impact on

252 Quoted during a panel discussion at the European University Institute at Fiesole, June 1997 in Ehlermann and Laudati ed., *supra*, at page 9.

253 It would not, moreover, be unusual for non-competition issues to influence merger control. Other legal systems, including some in the EU Member States, permit a government minister to intervene in merger control in the name of defined public policy considerations.

254 Cook and Kerse, *supra*, at page 271.

employment may tip the balance and sway the Commission in one direction or the other.

As indicated in the introduction to this contribution, concluding that a merger's impact on employment should be examined in certain merger cases is but a first step. The precise level of impact that might be considered relevant in the Commission's assessment (one might think of specifying a particular percentage impact) also needs to be analyzed. This raises the question how the transaction's effect on employment might be measured. Here, however, at least some parallels could be drawn from the way in which DG COMP, often with the aid of its Chief Economist's Team, has when appropriate taken account of merger-related synergies. Answers to these questions need to be developed in response to what we have hoped to have shown is the Commission's duty not to ignore the relevance of employment (and indeed other factors) in its merger control review.

Peter Freeman

A VIEW FROM THE COMPETITION COMMISSION ON THE UNITED KINGDOM MERGER PROCEDURE

1. THE UK MERGER CONTROL SYSTEM

In most countries of the European Union, the system of merger control is 'mandatory' in the sense that it requires the pre-notification of qualifying transactions to the relevant competition authorities prior to completion. Usually, the transaction is suspended until clearance has been granted (or remedies agreed). Only after a proposed transaction has been approved, can the merger proceed to completion. There are differences in detail, but that appears to be the general rule.

The UK, however, operates a different system. It does not require mandatory pre-notification and there is no general prohibition on completing a merger which falls under the competition authorities' jurisdiction. This means that in the UK, it is up to the merging companies to choose whether to go ahead with a merger without obtaining a prior approval. This is not to say that such an approach is entirely risk-free for mergers which meet the jurisdictional criteria of the Enterprise Act 2002.[255]

The UK's Office of Fair Trading (OFT) deals with mergers at the initial stage ('Phase I') and it can and will 'call in' those mergers which have not been notified to it but which, on the basis of the available information, look potentially problematic. In any completed merger (or merger which is in the process of being completed) under investigation by the UK competition authorities, interim measures may need to be taken to hold the businesses separate and to prevent any steps or further steps towards integration. This article describes briefly how the UK system works in practice, and discusses its advantages and disadvantages.

255 The Enterprise Act 2002 replaced the Fair Trading Act 1973. It entered into force on 1 April 2003 and is the present legal basis for the assessment of mergers and market in the UK. Section 23 of the Enterprise Act defines a relevant merger situation as cases in which 'two or more enterprises have ceased to be distinct enterprises…' and 'the value of the turnover in the United Kingdom of the enterprise being taken over exceeds £ 70 million' ('turnover test'). Alternatively, the merger qualifies for investigation if the merged entity supplies at least 25 percent of certain goods or services in the UK ('share of supply test').

2. NOTIFICATION OF MERGERS IN THE UK

In the UK, the initial processing and assessment of mergers is carried out by the OFT as the Phase I authority. Cases requiring an in-depth investigation are referred to the Competition Commission (CC) at Phase II. As regards notification, there are three possible types of situations. First, parties voluntarily pre-notify; second, parties notify 'informally' (and either decide to complete or not); third, parties do not notify but complete.

While the UK system does not require pre-notification, it provides for the option of doing so voluntarily. A statutory procedure is laid down in the Enterprise Act. 2002.[256] Once the parties choose to pre-notify, they are no longer able to complete the transaction until the competition authorities have reached their decision.

In the majority of cases, the parties choose the second option and notify under the so-called 'informal' procedure, either voluntarily or in response to an inquiry letter by the OFT. It is then in principle up to them to decide whether to complete the transaction, either before or after they have notified. But this is subject to an important caveat. Once they know about the transaction, competition authorities may require hold-separate measures if they think the transaction is likely to raise competition issues, which will normally prevent the completion of the transaction.

The most difficult cases are often those in which the parties have completed but chosen not to notify. This may either be a deliberate tactic or they may genuinely believe the transaction does not qualify for investigation. In these situations the authorities have to seek the information necessary for an assessment, apply interim measures to safeguard the position for any later ruling, and conduct a proper review of the case.

3. ADVANTAGES OF A VOLUNTARY SYSTEM?

There are several advantages in operating a voluntary system. The main argument for having a voluntary merger regime centres around the perception that it is more 'business-friendly' than a mandatory system. These arguments certainly have something in their favour.

256 Section 96 of the Enterprise Act.

There is a perfectly respectable view that most mergers are benign and do not call for any intervention by the competition authorities. According to this school of thought, it would be wrong to subject all mergers (meeting certain criteria) to prior approval. Even with the most careful choice of criteria, there will be a strong risk of over-policing in that too many mergers that have no realistic prospect of harming competition would be reviewable.

A voluntary system also avoids any unnecessary 'chilling' effect on the economy. Firms can be bought and sold with immediate effect, for example in auction situations, without any delays caused by the need to notify and to obtain clearance.

Another benefit is that the authorities can concentrate their resources on those mergers that truly merit a closer review. It is fair to assume that parties are usually best placed to make their own assessment as to whether a merger is problematic. The 'threat' remains, i.e. the authorities can still 'call in' mergers that have not been notified so the merging parties should have the incentive to conduct a proper self-assessment and take the appropriate action.

4. DIFFICULTIES WITH A VOLUNTARY SYSTEM

Against these advantages, there are some areas of difficulty. First, there is the need to keep businesses separate during the investigation, and second, there are difficulties in making divestments in cases where a significant lessening of competition (SLC) is found.

With anticipated mergers (i.e. mergers come to the authorities' attention as proposals before any steps are taken to complete and integrate the businesses), these difficulties are less. Greater difficulty arises when the merger has already been completed or is in the process of completion. We need to look separately at the position in Phase I and Phase II.[257]

At Phase I, the OFT has to decide whether hold-separate measures are needed and what should be their scope. The problem is that steps may already have been taken to merge the businesses – key personnel may have been dismissed or have left, sales data may have been acquired and plants taken over or closed[258].

257 Note also that, for mergers by acquisition of shares, when a case is referred to the CC, no future shares can be bought; also that for mergers between publicly quoted companies the Stock Exchange Rules require a bid to lapse when a case is sent to the CC.

258 For example in the Stonegate/Dean merger discussed below.

At Phase II the problem is similar but more serious, as integration may have progressed even further. The CC's normal practice is initially to adopt the OFT's interim measures, if applicable, and then shortly afterwards to impose its own measures. The legal basis for this is the need to keep all options open, in the event of an SLC finding by the CC. The CC has wide discretion as confirmed by the relevant appeal body the Competition Appeal Tribunal (CAT) in the *Stericycle* case[259].

All this involves a great deal of time and effort, both for the authorities and the parties and it is not a particularly good use of either. From the authorities' perspective, these resources would much better be devoted to the substantive assessment.

If the final decision is an SLC finding and the remedy is separation of the merged businesses, it is then much more complex and difficult to separate out a viable stand-alone business which will be able to compete effectively from what has been merged together. There are very real and practical problems and a good example of the difficulties which can arise in such cases was the *Stonegate/Dean*[260] merger. The parties were both active in the supply of fresh and processed eggs. The merger would have brought together the two largest UK suppliers of fresh shell eggs and processed eggs. The CC found in its final report that the merger would substantially lessen competition and ordered divestment. In that sense the CC had literally to, 'unscramble the eggs'.

Finally, there is the overall effect of legal uncertainty of a system which allows mergers to proceed without pre-notification, but may nonetheless require them to be dismantled after a period of time. This diminishes the 'business friendliness' of the regime.

259 Stericycle International LLC and Stericycle International Limited v Competition Commission, Judgment of 17 January 2007. This case concerned a completed merger of two clinical waste companies where the CC ordered divestment of part of the acquired business (see CC report, Stericycle International LLC and Sterile Technologies Group Ltd. A report on the completed acquisition of Sterile Technologies Group Ltd by Stericycle International LLC. 12. December 2006).

260 Clifford Kent Holdings Limited and Deans Food Group Limited, A report on the completed merger of Clifford Kent Holding Limited, parent company of Stonegate Farmers Limited, and Deans Foods Limited, 20 April 2007.

5. IS THERE A PROBLEM?

The main issues, as we have seen, relate to dealing with mergers that have been completed. Out of 76 merger cases (4 of which have not yet been reported on) considered by the CC since the new regime took effect in 2003, 31 involved completed mergers. In 18 of the CC's 31 completed merger cases, divestment was required. In all of these cases, considerable resources were expended to deal with the issues raised by completion and the divestment process for those mergers where an SLC was found was more difficult as a result of the completion of the transaction. The time and effort spent in dealing with those problems could probably have been better spent on assessing the merits of the merger.

Then there is the overall risk of damage to competition. Cases of this kind can take up to a year from the start of Phase I to the end of Phase II. This is in itself undesirably long. But in the case of a merger which has already completed before the start of the review process by the competition authorities, it means that for the duration of the examination, the 'acquirer' has removed or at least seriously weakened competition from the 'target'. It also will have made the re-creation of a competitor more difficult, in case of an SLC finding.

The acquirer may have had access to internal business information from the target, possibly also to confidential information relevant to competition. It is possible that these factors may encourage some businesses to pursue a merger as a deliberate anti-competitive strategy, although it is fair to say we have no evidence that this is occurring on a significant scale.

All in all, the voluntary system in the UK has a long history, and much to commend it, but the problems it poses for dealing with completed mergers suggest that there is a case to be made, at least, for a move to a mandatory system and a need for a proper debate.

Nicolas Petit and David Henry

WHY THE EU MERGER REGULATION SHOULD NOT ENJOY A MONOPOLY OVER TACIT COLLUSION

1. INTRODUCTION

In a situation of tacit collusion firms rationally coordinate their commercial policies in such manner that their conduct closely resembles a cartel.[261] Yet, their decision to mimic the others' commercial policy is not the result of any agreement whatsoever. It stems from a range of market-specific features which the market players must accept as a given (oligopolistic market concentration, transparency, barriers to entry, etc.).[262] In European Union ("EU") law parlance, firms involved in a situation of tacit collusion are said to enjoy a "*collective dominant position*".

Over the past two decades, the European Commission ("the Commission") has adopted a stance whereby the implementation of *ex ante*, structural merger rules is deemed more appropriate when seeking to challenge collective dominant positions than *ex post*, behavioural instruments (e.g. on the basis of Article 102 of the Treaty on the Functioning of the EU ("TFEU"). As a result, the EU merger regulation[263] ("EUMR") is the preferred, if not sole, legal tool deployed by the Commission in order to address risks of tacit collusion.[264] Since the entry into force of the EUMR, the number of Commission decisions in which the future emergence of risks of collective dominance was examined lies in the region of 130.[265] In stark

261 The classic model of tacit collusion draws on the idea that in a transparent market where oligopolists compete for market share, each operator contemplating a price cut anticipates that its rivals will immediately follow suit, as a result of which there is no point in decreasing prices in the first place. Rather, operators can follow each other's pricing strategies and, through so-called "*tit for tat*" interactions, progressively increase prices. Any deviation from the common price strategy triggers immediate punishment from the other oligopolists. As a result each and every operator cooperates. This theory can be traced back to the early works of the famous economist CHAMBERLIN in the late 1920s. See E. H. Chamberlin, "Duopoly: Value Where Sellers Are Few", (1929) 44 *Quarterly Journal of Economics*, 63.

262 Yet, a number of authors are challenging the view that tacit collusion may originate simply from the market's structural features. Those authors tend to consider that at a minimum, oligopolists must have recourse to so-called "facilitating practices" to ensure the stability of the tacitly collusive equilibrium. See, for instance, T. Penard, "Collusion et comportements dynamiques en oligopole: une synthèse", mimeo.

263 See Council Regulation (EC) No. 139/2004 of 20 January on the Control of Concentrations Between Undertakings, (2004) OJ L24/1.

264 See in this regard N. Petit, *Oligopoles, collusion tacite et droit communautaire de la concurrence*, Bruylant-LGDJ, Brussels, 2007 and B. Hawk and G. Motta, "Oligopolies and Collective Dominance: A Solution in Search of a Problem", in E. Raffaelli ed., *Antitrust between EC Law and National Law*, Bruylant, 2008, at p. 65.

265 For an exhaustive list of the 127 decisions adopted under the EUMR between 21 September 1990 and 6 June 2006, see N. Petit, id. For recent decisions adopted since June 2006, see, in particular, Case No COMP/M.4601 – *Karstadtquelle/Mytravel*, 04/05/2007; Case No COMP/M.4381 – *JCI/Fiamm*, 10/05/2007; Case No COMP/M.4600 – *TUI/First Choice*, 04/06/2007;

contrast, and despite pronouncements of the General Court ("GC", or the Court) that Article 102 TFEU may apply to tacit collusion, the Commission has not yet taken a single decision enforcing this particular provision against tacitly collusive oligopolies.[266] Similarly, the silence of the 2009 Guidance Communication on Enforcement Priorities[267] on this issue implicitly confirms the Commission's reluctance to rely on abuse of dominance rules to address tacit collusion.[268]

Overall, within the realm of EU competition law, the EUMR can thus be said to enjoy a *de facto* jurisdictional monopoly over collective dominance issues. The present article challenges the conventional view that tacit collusion should be exclusively addressed through the use of the EUMR.[269] To this end, it examines and seeks to set straight five possible misconceptions on which such view seems to be based.

Case No COMP/M.4523 – *Travelport/Worldspan*, 21/08/2007; Case No COMP/M.4781 – *Norddeutsche Affinerie/Cumerio*, 23/01/2008; Case No COMP/M.4854 – *TomTom/Tele Atlas*, 14/05/2008; Case No COMP/M.4513 – *Arjowiggins/ M-real Zanders Reflex*, 04/06/2008; Case No COMP/M.4942 – *Nokia/Navteq*, 02/07/2008; Case No COMP/M.5020 – *Lesaffre / GBI UK*, 11/07/2008; Case No COMP/M.4980 – *ABF/GBI Business*, 23/09/2008; Case No COMP/M.5141 – *KLM/ Martinair*, 17/12/2008; Case No COMP/M.5406 – *IPIC/MAN Ferrostaal AG*, 13/03/2009.

266 See judgment of the GC (formerly CFI), Case T-193/02, 6/01/2005, *Piau v. Commission*, [2005] ECR II-209. There is, however, a "commitments" decision which identified concerns of abuse of collective dominance. See Commission Decision of 26/11/2008 COMP/39.388 *German Electricity Wholesale Market* and COMP/39.389 *German Electricity Balancing Market*. It ought to be noted here that since the judgments of the ECJ in *Dyestuffs* (ECJ, joined cases 89, 104, 114, 116, 117 and 125 to 129/85, *A. Ahlström Osakeyhtiö and others v Commission*, [1988] ECR-5193) and *Woodpulp* (ECJ, Case 48/69, *Imperial Chemical Industries Limited v. Commission* [1972] ECR 619) the possibility of applying Article 101 TFEU to oligopolistic tacit collusion has been removed.

267 See Guidance Communication on the Commission's enforcement Priorities in Applying Article 82 of the EC Treaty to Abusive Exclusionary Conduct by Dominant Undertakings, C(2009) 864 final.

268 See L. Vitzilaiou and C. Lambadarios, "The Slippery Slope of Addressing Collective Dominance under Article 82 EC", *GCP: The Antitrust Chronicle*, October 2009(1), p.10.

269 Many Commission officials, practitioners and scholars support this view: See, for instance, G. Drauz, "Collective Dominance/ Oligopoly Behaviour under Articles 81/82 and the EC Merger Regulation" in B. Hawk (Ed.), (2002) *Fordham Corporate Law Institute*, 380; J. F. Briones Alonso, "Economic Assessment of Oligopolies under the Community EC Merger Regulation", (1996) 3 *European Competition Law Review*, 118, p.119; P. Christensen and V. Rabassa, "The Airtours Decision: Is there a New Commission Approach to Collective Dominance?", (2001) 6 *European Competition Law Review*, 227. Many legal scholars are also supportive of this view. See, for instance, S. Stroux, *US and EC Oligopoly Control*, Kluwer Law International, The Hague, 2004, pp. 3 and 248; V. Korah, "Gencor v. Commission: Collective Dominance", (1999) 6 *European Competition Law Review*, 337, p. 341; R. Whish and B. Sufrin, "Oligopolistic Markets and EC Competition Law", (1992) 12 *Yearbook of European Law*, 59, p. 82.

2. THE EUMR IS MORE APPROPRIATE THAN OTHER LEGAL INSTRUMENTS WHICH ADDRESS COLLECTIVE DOMINANCE CONCERNS THROUGH A PUNITIVE APPROACH

A crucial explanatory factor underlying the exclusive jurisdiction of the EUMR over tacitly collusive oligopolies resides in the premise that the ex post, corrective instruments enshrined in Articles 101 and 102 of the TFEU cannot adequately regulate this area of concern. This is allegedly due to the perceived fact that addressing tacit collusion through the enforcement of Articles 101 and 102 TFEU would entail punishing in an unwarranted manner what constitutes a purely rational course of conduct.[270] Espousing this conventional belief, the Commission has refrained from applying Articles 101 and 102 TFEU on oligopolistic markets and has focused its enforcement resources on preventing the emergence of pro-collusive oligopolies through the careful monitoring of industry consolidation under the EUMR.[271]

On close examination, the view that Articles 101 and 102 TFEU should not be applied to purely rational conduct is, however, puzzling. To the best of our knowledge, the very rationale of Articles 101 and 102 TFEU is to eliminate market failures arising from the rational behaviour of market players. Firms engage in anticompetitive conduct, abusive tying or refusals to deal, for example, because they view such courses of action as rational, profit-maximizing strategies. Moreover, oligopolists that tacitly collude deliberately choose to follow the others' commercial conduct.[272]

Of course, one may legitimately question whether oligopolists should be sanctioned, pursuant to Articles 101 and 102 TFEU, for what constitutes mere rational adaptation to the others' conduct.[273] Whilst, from a common sense

270 See for expressions of this concern B. Carsberg and M. Howe, "Dealing with Abuse of Market Power", in B. Hawk (Ed.), (1993) *Fordham Corporate Law Institute*, 177; R. Whish and B. Sufrin, "Oligopolistic Markets and EC Competition Law", id, p. 75; B. J. Rodger, "Oligopolistic Market Failure: Collective Dominance versus Complex Monopoly", (1995) 16 *European Competition Law Review*, 21, pp. 26 and 29; V. Korah, "Gencor v. Commission: Collective Dominance", id; P. Muñiz, "Increasing Powers and Increasing Uncertainty: Collective Dominance and Pricing Abuses", (2000) 25 *European Law Review*, 645, p. 650; G. Monti, "The Scope of Collective Dominance Under Article 82 EC", (2001) 38(1) *Common Market Law Review*, 131, p. 145 (alluding to a "*tax on market structure*"); B. Hawk and G. Motta, supra note 264, p. 65.

271 In this respect a former DG COMP official coined the maxim that it is "*always better to put care before cure*"- see G. Drauz, "Collective Dominance/Oligopoly Behaviour under Articles 81/82 and the EC Merger Regulation", id. See also, S. Stroux, *US and EC Oligopoly Control*, supra note 269, pp. 3 and 248.

272 See R. Posner, "Oligopoly and the Antitrust Laws: A Suggested Approach", (1969) 21 *Stanford Law Review*, 1562, p. 1575.

273 Some commentators argue that in an oligopoly situation, the very structure of the market itself "requires" undertakings to behave as though they were part of a cartel.

perspective, such question is probably to be answered in the negative, this argument does not eschew the overall applicability of these provisions. In this context, one may for instance think of applying Articles 101 and 102 TFEU on a *no fault* basis, through the recognition that absent a wilful intention to restrict competition, oligopolists should enjoy immunity from fines.[274] In order to correct the market failure, the Commission would nonetheless remain entitled to impose remedies (behavioural or structural), pursuant to Article 7 of Regulation 1/2003, or negotiate commitments pursuant to Article 9 of Regulation 1/2003.[275] The Commission could, for example, draw inspiration from the well-known "*State compulsion doctrine*" (known in the US under the expression "*Act of State defence*") and devise a similar, yet distinct, "*oligopolistic compulsion doctrine*".[276] Since the oligopolists' conduct is dictated by the market's intrinsic structure (and other endogenous features, e.g. transparency) it is submitted that they should not be subject to penalties.[277]

3. THE EUMR ADEQUATELY PREVENTS THE EMERGENCE OF COLLECTIVE DOMINANCE

A second, possible reason in support of the EUMR's jurisdictional monopoly over situations of collective dominance lies in the belief that the Regulation's scope of application is sufficiently extensive as to prevent markets from blossoming into tacitly collusive outcomes.

In our opinion, any such view clearly accords the EUMR too much credit as far as its ability to prevent the appearance of tacitly collusive oligopolies is concerned. The jurisdictional scope of the Regulation, as defined in Articles 1 and 3, only encompasses *external growth* strategies in the form of mergers, acquisitions of control

274 The legal instrument used in the context of setting fines would be the Commission's Guidelines on the method of setting fines imposed pursuant to Article 23(2)(a) of Regulation No 1/2003, (2006) OJ C 210/2. At para. 29, the Guidelines mention negligence as a possible mitigating circumstance for the purpose of setting fines. In addition, the Commission occasionally reduces the amount of the fine when it is faced with companies that have not intentionally infringed the competition rules. See Van Bael & Bellis, *Competition Law of the European Community*, 4th Ed., Kluwer Law International, The Hague, 2005. p. 1116.

275 See Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty, (2003) L1/1.

276 See ECJ, Cases C-350/95 P and C-379/95 P, *Commission and French Republic v. Tiercé Ladbroke Racing Ltd.*, [1997] ECR I-6265, para. 33.

277 Yet, unlike in the State compulsion doctrine, only the penalty should be rendered inapplicable. The applicability of the competition rules should, however, be maintained. It ought to be noted here that the applicability of the State compulsion doctrine does not preclude, in practice, the risk that the tacitly colluding oligopolists could be found liable for damages in the context of follow-on actions before ordinary courts. However, they may be able to benefit from the recognition of a form of "force majeure" under tort rules.

and joint ventures. In so doing, the EUMR inevitably fails to apprehend a number of market developments which significantly contribute to market concentration and, in turn, may create or strengthen tacitly collusive equilibriums. This is firstly the case with regard to firms' internal (or organic) growth strategies, which may lead to the creation, or the strengthening of anticompetitive oligopolies.[278] Put simply, the economic theory behind this is as follows: in the competitive process less efficient operators yield business to more efficient undertakings. In order to serve those customers which they manage to wrest from the former, the latter expand their scale of production through internal investments (internal growth). In the mid term, less efficient operators are forced from the market. The market eventually reaches a state of maturity with the appearance of a small number of large, entrenched firms. Those oligopolists subsequently find themselves in a position where they can cease competing, and adopt profitable, passive commercial strategies. In practice, many sectors, such as retail distribution, tyres, or professional software have experienced a significant level of oligopolistic concentration through internal growth. In *MCI/WorldCom/Sprint*, the Commission acknowledged this issue by noting that a collective dominant position may have been created prior to the notified merger following the exit of a number of players from the market.[279]

This is secondly the case with regard to a myriad of additional – often overlooked – market practices which may turn a competitive oligopoly into a tacitly collusive one.[280] For example, contractual "*meet and release*" clauses (also known as "*English*" clauses),[281] "*Most Favoured Customer*" clauses,[282] minority shareholdings and interlocking directorates,[283] basic point pricing systems,[284] etc. may also significantly contribute to the emergence of collective dominant positions on the market. The same holds true with regard to a number of other "facilitating" measures adopted

278 See J. Steindl, *Maturity and Stagnation in American Capitalism*, Monthly Review Press, New York, 1976.

279 See Case No COMP/M.1741 – *MCI/Worldcom/Sprint*, 28/06/2000.

280 See, for a discussion of those practices, Canadian Competition Bureau, The Abuse of Dominance Provisions (Sections 78 and 79 of the Competition Act) as Applied to the Canadian Grocery Sector, *Enforcement Guidelines*, November 2002, para 5.2.3.

281 See S. C. Salop, "Practices that (Credibly) Facilitate Oligopoly Coordination" in J. E. Stiglitz and G. F. Mathewson (Eds), *New Development in the Analysis of Market Structure*, MIT Press, Cambridge, 1986, p. 265.

282 See T. E. Cooper, "Most Favored Customer Pricing and Tacit Collusion", (1986) 17 *RAND Journal of Economics*, 377.

283 See D. Gilo, Y. Moshe and Y. Spiegel, "Partial Cross Ownership and Tacit Collusion", (2006) 37, *RAND Journal of Economics*, 81.

284 See D. W. Carlton, "A Reexamination of Delivered Pricing Systems", (1983) 26-1 *Journal of Law and Economics*, 51; D. D. Haddock, "Basic Point Pricing: Competitive vs. Collusive Theories", (1982) 72 *American Economic Review*, 289.

by public institutions, including competition authorities and regulators.[285] This is, for instance, the case with measures adopted by sector specific regulators, which compel market players to observe price caps or to disclose information on their pricing policy. In increasing price transparency, such measures facilitate the surveillance activities within the oligopoly, thereby supporting the emergence of tacitly collusive market outcomes.

From the foregoing it is clear that collective dominant positions do not only result from external growth strategies, but may equally arise as a corollary of other business practices, which the EUMR does not, and indeed cannot, regulate. Whilst this article does not submit that the scope of the Regulation should be extended to cover such strategies, it nonetheless stresses that, contrary to a widely held belief, the EUMR does not, and cannot to the exclusion of other legal instruments, fully prevent the emergence of tacitly collusive oligopolies.[286] Furthermore, in oligopolistic markets which are not subject to a significant level of merger activity, situations of tacit collusion may well appear, develop and become consolidated for a significant period of time without the applicability of the EUMR being triggered until a structural change has occurred on the market. In such circumstances, the Regulation fails entirely to prevent a situation of tacit collusion and, absent any *ex post* enforcement policy, such market failure indefinitely benefits from a state of provisional immunity.[287]

4. THE COMMISSION CAN PREDICT THE EMERGENCE OF COLLECTIVE DOMINANT POSITIONS ON THE BASIS OF ECONOMIC THEORY

A third possible misconception is that competition authorities, the Commission in particular, can safely predict the emergence of collective dominance. This idea draws on the intuition that modern industrial organization theory provides robust and practical economic tools for anticipating situations of tacit collusion.

Again, however, this intuition fails to reflect the complexity and nuances of

285 See S. Albæk, H. P. Møllgaard and P. B. Overgaard, "Law-Assisted Collusion? The Transparency Principle in the Danish Competition Act", (1996) 17 *European Competition Law Review*, 339.

286 A related concern is that the view that the EUMR prevents most, if not all, risks of future collective dominance seems to have been so deeply inculcated into competition agencies' staff that only meagre, if any, enforcement resources are dedicated to such practices.

287 This being said, it ought to be noted here that Article 101 TFEU covers a number of facilitating practices that take the form of inter-firm agreements. See, on this, N. Petit, supra note 264 at Chapter IV.

modern industrial organization theory. Of course, a consensus would appear to exist amongst economists (and lawyers) on the very core analytical framework to be used in order to establish collective dominance.[288] In particular, most economists agree that four cumulative elements, in accordance with the GC's case law and the Commission's Guidelines, must be identified for tacit collusion to occur, *i.e.* mutual understanding of the terms of coordination; ability of oligopolists to detect cheating behaviour; availability of retaliatory instruments; and absence of countervailing power of rivals, and other economic partners. However, economists tend to consider that the theory of tacit collusion provides a very fragile basis upon which decision makers may predict the future. As noted previously by Nobel Prize winner G. Stigler, "*with oligopoly, virtually everything is possible*".[289] This is because a gulf subsists between opposing sets of economists as regards the effect that relevant market conditions produce on the abovementioned four conditions. To take but a few examples, the existence of *capacity constraints* certainly prevents an oligopolist from cheating in the first place, and thereby facilitates tacit collusion.[290] Simultaneously, however, the existence of capacity constraints is often deemed to neutralize the threat of retaliation.[291]

A similar ambiguous, complex effect can be ascribed to so-called "*multi-market contact*". When oligopolists are active on several distinct markets, they are able to punish deviations on a wider range of sectors, a consequence of which is that the deterrent effect of any punishment increases. As a result, multi-market contacts are deemed to facilitate tacit collusion.[292] Yet, other economists stress the fact that when oligopolists are active on several markets, retaliating on several markets is extremely costly.[293] In addition, in such a situation, an oligopolist may have increased incentives to cheat, in the hope of reaping profits not only on one market, but also on the other markets on which it is active.

288 See D. K. Osborne, "Cartel Problems", (1976) 66(5) *American Economic Review*, 835; D. Orr and P. W. McAvoy, "Price Strategies to Promote Cartel Stability", (1965) 32 *Economica*, 186; I. Ayres, "How Cartel Punish: A Structural Theory of Self Enforcing Collusion", (1987) 87(2) *Columbia Law Review*, 295, p. 296; T. Penard, "Collusion et comportements dynamiques en oligopole: une synthèse", supra note 262, p. 3.

289 See G. J. Stigler, "Theory of Oligopoly", (1964) 72 *Journal of Political Economy*, 44.

290 See Study on Assessment Criteria for Distinguishing between Competitive and Dominant Oligopolies in Merger Control, Report for the European Commission, DG Enterprise, May 2001, Europe Economics.

291 See F. Jenny, "Economic Analysis, Anti-trust law and the Oligopoly Problem", (2000) 1 *European Business Law Review*, 41; See K.U. Kühn, "An Economists' Guide through the Joint Dominance Jungle", Paper #02-014, John M. Olin Center for Law & Economics – University of Michigan.

292 See B. D. Bernheim and M. D. Whinston, "Multimarket Contact and Collusive Behavior", (1990) 21 *RAND Journal of Economics*, 1.

293 See S. Bishop and M. Walker, *The Economics of EC Competition Law*, 2nd Ed., Sweet&Maxwell, London, 2002, para. 7.60, p. 288.

Finally, *demand growth* is also a notoriously ambiguous market characteristic.[294] Some economists contend that it prevents tacit collusion because oligopolists have strong incentives to engage in cut-throat competition in order to capture new customers.[295] In addition, demand growth could trigger market entry which, in turn, undermines the potential for tacit collusion.[296] This being said, other economists argue that faced with demand growth, oligopolists are increasingly likely to collude.[297] This is because oligopolists have no incentives to engage in price competition strategies in the short run for fear of undermining their joint ability to coordinate prices in the future.

Because many market characteristics may either facilitate (pro-collusive effect) or undermine (anti-collusive effect) tacit collusion, it is almost impossible for competition authorities to prospectively determine (absent *ex post* evidence) which of those effects will prevail. In other words, the decision that a given market characteristic will lead to one type of effect rather than another invariably involves a certain degree of over-generalization and arbitrariness.[298]

This problem is further compounded by the fact that the risks of tacit collusion may be influenced by other unobservable variables. Regardless of economic profit-maximization considerations, the psychological, social and historical background of the oligopolists may influence their decision to adhere to a tacitly collusive equilibrium.[299] For instance, these firms may be particularly prone to acting in parallel because their CEOs have been educated together and thus share strong cultural bonds. In the same vein, an irrational competitor may decide to cheat regardless of the risk of costly punishment, simply because it wishes to maintain its reputation as a hard discount player on the market.

294 See J. Haltiwanger and J. E. Harrington, "The Impact of Cyclical Demand Movements on Collusive Behavior", (1991) 22 *RAND Journal of Economics*, 89.

295 See M. Ivaldi, B. Jullien, P. Rey, P. Seabright and J. Tirole, *The Economics of Tacit Collusion*, Final Report for DG Competition, European Commission, March 2003, p. 28.

296 Id.

297 See M. Motta, *Competition Policy – Theory and Practice*, Cambridge University Press, Cambridge, Massachusetts, 2004, p. 146.

298 See on this T. Kauper, "Oligopoly: Facilitating Practices and Plus Factors", in B. Hawk (ed.) 2007, *Fordham Competition Law Institute*, 751 at pp. 754-755.

299 See F. M. Scherer and D. Ross, *Industrial Market Structure and Economic Performance*, 3rd Ed., Houghton Mifflin Company, Boston, 1990, pp. 235-236, who provide the example of the dinners organized by Judge Elbert H. Gary, the President of US Steel's Board of Directors between 1907 and 1911. Judge Gary explained once that: "*these dinners generated such mutual respect and affectionate regard among steel industry leaders that all considered the obligation to cooperate and avoid destructive competition more binding than any written or verbal contract*".

Finally, in merger control proceedings involving tacit collusion there is an additional hurdle. Because a situation of collective dominance entails the cooperation of most, if not all, players on the market, the Commission must not confine itself to investigating the merging parties, but also extend its inquiries to their rivals. In particular, it must collect information on their costs, investment, pricing strategies, etc. This implies that in collective dominance cases the Commission must in reality conduct an investigation which is tantamount to a broad and burdensome "*sector inquiry*". However, unlike under Article 17 of Regulation 1/2003,[300] such sector inquiry must be carried out within the tight time limits provided for in the EUMR. Though perhaps a trite observation, any such investigation is likely to prove extremely difficult for the Commission.

Despite recent papers suggesting the contrary, the Commission's recent decisional practice bears testimony to the difficulties of proving tacit collusion in merger cases.[301] In recent years, the Commission has erred on the side of caution and promoted a "*low-profile*" enforcement policy. Since the *Airtours* judgment,[302] the Commission has only scrutinized the risks of tacit collusion/collective dominance/coordinated effects in 11 cases.[303] The staggering number (95 in total) of collective dominance-related decisions adopted by the Commission between 1989 and the *Airtours* judgment, a period during which the evidentiary burden on the Commission was considerably lower, puts the Commission's enforcement activity since *Airtours* into perspective. In addition, in a not insignificant number of those cases, the Commission has seemed incapable of proving the initial collective dominance concerns identified in its Statement of Objections. The Commission

300 See Article 17 of Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty, (2003) L1/1, in particular para. 1 which provides: "*Where the trend of trade between Member States, the rigidity of prices or other circumstances suggest that competition may be restricted or distorted within the common market, the Commission may conduct its inquiry into a particular sector of the economy or into a particular type of agreements across various sectors. In the course of that inquiry, the Commission may request the undertakings or associations of undertakings concerned to supply the information necessary for giving effect to Articles 81 and 82 of the Treaty and may carry out any inspections necessary for that purpose. The Commission may in particular request the undertakings or associations of undertakings concerned to communicate to it all agreements, decisions and concerted practices. The Commission may publish a report on the results of its inquiry into particular sectors of the economy or particular types of agreements across various sectors and invite comments from interested parties*".

301 See A. Amelio, P. Asbo, M. de la Mano, R. Maximiano and V. Porubsky, "ABF/GBI Business: coordinated effects baked again", Competition Policy Newsletter, 2009-1.

302 See CFI, Case T-342/99, *Airtours plc. v. Commission*, [2002] ECR II-2585. In April 1999, Airtours notified its proposed acquisition of First Choice to the Commission. The latter was a direct competitor of Airtours on the British market for short-haul foreign package holidays. The operation reduced the number of tour operators to three (the merged entity, Thomson and Thomas Cook). They together held an 83 percent share of the market. At the end of its assessment, the Commission concluded that the operation would lead to a collective dominant position and thus prohibited it.

303 See the decisions quoted at footnote 265.

ultimately chose to leave the issue open.[304] This problem is particularly apparent in the *JCI/Fiamm*,[305] *Lesaffre/GBI UK*,[306] *IPIC/MAN Ferrostaal AG*,[307] *T-Mobile/Tele.ring*,[308] and *Arjowiggins/M-real Zanders Reflex* cases.[309]

5. THE SUBSTANTIVE LEGAL PRINCIPLES GOVERNING COLLECTIVE DOMINANCE ARE SOUND AND WELL-SETTLED

A fourth possible misconception consists in believing that the EUMR's jurisdictional monopoly over tacit collusion is legitimate because the merger control regime is grounded upon a high degree of *legal soundness, maturity* and *certainty* (as opposed to the perceived obscurity and novelty of the concept of abuse of a collective dominant position under Article 102 TFEU).

In the authors' opinion, there is a distinct want of merit in the contention that the dust has settled as far as the legal standards underpinning collective dominance are concerned.[310] *Airtours v. Commission* and the Guidelines on Horizontal Mergers ("the Guidelines")[311] indeed ushered in an increased degree of legal clarity, with the laying down of four cumulative conditions for a finding of collective dominance. The recent rulings handed down by the GC and the Court of Justice of the EU ("CJ", formerly the "ECJ") in *Impala v. Commission* have, however, muddied the waters regarding the application of those standards.[312] In *Impala*, which concerned a proposed joint venture between Sony and BMG in recorded music markets, the GC explicitly, albeit in an *obiter dictum*, undermined the relevance of the four cumulative conditions set out in *Airtours v. Commission* and in the Guidelines on horizontal mergers. At paragraph 251 of its judgment,

304 The Commission decided to rely on other theories of harm and/or declared that the proposed remedies, in restoring the *status quo*, allayed all competition concerns.

305 See Case No COMP/M.4381 – *JCI/Fiamm*, supra note 265, para. 505 ("*Based on the results of the market investigation, it is therefore concluded that, while the merger [...] may increase the likelihood of the emergence of coordinated effects on the OE markets for starter batteries for cars/LCV and trucks/HCV by removing an important competitor, the Commission has not found sufficiently convincing evidence to demonstrate that such coordinated effects are more likely than not to emerge*").

306 See Case No COMP/M.5020 – *Lesaffre/GBI UK*, supra note 265, para. 47.

307 See Case No COMP/M.5406 – *IPIC/MAN Ferrostaal AG*, supra note 265, para. 63.

308 See Case No COMP/M.3916 – *T-Mobile Austria/Tele.ring*, 26/04/2006, para. 129.

309 See Case No COMP/M.4513 – *Arjowiggins/ M-real Zanders Reflex*, supra note 265, para. 434.

310 See, for a similar opinion, J. Briones, "From Collective Dominance to Coordinated Effects in EU Competition Policy", *GCP: The Antitrust Chronicle*, October 2009(1), at p. 7 ("*we have little guidance as to how oligopolies will be handled*").

311 See Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, OJ C 31, 05.02.2004, pp. 5-18.

312 See CFI, Case T-464/04, *Independent Music Publishers and Labels Association (Impala) v. Commission*, 13 July 2006, [2006] ECR I-2 and ECJ, Case C-413/06 P. *Bertelsmann AG and Sony Corporation of America v Independent Music Publishers and Labels Association (Impala)*, [2008] ECR I-4951.

the GC declared that:

> "*[I]n the context of the assessment of the existence of a collective dominant position, although the three conditions defined by the Court of First Instance in Airtours v Commission, paragraph 45 above, which were inferred from a theoretical analysis of the concept of a collective dominant position, are indeed also necessary, they may, however, in the appropriate circumstances, be established indirectly on the basis of what may be a very mixed series of indicia and items of evidence relating to the signs, manifestations and phenomena inherent in the presence of a collective dominant position.*"

The CJ, on appeal,[313] seemed to confirm this analysis at paragraphs 125 and 128 of its judgment.[314] Such pronouncements – the interpretation of which remains keenly disputed by legal scholars –[315] are obviously unfortunate from the standpoint of legal certainty. Whilst, of course, the four demanding *Airtours* conditions had raised the evidentiary burden imposed on the Commission in merger proceedings – and allowed parties to discredit in their entirety tacit collusion theories of harm by simply proving the absence of one condition – those conditions provided a clear, comprehensive legal framework for the assessment of collective dominance.[316] Following the *Impala* rulings, the Commission may now "*indirectly*" reach findings of collective dominance. The abstract wording of the ruling, where the GC evokes "*a very mixed series of indicia and items of evidence relating to the signs, manifestations and phenomena inherent [in] a collective dominant position*" bears testimony to the fact that legal certainty has been somewhat watered down.

Second, the substantive principles established in those recent judgments are not based on sound economics. In particular, the standard according to which

313 On points of law.

314 See B. Van Rompuy, "Implications for the Standard of Proof in EC Merger Proceedings: Bertelsmann and Sony Corp. of America v. Impala (C-413/06 P) ECJ", (2008) 10, *European Competition Law Review*, 608, p. 611. See ECJ, id, at paras. 125 and 128. The Court noted that "*objection cannot be taken to paragraph 251 of itself*". It also observed: "*In applying those criteria, it is necessary to avoid a mechanical approach involving the separate verification of each of those criteria taken in isolation, while taking no account of the overall economic mechanism of a hypothetical tacit coordination*". See, for a similar interpretation, S. Stephanou, "Collective Dominance Through Tacit Coordination: The Case for Non-Coordination Between Article 82 and Merger Control 'Collective Dominance Concepts', *GCP: The Antitrust Chronicle*, October 2009(1), at p. 6 note 15. For a discussion of the case see also J. Luebking and P. Ohrlander, The Joint Venture Sony BMG: final ruling by the European Court of Justice, Competition Policy Newsletter 2009-2.

315 See, for instance, T. Käseberg, "Case C-413/06 P. Bertelsmann AG and Sony Corporation of America v. Independent Music Publishers and Labels Association (Impala), (2009) 46 *Common Market Law Review*, 255.

316 See S. Baxter and F. Dethmers, "Collective Dominance under EC Merger Control – After Airtours and the Introduction of Unilateral Effects is there Still a Future for Collective Dominance?", (2006) 27(3) *European Competition Law Review*, 148.

a collective dominant position can be inferred from mere observations of price uniformity, supra-competitive profits and other empirical data suffers from the very obvious flaw that correlation does not imply causation.[317] Situations of price uniformity may appear, for instance, in mature markets where technology and costs remain constant when operators price at marginal cost as a result of fierce competition in the market. Similarly, in a model of so-called COURNOT competition, which leads to price equilibriums situated between marginal costs-pricing and monopoly pricing, oligopolists may achieve supra-competitive profits absent tacit collusion.[318] Furthermore, in markets where scale matters, large incumbent oligopolists may enjoy generous margins simply because they are very efficient.

Rather, we believe that the aforementioned principle may lead to a risk of decisional abuse. The Commission may, by rigidly adhering to such standard, reserve to itself the ability to freely brush aside and disregard key tenets of economic theory in order to reach findings of collective dominance. For instance, it may rely on the fact that the parties' prices have followed a similar evolution, and pay no heed to the fact that the market is not sufficiently transparent to harbour a situation of tacit collusion.

A similar analysis applies to retaliation, which represented a core issue in the *Airtours* case. The level of vehemence of any retaliatory measure required to discourage cheating and, in turn, give rise to a situation of collective dominance remains unclear. The relevant guidelines in this respect are couched in rather loose terms, a consequence of which is that the Commission is accorded a significant margin of discretion in this context. In a footnote, the Guidelines consider that:

> *"The expectation that coordination may break down for a certain period of time, if a deviation is identified as such, may in itself constitute a sufficient deterrent mechanism."*[319]

317 The GC seemed to recognize this at para. 252 of its judgment in stating that: "*loose alignment of prices over a long period, especially if they are above a competitive level, together with other factors typical of a collective dominant position, might, in the absence of an alternative reasonable explanation, suffice to demonstrate the existence of a collective dominant position* (emphasis added)". However, the scope of this qualification is unclear. See, on this, N. Petit, supra note 264, pp. 253-260.

318 See A. Cournot, *Recherches sur les principes mathématiques de la théorie des richesses*, Dunod, Paris, 2001 (réédition de l'article paru au *Journal des Savants*, 1883). It is interesting to note that the OECD alluded in 2002 to the possibility of extending the concept of collective dominance to anticompetitive oligopolistic inter-dependence falling short of tacit collusion. See OECD, Policy Roundtables, *Substantive Criteria used for Merger Assessment*, 2002.

319 See Guidelines on the assessment of horizontal mergers under the Council Regulation, supra note 311, at note 70.

Yet, this contention is disputed in economic theory. Whilst it is conventionally accepted that retaliation must be such that it is able to cancel out the profits achieved through a cheating strategy,[320] economists are generally loath to hold that the mere risk of a return to the competitive equilibrium is sufficient to constitute a retaliatory mechanism. Depending on the circumstances, tacit collusion may only be sustainable if the oligopolists have the ability and incentives to retaliate through, for instance, below-costs pricing strategies (i.e. predatory pricing).

Finally, the Guidelines primarily focus on the factors that facilitate tacit collusion, and thus paint a grim picture of the effects that mergers may have on the likelihood of its occurrence.[321] In so doing, the Guidelines fail to reflect the current state of economic thinking in the literature, which equally insists on those factors which hinder tacit collusion. This is true in two particular respects. First, the Guidelines are silent on a number of market features which exert ambivalent effects on tacit collusion. For example, the document disregards a number of factors (e.g. overcapacities, capacity constraints, demand growth, demand inelasticity, network effects, etc.), which all produce contrasting effects on tacit collusion. Second, the document alludes to certain economic parameters in so far as they have a positive effect on the risks of collective dominance, but rather remarkably remain silent on the parallel, undermining effect which such parameters may produce. For instance, multi-market contacts are only referred to as facilitating retaliation, with no reference being made to the fact that they may increase profits pursuant to a cheating strategy (and increase the costs of retaliation).[322]

Third, and aside from the confused state of affairs resulting from the *Impala* rulings, the *Airtours* case and the Guidelines leave many technical and substantive issues unanswered. It remains for instance open to question whether, in order to establish a situation of tacit collusion, the Commission must prove that retaliation will be specifically targeted at the cheating firm (through, for instance, target rebates, price discrimination in favour of the cheating undertaking's customers, other exclusionary and boycott tactics), or whether it is sufficient to prove a risk of *general* retaliation through market-wide price reductions. Again, relying on the mere observation of untargeted retaliation to establish collective dominance has given rise to criticism. Indeed, in such situations a punishing firm may cause other oligopolists to incur costs, and may as a result expose itself to the risk of retaliatory

320 See N. Petit, supra note 264, p. 39.

321 Id, pp. 233-237.

322 See S. Bishop and M. Walker, supra note 293, paras. 7-60.

measures at a later stage.[323] In order to avoid this in the first place, the punishing firm may simply forgo the opportunity to enforce the retaliatory mechanism. In other words, the inability of oligopolists to specifically target retaliatory measures may jeopardize all future prospects of effective punishment and, as a corollary, impede the emergence of tacitly collusive strategies.

Similarly, a number of uncertainties arise as regards the issue of whether all oligopolists must be in a position to retaliate, and indeed be likely to do so, for collective dominance to occur. The Guidelines indicate rather laconically that "*The credibility of the deterrence mechanism depends on whether the other coordinating firms have an incentive to retaliate* (emphasis added)".[324] Unless the Commission can anticipate which firm is likely to cheat, and subsequently focus only on the other players' ability to retaliate, there are solid grounds for believing that the Commission should consider each and every market player's ability to punish a cheating strategy.

6. REMEDIES NEGOTIATED UNDER THE EUMR APTLY ALLAY COLLECTIVE DOMINANCE CONCERNS

A final mistaken belief is that, once a risk of collective dominance has been identified, the Commission could appropriately assuage any tacit collusion concerns by requiring the parties to offer structural remedies as a *quid pro quo* for a conditional clearance decision. A few years ago, one of the authors of this article conducted a survey which demonstrated that 54 percent of the remedies negotiated by the Commission with a relevant party in collective dominance cases consisted in creating a new, external competitive entity on the market (through structural divestitures, for instance), which could compete with the incumbent oligopolists. By contrast, 40 percent of the remedies consisted in the severance of internal links between oligopolists (joint ventures, etc.).

Contrary to this conventional view, we believe that the structural remedies negotiated by the Commission with the merging parties may generate perverse effects, and in particular, may further exacerbate the risks of tacit collusion. As far as the first type of remedy is concerned – *i.e.* the creation of a new competitive entity on the market – the Commission has often requested

323 See R. O'Donoghue and C. Feddersen, "Case T-342/99, Airtours plc v. Commission, Judgment of the Court of First Instance of 6 June 2002, nyr" (2002) 39 *Common Market Law Review*, 1171.

324 See Guidelines on the assessment of horizontal mergers under the Council Regulation, supra note 311, para. 54.

incumbent oligopolists to transfer relevant assets. Such measures, which normally fall beyond the scope of the Commission's oversight capabilities (they are implemented by the parties and trustees) imply a potential risk of secret, arm's length collaboration between the incumbent oligopolists and the new entrant. As a result, one cannot exclude that a vendor will seek to induce the acquirer to join the tacitly collusive oligopoly. As explained by Professor Farrell: "*[a]gencies should beware of over-trusting the buyer of the divested assets. A strong argument can be made that the buyer is a team-mate not of the agency but of the merging parties*".[325] In practice, the US Federal Trade Commission has found empirical evidence of this problem in two merger cases.[326]

In the same vein, whilst a divestiture of assets to a new entrant will in theory undermine collective dominance by increasing the number of firms active on the market, it may simultaneously increase the degree of symmetry between the incumbent oligopolists and thus indirectly encourage tacit collusive dynamics. This risk is particularly acute when the proposed merger entails the creation of an asymmetric oligopoly where the collusive outcome takes the form of price leadership.[327] Whilst the divestiture of assets may well erode the price leader's market share, it may concomitantly increase the symmetry of market shares held by the relevant oligopolists. The remedy may thus fall into the trap of simply bringing about a change in the nature of collusion.

As far as the second type of remedy is concerned – i.e. the severance of internal links between oligopolists – they are likely to be ineffective because the Commission's powers under the EUMR can exclusively bear on the "*undertakings concerned*", i.e. those participating in the concentration.[328] In contrast to Article 101 TFEU, the Commission cannot request third parties (firms that are for instance linked to the merged oligopolist) to sever commercial, industrial, and other financial links. In practice, this means that the ability of the merging parties to enforce a proposed commitment will ultimately depend on the goodwill of third parties. Moreover, because the implementation of the merger might be conditional on the attendant implementation of the relevant remedy, third parties may

325 See J. Farrell, "Negotiation and Merger Remedies: Some Problems", (in:) F. Levêque and H. Shelanski (Eds), *Merger Remedies in American and European Competition Law*, Edward Elgar, Cheltentham, 2003, p. 95.

326 See F. Leveque, "Quelle efficacité des remèdes du contrôle européen des concentrations?", (2006) 1 *Concurrences*, 27.

327 In such a setting, one firm – the one with high market shares – would lead the market (*i.e.* it sets the prices), and the others would follow.

328 See Article 8(2) of Council Regulation (EC) No. 139/2004, supra note 263.

be in a position to hold the merging parties hostage in order to extract significant financial compensation, etc. Finally, it ought to be remarked that such remedies are, *ex hypothesi*, unavailable in cases of pure tacit collusion (*i.e.* collusion absent structural, or commercial links).[329]

7. CONCLUSION

The current "monopoly" position occupied by the EUMR vis-à-vis issues pertaining to tacit collusion issues is somewhat paradoxical. Whilst there remains a gulf between opposing sets of economists regarding the real existence of pure, oligopolistic tacit collusion on markets for everyday products/services,[330] the Commission's practice "*systematically*" scrutinizes the risk of collective dominance arising from oligopolistic mergers on the basis of the EUMR.[331] Whilst we believe that, from a resource-based perspective, the cost of testing all oligopolistic mergers on the grounds of potential collective dominance concerns is likely to be high, the Commission seems to believe that it is lower than the cost attributable to the allegedly complex and cumbersome system of *ex post* monitoring under Article 102 EC.[332] This cost-benefit perspective, however, is not based on any empirical evidence. In addition, it fails entirely to factor in the huge costs which may result from erroneous *ex ante* predictions under the EUMR.

In addition, such a systematic, preventive approach is problematic for a number of reasons. Exclusive reliance on the EUMR in order to abate tacit collusion concerns fails first to apprehend certain market constellations which arise from organic growth strategies.[333] Second, it imposes unwarranted informational

329 See J. Temple Lang, "Oligopolies and Joint Dominance in Community Antitrust Law" in B. Hawk (Ed.), (2000) *Fordham Corporate Law Institute*, 269, p. 347.

330 See T. Penard, "Collusion et comportements dynamiques en oligopole: une synthèse", supra note 262. See also T. Kauper, supra note 298, pp. 754-755. Experimental economics also casts doubt on the plausibility of the existence of tacit collusion absent any communication. See, for instance, A. Muren and R. Pyddoke, "Does Collusion without Communication Exist?", *Research Papers in Economics* 1999, 11, Stockholm University, Department of Economics and the various references cited in this study. See finally R. Posner, "Oligopoly and the Antitrust Laws: A Suggested Approach", supra note 272 who considers that core tacit collusion is in reality likely to be rare, absent additional facilitating practices and contacts between oligopolists.

331 See J. Briones, supra note 269, p.1. The Commission also scrutinizes collective dominance in vertical mergers. See for instance, the *TomTom/TeleAtlas* and *Nokia/Navteq* decisions, supra note 265.

332 See F. Mezzanotte, "Can the Commission use Article 82EC to Combat Tacit Collusion?" – CCP Working Paper 09-5, available at http://www.uea.ac.uk/polopoly_fs/1.111282!ccp09-5.pdf (stressing the costs and burdens of collective dominance investigations under Article 102 TFEU).

333 In addition, assuming the existence of textbook tacit collusion situations where symmetrical oligopolists charge supra-competitive prices and make abnormal profits, it is doubtful that such oligopolists will actually merge, on pain of (i) creating a structural imbalance in the market which will undermine their ability to achieve supra-competitive profits; and (ii) attracting the attention of competition authorities.

and procedural burdens on oligopolistic firms. Third, and more fundamentally, it increases the risk of decisional errors because of the flaws in the economic theory on which the Commission relies and the short deadlines within which it is required to predict future occurrences. Finally, it does not reflect the very economic idea that tacit collusion is, in so far as its effects are concerned, almost as damaging as a hardcore horizontal cartel. As a result, competition authorities should arguably use the full range of their legal weaponry to dissolve tacitly collusive equilibriums and not close the door to *ex post* enforcement actions.

Stanisław Sołtysiński, Krzysztof Kanton

CRITERIA FOR NOTIFYING INTENDED MERGERS TO THE PRESIDENT OF THE OFFICE OF COMPETITION AND CONSUMER PROTECTION – DE LEGE LATA AND DE LEGE FERENDA COMMENTS

1. INTRODUCTION

Regulations concerning the control of mergers between undertakings have been in force in the Polish legislation for almost twenty years now. Their present shape is based on the EU regulations. Similarly to the Community model, the turnover of the undertakings taking part in a transaction is the basic criterion with respect to notifying a merger to the President of the Office of Competition and Consumer Protection ("competition authority"), and only the types of transactions specified in the Polish competition act are subject to preventive control by the competition authority. The fundamental concepts developed in the EU legislation (e.g. "acquisition of control" or "enterprise concerned") have also been reflected in Polish regulations.

Changes in legislation carried out over the past years not only made Polish regulations closer to the solutions functioning in the Community law, but also eliminated or specified solutions which previously gave rise to numerous legal doubts. An important event from the point of view of the above process was entry into force of the Act on competition and consumer protection of 2007[334] (the "Act"), which introduced a number of positive changes to the regulations concerning the control of intended mergers. With relation to the above changes, one should draw attention in particular to limiting the catalogue of transactions which may be subject to the notification obligation to those which can have a real effect on the market (thus the notification obligation does not cover the quasi-concentrations[335], which do not result in significant changes in the state of competition). The thresholds concerning the turnover of the merging companies were raised and the way of calculating the turnover of the acquired undertaking for the purpose of applying

334 (Dz.U. of 21 March 2007 No. 50, item 331 as amended).

335 It was especially important here to eliminate the need to obtain prior permission of the competition authority for acquiring the right providing 25 percent of votes at the general shareholders' meeting (shareholders' meeting) of another undertaking.

the *de minimis* exemption specified in Article 14(1) of the Act was changed as well.[336] The Act also modified regulations concerning exemptions from the notification obligation (e.g., it eliminated the provision excluding the application of the *de minimis* rule when the merger could lead to the creation or strengthening of a dominant position on the market, which caused many doubts in practice).

The basic aim of the introduction of the above changes was to attempt to limit the number of notifications, which would enable the competition authority to focus its attention on mergers having important consequences for competition in Poland.[337] At the same time the legislator's intention was to make the regulations more precise in order to introduce clear and objective criteria concerning the notification obligation, which could be applied automatically by the enterprise, without the need to carry out in-depth analyses.

One may ask whether the above aims were achieved. Referring to the first of the above objectives, increasing the turnover thresholds and modifying the rules concerning the calculation of turnover for the *de minimis* exemption, actually reduced the number of notifications concerning mergers having neutral impact on the state of competition in Poland. At the same time, the catalogue of exemptions from the notification obligation set out in Article 14 of the Act which is now based on objective criteria, contributed to the increase in the legal certainty of undertakings as regards the existence of the notification obligation.

A closer analysis of the criteria concerning the notification of intended mergers leads, however, to the conclusion that certain legislative solutions stipulated by the Act seem to set the scope of preventive merger control still too broadly, in particular if compared to the Community rules set out in Council Regulation (EC) No. 139/2004 of 20 January 2004 on the control of concentrations between undertakings ("Regulation 139/2004") which governs the criteria for the notification of mergers of a Community dimension. While applying the described regulations, a number of crucial practical doubts arises, often connected with such basic issues as determining whether a particular transaction is a merger (or "concentration")

336 In accordance with this regulation, concentration is not subject to the notification to the competition authority if the turnover of the target undertaking gained in Poland did not exceed the equivalent of 10 million euro in any of the two financial years preceding the notification.

337 This results directly from the justification of the draft law, where while pleading the necessity of increasing the notification thresholds, the authors pointed out that: "*In practice this change is to create a situation where the competition authority shall control only the largest concentrations, which shall have a real impact on the state of competition on the market. This refers mainly to the trade concentrations, which can definitely lead to the distortions of free competition mechanisms*".

within the meaning of the Act (especially in connection with transactions which consist in acquiring another undertaking's assets). The above issues are discussed in the next part of the paper.

2. THE CRITERION OF CONCENTRATION EFFECT IN THE TERRITORY OF POLAND

While determining whether the provisions of the Act shall be applied to a given transaction, first it needs to be determined whether the transaction has or may have effects in the territory of Poland. Considering this issue is necessary to determine the notification obligation of mergers carried out outside the territory of Poland, referred to as „extraterritorial concentrations". Absence of effects in Poland creates a situation where the provisions of the Act will not apply even if the general premises concerning the turnover of the undertakings concerned are met and the transaction is not subject to any exemption on the basis of Article 14 of the Act.[338]

The Act does not include any indications concerning the criteria of assessing whether or not a particular extraterritorial concentration has effects in the territory of Poland. Attempts to introduce certain rules in this respect have been made in the past, and consequently it was assumed that a concentration has effects in Poland when the undertakings concerned or their capital groups are present or carry out business activity in the territory of Poland. For example, in the Guidelines of the President of the Office of Competition and Consumer Protection on the criteria of merger notifications published in 2003 (the "Guidelines"), an extraterritorial transaction required notification to the competition authority if: (i) there was a company registered in Poland belonging to the capital group of at least one direct participant to the concentration or (ii) there were permanent sales or a distribution network in Poland operated by a company belonging to the capital group of at least one direct participant to the concentration. In 2005 an official interpretation concerning the effects of extraterritorial mergers in Poland was published on the Office's website. According to this interpretation, it was assumed that a concentration of foreign undertakings has an effect in Poland only if at least two entities participating in it belong to capital groups having

338 This results directly from Article 1 of the Act, where the rule of extraterritorial operation of its provisions is included: *"The Act regulates the rules and measures of counteracting practices restricting competition and practices violating collective consumer interests, as well as anti-competitive concentrations of undertakings and associations thereof, where such practices or concentrations cause or may cause effects in the territory of the Republic of Poland"* (underlined by the authors).

a dependent entity with its seat in Poland. The above interpretation was removed from the Office's website in autumn 2007.

Developing certain general and precise rule concerning the "effects" of a transaction in Poland seems to be very difficult due to the variety of different states-of-play which we face in practice. Thus, each extraterritorial concentration requires individual assessment concerning its impact on the Polish market. In this context, it should be highlighted that the future geographical scope of the target undertaking or the new undertaking created as a result of the merger should be analysed in the first place. The analysis should cover the directions of sales which are planned after the merger, plans concerning future activity, the possibility of starting business in Poland, etc. It seems that the key issue here is to determine whether a new competitor, within the meaning of Article 4 (11) of the Act[339], appears in the Polish market or in the market which covers the territory of Poland.

If the mentioned analysis shows that there is no connection between the planned transaction and the territory of Poland, then the Act does not apply. The above rule should be applied also with relation to a concentration which takes place outside of the territory of Poland in which a Polish undertaking participates (e.g. by creating a foreign company or acquiring control of such a company).

The above "economic approach" towards the issue of a merger's effects has been reflected in some of the present decisions of the competition authority. For example, having considered the acquisition of ORKLA media concern by Mecom Group Ltd, the authority issued a clearance for acquiring control over Polish subsidiaries of the concern, and at the same time discontinued as groundless the proceedings concerning the acquisition of control over Det Berlingske Officin A/S. The competition authority recognized that the foregoing company, as well as its subsidiaries, do not carry out any activity in the territory of Poland, and the markets on which it operates are local markets. When justifying the decision on discontinuation of the case, the competition authority pointed out that:

> *"It should be thus acknowledged that the transaction consisting in the acquisition of DBO, operating only in the territory of Denmark, by Mecom Group plc. will not*

339 The Act defines competitors as undertakings which at the same time release or may release, purchase or may purchase goods in the relevant market. In the light of the Guidelines, a competitor is both a "real competitor" and a "potential competitor", which means an undertaking who has an appropriate production, technological or financial potential and is able to enter the market in a comparatively short time and regardless of the costs.

cause in any way any effects in the territory of the Republic of Poland. Taking the above into consideration, the President of the Office was not the competent authority for adjudicating the present case.[340]

One of the shortcomings of invoking "exemption" from the notification obligation due to lack of effects in the territory of Poland is the possibility of questioning the results of the analysis carried out by an undertaking (in particular taking into account the fact that the Act uses the term "potential effects" on the market). In this context it is worth considering a modification of the rule requiring an intended concentration to be notified when either of the turnover thresholds referred to in Article 13 of the Act[341] has been exceeded. In light of the provisions in force, the notification obligation applies even if the undertakings participating in the transaction did not achieve any turnover in the territory of Poland. Taking into account the intention to limit the formal need to notify mergers only to those transactions which have actual effects in the territory of Poland, it is justified to consider amending the Act by means of introducing the obligation to notify a merger only if the aggregate worldwide turnover and the turnover achieved in the territory of Poland by the participants of the concentration exceeded at the same time the thresholds referred to in the Act.

It is worth noting that a solution combining both thresholds (i.e. worldwide turnover and turnover in the territory of the European Community) was adopted in the Community regulations. In accordance with Article 1(3) of Regulation 139/2004, a transaction has a Community dimension where: (i) the combined aggregate worldwide turnover of all the undertakings participating in it is more than 5 billion euros; and [author's emphasis] (ii) the aggregate Community-wide turnover of each of at least two of the undertakings concerned is more than 250 million euros, unless the so-called two-thirds rule applies.[342] The same rule is in force with relation to the verification of Community dimension of a merger referred to in Article 1 (4) of Regulation 139/2004.[343]

340 Decision of the President of the Office of Competition and Consumer Protection of 10 October 2006, No. DOK 119/06.

341 A transaction has to be notified if it involves undertakings whose aggregate global turnover exceeds the equivalent of 1 billion euros or their aggregate turnover in Poland exceeds the equivalent of 50 million euro in the financial year preceding the notification year.

342 A concentration has no Community dimension if each participant achieves 2/3 of his turnover within one and the same EU Member State.

343 It is worth pointing out, by the way, that similar rules were introduced in March 2009 to German merger regulations. Now, a merger requires to e notified to the Bundeskartellamt when all of the following conditions are met: (i) the worldwide turnover of the merger participants exceeds 500 million euro; (ii) at least one participant of the merger has a turnover exceeding 25 million euro in Germany; (iii) the other undertaking concerned has a turnover exceeding 5 million euro in

Linking the merger notification obligation with the turnover achieved in the territory of Poland would be cohesive with the Community law and would, at the same time, enable to refer to an unequivocal turnover criterion while assessing whether a transaction has a national dimension or not, without the necessity to draw up detailed analyses concerning the occurrence of real or potential effects of a transaction in Poland.

3. CALCULATING THE TURNOVER

As regards transactions consisting in acquiring control over another undertaking, the Act introduced a very significient, from the practical point of view, change in the way of calculating the turnover of the target entity for the purpose of assessing whether the *de minimis* rule applies to a transaction. Pursuant to the *de minimis* exemption, there is an obligation to notify the concentration if the turnover of the target undertaking in Poland does not exceed the equivalent of 10 million euros. Under the previous regulations, the turnover of the entire capital group of the target undertaking had to be included in the calculations, i.e. also the turnover of the undertaking exercising the ultimate control over the target undertaking and the turnover of all the undertakings which were its subsidiaries.[344] In accordance with the explanatory notes to the draft law: "*such solution was inappropriate (the turnover of the latter is not important when assessing the impact of this type of transaction on the market), therefore, it must be changed.* Currently, in accordance with Article 16(2) of the Act, to verify whether a transaction is subject to the exemption, only the turnover of the acquired undertaking as well as of its subsidiaries is taken into account.

The same principle, excluding the turnover of a capital group of the so-called passive participant of a merger (i.e. target entity), was not introduced to Article 13 of the Act, which sets forth the general turnover thresholds. This means that in the case of a transaction consisting in the acquisition of control over another undertaking, the aggregate turnover of the undertakings involved would include the turnover of the target's capital group, including both the turnover of the seller and the future parent company and its all subsidiaries. In the case of transactions consisting in two or more undertakings merging together or creating

Germany. The above changes were introduced to the German law as a response to demands concerning reduction of the very large number of notifications made under previous regulations, which set forth the obligation to notify a merger if the turnover of one of the undertakings concerned exceeded 25 million euro in Germany.

344 Cf. the Guidelines, page 15.

a joint undertaking, taking into account the turnovers of the involved companies' capital groups is justified since (at least indirectly) these groups are engaged in the transaction. It is difficult, at the same time, to find justification for the necessity to consider the capital group which as a result of a transaction loses control over the target company when evaluating the economic potential of the participants to the concentraton.

The above legislative solution is not coherent with the Community regulations[345], which state that in order to establish whether a transaction consisting in the acquisition of control over another undertaking has a Community dimension, only the turnover achieved by the acquirer, its capital group and the target undertaking, plus its subsidiaries[346] should be taken into consideration. It is worth to note point 136 of the Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No 139/2004 on the control of concentrations between undertakings ("Notice"), which states that: *"The possible impact of the transaction on the market will depend only on the combination of the economic and financial resources that are the subject of the transaction with those of the acquirer and not on the remaining business of the seller. In this case, the undertakings concerned will be the acquirer(s) and the acquired part(s) of the target undertaking, but the remaining businesses of the seller will be ignored".*

It should be noted, by the way, that the method of calculating turnovers in the case of acquiring control set out in the Act is also not cohesive with the methodology of calculating turnovers which is applicable to acquisitions of another undertaking's assets. In accordance with the Regulation of the Council of Ministers of 17 July 2007 concerning the method of calculation of the turnover of undertakings participating in the concentration[347], in such transactions, the turnover of the seller and its capital group are not taken into account. This means that in certain cases the notification obligation may depend only on the structure of a transaction.

4. FORMS OF TRANSACTIONS

A closed catalogue of transactions which may have to be notified to the competition authority is included in the Act. As regards (i) mergers of undertakings and

345 Cf. Article 5 (2) of Regulation 139/2004.
346 Cf. Article 5 (4) of Regulation 139/2004.
347 Dz.U. of 2007 No. 134 item 935.

(ii) acquiring control over another undertaking, the solutions adopted in the Act are coherent with the Community regulations. Substantial concerns arise, however, in this respect, as regards the two remaining types of transactions referred to in the Act, namely creation of a joint venture by two independent undertakings and acquisition of another undertaking's assets, if the turnover achieved by their assets in the territory of Poland exceeds the equivalent of 10 million euros.

4.1 NOTIFICATION OF CREATING A JOINT VENTURE

Council Regulation No 139/2004 introduces an important division of joint ventures into: (i) cooperative joint ventures where the entities involved intend to create the platform for their future cooperation on e.g. the implementation of a particular research project; and (ii) concentrative joint ventures aiming at the creation of a new entity which, from the economic point of view, will perform all the functions of an independent undertaking. According to the Community law, only joint ventures of concentrative character are considered "concentrations" within the meaning of Regulation 139/2004. As a result, only a transaction envisaging creation of an independent business entity is subject to the notification obligation since only such an entity has the potential to have a real impact on the state of competition on the market. Cooperative joint ventures, on the other hand, are not treated as "concentrations" – they should be evaluated by competition authorities from the perspective of Article 81 of the Treaty establishing the European Community, which bans anti-competitive agreements).

The above differentiation, consolidated also in the European courts' case law, between joint ventures of a concentrative and cooperative character was not reflected in the Polish Act. Consequently, regardless of whether a joint venture created by two or more independent undertakings is of a cooperative character or whether it is strictly concentrative, it needs to be notified to the competition authority if the undertakings concerned meet the relevant turnover thresholds. Some authors refer to telological and functional interpretations pointing out that also under the Polish law it is possible to apply the differentiation adopted by the Community law. Nonetheless Article 13(2) (3) of the Act unequivocally indicates that the intention of the lawmakers was to subject all planned joint ventures, regardless of their character, to scrutiny. This approach is too restrictive and is not justified in light of the Act's objectives.

A procedural issue should also be pointed out here. According to Article 4(2) of Regulation 139/2004, the notification obligation concerns only those participants of a transaction who acquire joint control over the newly created entity. However, under the Polish Act, all entities participating in a joint venture have the obligation to notify it to the competition authority, regardless of the actual level of participation in this undertaking (it does not matter if the applicant has actual impact on the operations of the newly created undertaking). It seems that the obligation of notification should exist only with respect to the entity (entities) which may acquire control over the newly created undertaking, as it is provided in the Community law.

4.2 NOTIFICATION OF ACQUIRING ANOTHER UNDERTAKING'S ASSETS

It is fully justified to make transactions envisaging acquiring another undertaking's assets subject to the notification obligation, since, as the doctrine points out, the effects of such transactions do not differ in the economic sense from the effects of transactions consisting in acquiring control overan undertaking[348]. Acquisition of assets can, in certain cases, constitute a concentration with a Community dimension, which has to be notified based on Regulation 139/2004. According to the Notice, "*the acquisition of control over assets can only be considered a concentration if those assets constitute the whole or a part of an undertaking, i.e. a business with a market presence, to which a market turnover can be clearly attributed*".

Crucial doubts concerning the Act are raised by the wording of the provision regulating the discussed transactions and its reference to the imprecise term " the acquisition of a part of another undertaking's assets". According to Article 13(2)(4) of the Act, what needs to be notified is an intended "*acquisition of a part of another undertaking's assets (the whole or a part of a business), if the turnover achieved by means of the assets in any of the two financial years preceding the notification exceeded the equivalent of 10 million euro in the territory of the Republic of Poland*".

Reference to the term "assets" in Article 13(4) of the Act creates a risk that this provision can be interpreted only from the point of view of Article 44 of the Polish

348 E. Kosiński, (in:) *Ustawa o ochronie konkurencji i konsumentów. Komentarz*, collective study edited by C. Banasiński and E. Piontek, LexisNexis, ed. 1, Warszawa 2009, p. 342.

Civil Code[349] with the omission of the requirement that the assets which are the subject of the transaction should function as an autonomous business on the market. Interpretation of the language of said provision alone can lead to the conclusion that the competition authority should have control over e.g. large-scale purchases of raw materials, or takeover of lease contracts, which are generally fixed-term and can include the limitations on using the object of the lease. The lessee is also not entitled to dispose of the object of the lease. In this context, crucial doubts also arise in connection with the issue of calculating the turnover when the object of the acquisition is e.g. rights resulting from a lease contract, since the lessee does not achieve any turnover from lease contracts concerning real property. It is difficult to assume at the same time that the turnover in the case of a transaction consisting in the takeover of the rights and obligations of a lessee should include the turnover generated by the business operated by a lessee.

Considering the principles of functional interpretation, only transactions consisting in the acquisition of a business, within the meaning of Article 55^1 of the Civil Code [350], or parts of an undertaking, should be subject to the merger review, provided that the acquired part is an organized set of tangible and intangible components of an undertaking, used for the achievement of specific economic objectives. In our opinion, the above position presented in the Guidelines is fully up-to-date under the Act in force. The above interpretation also seems to be cohesive with the general interpretative directive concerning the term "assets" resulting from the Notice. Due to the above mentioned reasons, *de lege ferenda*, the need for making the analyzed provisions of the Act more precise should be considered, e.g. by means of removing the reference to the term "assets" in the discussed provision.

5. CONCLUSION

The aim of the present article was to attempt to outline the problems which appear in connection with applying the provisions regulating the criteria of notifying

349 Property is ownership and other property rights.

350 A business is an organised set of tangible and intangible components dedicated to carrying out a business activity. It includes in particular: 1) identification of the business or its separated parts (name); 2) ownership titles to immovable or movable assets, including equipment, materials, goods and products, as well as other property rights to immovable or movable assets; 3) rights resulting from hire or lease contracts concerning immovable or movable assets, and rights to use immovable or movable assets resulting from other legal staus; 4) receivables, rights from securities and cash; 5) concessions, licences and permits; 6) patents and other industrial property rights; 7) copyright and related rights; 8) business secrets; 9) books and documents connected with operating a business.

intended mergers and to indicate the directions of legislative solutions concerning the notification obligation. This concerns in particular the issues of calculating the turnover, referred to in point 3 of the article, and providing more precise the provisions regulating transactions consisting in the creation of a joint venture and acquiring another undertaking's assets. In both cases applying a functional interpretation of the provisions of the Act does not eliminate the risk of violating the Act.

As regards further harmonization of the Polish law with the Community regulations, what needs to be highlighted is the fact that it is neither required nor possible to ensure in practice that precise legislative solutions adopted in this legislative area are fully convergent with the Community regulations. However, it seems that the solutions concerning the key issues, such as the methodology of calculating the turnover for the purpose of verifying the necessity to notify a transaction or a precise definition of the term "concentration", should be cohesive with the solutions adopted in Regulation 139/2004, which forms part of Polish law.

We assume at the same time that from the point of view of undertakings, who are under the obligation to assess whether a merger which they intend to carry out needs a prior clearance from the competition authority, it would be helpful if the competition authority developed some practical guidelines regarding the issues which do not require detailed legislative regulation, but which raise crucial practical doubts. For example, according to Article 14(4) of the Act, the notification obligation does not cover transactions which are the result of insolvency proceedings, excluding cases when a target enterprise is taken over by its competitor or an undertaking belonging to the same capital group. The Act does not determine unequivocally how the term "insolvency proceedings" referred to in Article 14(4) of the Act should be interpreted, in particular, whether insolvency proceedings carried out under foreign law are also covered by this term. Functional interpretation favours a positive answer to this question and such interpretation of the discussed provision was finally approved by the competition authority in one of its merger cases.[351] It should be noted that in this case the lack of clear

351 Case No DKK-421/8/09/ES, concerning acquisition of control over Parts Holdings France by TowerBrooks Investors Ltd. It resulted from information included in the notification that the acquired undertaking is subject to the so-called securing procedure, considered a type of insolvency proceedings regulated in French law. At the same time, neither the acquiring enterprise nor any of the operating companies of TowerBrook group, to which this enterprise and the acquired enterprise belong, are not competitors within the meaning of Article 4(11) of the Act on competition and consumer protection. Due to the above reasons, the discussed transaction is subject to the exemption from the control of the President of the Office of Competition and Consumer Protection on the basis of Article 14 (4) of the above mentioned Act.

legislative guidelines in this respect lead the undertaking to submit a full merger notification to the competition authority. It seems that publishing guidelines explaining the existing interpretative doubts by the competition authority would crucially contribute to the legal certainty of undertakings intending to implement a merger.

Jarosław Sroczyński

WHEN CAN A MERGER THREATEN COMPETITION?

1. INTRODUCTION

A merger which, generally speaking, means one enterprise acquiring another enterprise, or a specific part of its business, may lead to accumulating considerable economic power in the hands of one entity, thus potentially threatening free competition. Economics assumes that the majority of enterprises (if not all of them) strive for a monopoly within their field of activity.[352] This is why public authorities protecting competition on the market face grave responsibility for monitoring and regulating consolidation processes.[353] Merger control legislation exists in the European Union as well as in the vast majority of EU Member States.[354] A great majority of these regulations are based on the obligation to notify the regulating authority of an envisaged merger before it is performed. Therefore, it is an ex ante control and not an ex post control. Apart from rare exceptions, usually exemptions *ad casu*, if they are at all allowed by relevant legal provisions[355], it is prohibited to carry out a transaction before obtaining formal clearance from the competition authority (early implementation ban). This way when transactions assessed by the competition authority present potential threat to competition, it is possible to implement preventive measures. These include, above all, the prohibition to carrying out a merger, as well as conditional clearance, under which enterprises have to meet conditions imposed by the authority itself or undertake commitments on their own. Conditional clearance may cover the disposal of part of the acquired assets (structural remedies), as well as undertaking or omitting certain actions (behavioural remedies). A transaction may also fail to come to life as a consequence of discontinuation of merger proceedings, which takes place when the parties withdraw their notification, because they do not want, for different reasons, to receive the ban or conditional clearance they expect.[356]

352 See e.g. J. Schumpeter, (1934). *Theorie der wirtschaftlichen Entwicklung*. Tübingen; W. Szpringer (1993). *Łączenie przedsiębiorstw a regulacja antymonopolowa*. Warszawa, p. 11-23.

353 See M. Krasnodębska-Tomkiel, *Urząd przygląda się fuzjom*. forsal.pl. Available at: http://forsal.pl/artykuly/118555,krasnodebska_tomkiel_urzad_przyglada_sie_fuzjom.html (Accessed 12 March 2009).

354 Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings (“Regulation 139/2004”, “ECMR”); Polish Act of 16 February 2007 on competition and consumer protection. Among EU Member States, only Luxembourg does not have legal provisions regulating concentration control.

355 See Article 7, (3) of Regulation 139/2004 and Articles 97 and 98 of the Act on competition and consumer protection respectively.

356 Cases of withdrawing the notification of merger intention, including the so-called “unofficial number” of notifications which

Nevertheless, generally mergers constitute a positive economic phenomenon. Acquiring other enterprises, even competitors, leads to better allocation of capital, reinforcement of positive globalisation processes and, in consequence, it contributes to increased technical development and standardization, as well as widening consumers' access to products[357]. Mergers constitute a measure for counteracting emergency situations that may occur within an enterprise, the entire sector, as well as the whole economy on a macroeconomic scale. Therefore, the intervention of a competition authority with relation to merger transactions, which are based on the basic principles of freedom of concluding agreements and disposing of ownership, should be a cautious and considered process, in order to minimise the risk of issuing a wrong decision.[358]

In the present article, I discuss the basic analytical tool which is used by competition authorities in assessing mergers from the point of view of their effects on competition, that is the test evaluating the significant impediment of effective competition, referred to as the SIEC test. A positive result of the SIEC test, indicating that the envisaged merger will significantly impede effective competition, signifies that it is necessary to block it by issuing a prohibiting decision. On the other hand, a negative result of the test means that parties shall receive a clearance, either unconditionally or conditionally, when eliminating the significant impediment of effective competition is dependent on fulfilling specified conditions.

Limited space makes it impossible to discuss issues which constitute an intrinsic part of the process of assessing mergers and issuing merger decisions by competition authorities. These issues include the above mentioned remedies, especially their legal nature and implementation procedures, as well as ancillary restraints related to mergers. They also include restitution measures (dismantling, unwinding) applied to transactions which have already been implemented. Such measures consist in re-establishing competition on the market so that the SIEC test requirements are met ex post. Moreover, this paper does not cover the issue

were abandoned due to a negative initial assessment carried out by the parties, should be taken into consideration when analysing effects of blocking provisions on merger control. The widespread opinion is that the anti-trust authorities issue many prohibiting decisions (e.g. European Commission from 1999 – 20, UOKIK from 1998 – 10). However, the number of withdrawn or abandoned notifications should also be taken into account. Studies carried out by Deloitte in 2007 at the request of the UK Office of Fair Trading (OFT) show that for each prohibiting or conditional decision issued by OFT there are five mergers which were either abandoned or modified by the parties themselves (cf. http://www.oft.gov.uk/shared_oft/reports/Evaluating-OFTs-work/oft962.pdf).

357 A. Fornalczyk, *Biznes a ochrona konkurencji*, Kraków 2007, p. 137-139.

358 This concerns the so-called Type-1-Error, i.e. situations in which a merger which should not (did not have to be) prohibited, was banned, and Type-2-Error, i.e. situations in which the merger consent was issued, although it should not be.

of merger assessment based on criteria which are not directly connected with competition on the market, such as individual or sector protection and socio-economic objectives.[359] A systemic approach of competition authorities to the assessment of mergers during the global economic crisis can also be a topic for a separate analysis.[360]

2. A MORE ECONOMIC APPROACH TO COMPETITION LAW

The introduction of the SIEC test is the consequence of a tendency described as "a more economic approach to competition law".[361] It basically consists in replacing the dominant position test, (DPT) which is mainly carried out formally, or even mechanically, on the basis of the criterion of dominant position with a test which includes a number of criteria concerning purely economic effects of the envisaged merger on effective competition on relevant market. To put it in a more graphic way, a more economic approach means that the "driver's seat in the vehicle regulating competition" was taken by the economists, whereas lawyers moved to "the backseat".

The concept of economic approach developed in the USA in the 1990s, especially during the second half of the decade, in the form of the so-called SLC test (substantial lessening of competition). The shortcomings of an approach concentrating solely on the criterion of dominant position had been revealed in several merger cases carried out by American competition authorities, where potential anti-competitive effects in the form of the so-called uncoordinated, unilateral effects were discovered. A case which should be briefly described in this context is the Heinz/Beech-Nut merger.[362] The merging enterprises were the first and the second largest producers of baby foods in the USA. They competed against Gerber, which held a dominant position on the market with around 60 percent market share. It would, therefore, seem that the merger would counterbalance the market

359 This mainly concerns state authorities' intervention into merger processes. See Commission Decision on the concentration of Dutch banks Fortis Bank/ ABN AMRO (Decision No COMP/M.4844 of 3 October 2007). The intervention may be in the form of a special act issued in order to prevent bankruptcy, as it was in the case of Alitalia/Air One merger in Italy, or to maintain the stability of financial system, like in the case of Lloyds TSB/ HBOS, a merger of British banks. In the Act on competition and consumer protection, the possibility to accept a merger on the basis of such non-competitive factors like economic development or technical progress was introduced in Article 20 (2).

360 The subject has been discussed during international seminar "Current Issues in Merger Enforcement" organised by UOKIK in Warszawa on 29 October 2009 in the framework of 20th anniversary of the Office. Cf. http://www.20lat.uokik.gov.pl/warsztaty-o-fuzjach-w-warszawie

361 K. Kohutek, *Tendencje do większej ekonomizacji prawa konkurencji* (in:) K. Kohutek, M. Sieradzka, *Ustawa o ochronie konkurencji i konsumentów, Komentarz*, Warszawa 2008, p. 68.

362 FTC v. H. J. Heinz Co. 246 F 3d 708 (2001), the so-called Baby Foods case.

power of the dominant enterprise (Gerber) and the DPT test would automatically result in the competition authorities clearing the transaction. However, after closer analysis it turned out that there were fundamental differences in the brand perceptions on the part of buyers. Gerber was an unchallenged leader as regards brand image, due to which sellers were always willing to have a considerable stock of Gerber products, whereas Heinz and Beech-Nut were forced to pay slotting fees for displaying their products on store shelves. The potential merger consent would eliminate head-to-head competition between Heinz and Beech-Nut as the second choice suppliers. After the merger, the new entity would be able to operate similarly to its largest market rival, Gerber, that is it could limit supply and raise prices. Sellers who would want to continue to offer more than one leading brand, would have to agree to conditions of a *de facto* monopolist entity, although it formally would not even have a dominant position on the market. The *Baby Foods* case revealed that merger assessment criteria which are based solely on dominant position may turn out not flexible enough in cases which require taking into consideration additional economic factors (in this case brand loyalty, that is consumers' attachment to a brand, as well as competition between brands[363]).

At the beginning of the 2000s, the discussion on the necessity for "a more economic approach" reached Europe. The debate that followed was not easy and the concept of "a more economic approach" initially had difficulties in making its way through the Community legislation.[364] There were reservations about introducing an assessment mechanism based mostly on criteria which were not precisely defined. What was also important was the insufficient personnel capacity of the Directorate General for Competition, which at that time lacked qualified economists specialising in the competition domain. With time, such barriers were surmounted and initial reservations overcome.[365] When Regulation 139/2004 entered into force, the SIEC test became binding in the enlarged, as of 1 May 2004, European Union.[366] Parallel changes also took place in the majority of Member

363 The criterion of brand loyalty has been applied in a recently issued decision of the President of UOKIK prohibiting merger on national markets of trading powdered whipped cream, instant cakes, dessert topping, baking powder, vanillin sugar, baking soda and cooking essences (case Rieber Foods Polska/FoodCare, decision of the President of UOKIK of 8 October 2009, no DKK-68/09).

364 See Green Paper on the ECMR (2001); G. Monti (2007). *EC Competition Law*, Cambridge University Press, p. from 258; J. Basedow (2007), *The Modernization of European Competition Law: A Story of Unfinished Concepts*. *Texas International Law Journal*, 42(3), p. from 433; T. Skoczny discusses evolution of competition tests in merger assessment on the basis of the Act on competition and consumer protection, (in:) T. Skoczny, A. Jurkowska, D. Miąsik (2009), *Komentarz OKIKU*. Warszawa, before article 18, Nb 4-19.

365 In 2003, the position and team of the Chief Economist was created at DG COMP. In 2001, the Department of Market Analyses was created at UOKIK. It participates in the decision process connected with merger control.

366 See Article 2(2) and (3) of Regulation 139/2004, according to which the Commission shall issue approval for a merger which

States, including Poland. The Act on competition and consumer protection of 15 December 2000, amended in 2004, introduced the SIEC test into Polish legal system. The test was adopted in its original form by the Act on competition and consumer protection that is currently in force.[367]

3. THE SIEC TEST

Detailed criteria for applying the SIEC test were formulated by European Commission in two documents of fundamental significance: the so-called Horizontal Guidelines[368] and Non-horizontal Guidelines (vertical and conglomerate[369]). Respectively, they concern mergers between competitors (which, obviously, can influence the state of competition), and mergers which take place between enterprises whose relation is vertical (e.g. a producer acquiring the distributor of his own products) or conglomerate mergers (e.g. a merger of producers of two different products which are, nevertheless, usually purchased by one customer). Both sets of guidelines constitute an extensive instructive and analytical material, and determine the methodology to be used by the Commission (and surely also national authorities) in assessing mergers which are potentially threatening to competition. Therefore, the guidelines are highly significant for competition law enforcement.[370]

4. ANTI-COMPETITIVE EFFECTS OF MERGERS

A merger's possible anti-competitive effects may be generally divided into uncoordinated and coordinated effects. Uncoordinated effects consist in increasing an enterprise's market power as a result of the merger and in eliminating previously existing limitations stemming from competition. In some measure, the process takes place spontaneously, without the necessity to coordinate actions with other enterprises. On the other hand, coordinated effects are connected with the change in the nature of market rivalry – after the merger, enterprises are more willing

does not significantly impede effective competition in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position.

367 See Article 18 of the Act on competition and consumer protection which stipulates that the President of the Office shall, by way of decision, issue a consent to implement a merger, which shall not result in significant impediments to competition in the market, in particular, by the creation or strengthening of a dominant position in the market.

368 Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, OJ C 31, 5.2.2004.

369 Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings, OJ C 265, 18.10.2008.

370 See T. Skoczny, op. cit., Article 18, Nb 24-32.

to coordinate their market activities and restrict competition, also by raising prices. In the case of enterprises which have been already coordinating their market activities, the merger may facilitate, stabilise or increase the effectiveness of such coordination.

The lack of uncoordinated effects analysis was the basis for overruling the decision of the European Commission by the Court of First Instance in the case of *Airtours*.[371] The Commission prohibited a merger between two competing tour operators, which, as a result of the transaction, would become the leader on the British market, with a ca. 35 percent market share. The European Commission decided that the new market structure would strengthen the key players' collective dominance. This argument was overruled by the Court, which emphasised that the relevant market in not transparent enough for the competitors to be able to mutually monitor their behaviour and coordinate it with due precision and speed.

The Horizontal Guidelines did not exhaust the inventory of the most important factors contributing to the fact that as a result of a merger significant uncoordinated effects may arise, leading to the merger being incompatible with the single market. These are factors that could be defined as inherent, because uncoordinated effects arise in a way from their very essence. They include: large market shares, close substitutability of products and the lack of alternative suppliers.[372] The second group comprises factors which need to be verified in detail by means of economic analysis before one can conclude that they might lead to uncoordinated effects. That is why, such factors can be defined as empirical ones. Among them, there is simulation of competitors' behaviour in a situation where enterprises increase prices after the merger. If competitors have sufficient production capacity and they believe that increasing production will be profitable, it is unlikely that the potential increasing of prices after the merger will be durable. Thus, the merger cannot cause damage to effective competition. The second factor is the merger's influence on the development of competition. Other factors in this category are the level of control over raw materials' supply and the distribution network's development. What would also have to be considered are the blocking effects of patents, trademarks and other intellectual property rights, as well as the

371 Case T-342/99, Airtours v Commission of the European Communities, [2002] ECR II-2585, paragraph 62.

372 The so-called Herfindahl-Hirschman Index (HHI), which is the sum of the squares of the market shares of enterprises operating on relevant market, exceeds in such cases the level of 2,000 points, and the increase in concentration level after it has been performed (Delta coefficient) exceeds 150 points. In some countries (Brazil, Japan, Germany) the so-called concentration ratio (CR) is also used. For example, in Germany the presupposition of an oligopolistic dominance is made when the CR3 indicator surpasses 50%, and the CR5 indicator exceeds 66.6% (they concern relevant market shares of three and five largest enterprises respectively).

interoperability of different infrastructures and platforms (e.g. within electricity or telecommunications networks).[373] Another empirical factor is the possibility of weakening and reducing the dynamics of competitiveness, for example as a result of a merger of two important innovators whose products belong to a distribution chain connected with a given product market.

5. ASSESSMENT OF THE EFFECTIVE MARKET POWER

Based on empirical analysis, we may conclude that in certain circumstances acquiring a market share even bigger than 40 percent, i.e. when it is assumed that an enterprise is holding a dominant position, actually does not lead to obtaining a dominant position[374] or, in a more general sense, will not cause a significant limitation of effective competition. The analysis performed by the Polish competition authority with relation to the case of *Boiron/Dolisos* merger may constitute a good example.[375] The case concerned acquiring a homeopathic remedies producer (Dolisos) by its larger competitor (Boiron). Their total market share, amounting after the merger to several percent, would suggest the presence of a strong dominant position. Although homeopathic medicines cannot entirely substitute allopathic (non-homeopathic) medicines, the analysis performed showed that sellers of homeopathic medicines faced the barrier of homogenous purchasing power on the part of medicinal products' buyers, which is limited irrespective of the medicine's type (homeopathic or allopathic) and, to a certain degree, irrespective even of the given medicine's use. Therefore, the real power of the enterprise to independently raise prices after the merger was assessed as minimal and the competition authority was able to clear the notified transaction.[376]

6. OTHER TOOLS TO ASSESS MERGERS

Coordinated effects stemming from horizontal mergers will be connected with the possibility of creating or strengthening collective dominance. Economic analyses devoted to the occurrence of coordinated effects should take into account many different factors such as: the market's maturity, stagnation or moderate increase

373 See E. Piontek, (Ed.) *Nowe tendencje w prawie konkurencji UE*, Warszawa 2008, p. from 261.

374 Article 4(10) of the Act on competition and consumer protection. See E. Piontek, and C. Banasiński, (eds.), *Ustawa o ochronie konkurencji i konsumentów*, *Komentarz*, Warszawa 2009, p. 360.

375 Decision of the President of UOKIK of 13 January 2006, DOK-3/2006, available at the website www.uokik.gov.pl in the database: Judgements of the President of UOKIK (Orzecznictwo Prezesa UOKiK).

376 This approach is consistent with the European Commission's methodology of assessing cases of the so-called countervailing buyer power (cf. points 64-67 of horizontal Guidelines).

in demand and its price flexibility, product homogeneity, similar cost structure between enterprises, similar market shares, lack of technological innovations and the advancement of the technologies applied, lack of capacity to increase outputs, high barriers to entry, lack of countervailing buyer power, lack of potential competition, different kinds of informal relations between enterprises, lack or limitation of price competition and the possibility to apply retaliation mechanisms.[377] However, it should be underlined that not all factors will have the same importance when assessed by the SIEC test. What is decisive in this context is a given relevant market's specificity, which will determine the hierarchy of factors which are the most important from the point of view of assessing the anti-competitive effects of the analysed merger.[378]

Competition evaluation of horizontal mergers will also take into consideration barriers that hinder potential competitors from entering the market (such as legal or financial barriers or the above mentioned brand loyalty). The issue of increased efficiency and improved conditions for development and living standards in the Community as positive effects of mergers (the so-called efficiencies) a separate topic for analysis. However, at the same time, these effects also have to be beneficial for consumers[379], merger-specific and verifiable. Furthermore, Horizontal Guidelines allow enterprises argue that a clearance is justified due to the involved enterprise's probable bankruptcy (failing firm defence). Here, the basic requirement is that the deterioration of the state of competition which occurs after the merger is not perceived as the result of the merger. The three basic assessment criteria applied by the Commission in this case are: the requirement that in absence of merger, the failing firm is indeed forced out of the market in a short period of time because of its financial difficulties, that there are no other, less anti-competitive alternatives to the merger and that, in the absence of the merger, the assets of the failing enterprise would inevitably exit the market.[380]

377 Decision of the President of UOKIK of 15 February 2006 on mobile phone network operators, DOK2-073-30/05/MKK. The decision states that three mobile phone operators functioning on the Polish market at that times (Era, Orange, Plus) held (but not abused) a collective dominance. Despite the fact that the President of UOKiK performed the analysis for the needs of proceedings conducted by the President of the Office of Electronic Communications on the basis of Telecommunications Law, described decision is essential for the practice of defining, on the basis of economic criteria, collective dominance within anti-trust law.

378 See *Chapter 4 – Coordinated Effects Analysis Under International Merger Regimes*, (in:) J.F. Rill, J. M. Taladay, A. Norton, J. Oxenham, M. Matsushita, F. Montag, A. Rosenfeld, *ICN Report on Merger Guidelines*, Seoul 2004, p. 10.

379 For more information on this matter see D. Miąsik, *Controlled Chaos with Consumer Welfare as the Winner – a Study of the Goals of Polish Anti-trust Law*, "Yearbook of Anti-trust and Regulatory Studies", Warszawa 2008: CSAiR, vol. (1), p. 49-52, with discussed judgements of the Court of Competition and Consumer Protection as well as the Supreme Court.

380 See K. Kohutek, op.cit., p. from 532.

The Non-horizontal Guidelines define foreclosure as the basic uncoordinated effect influencing the merger evaluation. Foreclosure becomes a fact if a merger is likely to restrict or block the access of its actual or potential competitors to the means of production or markets. Limiting the access to the means of production by a vertically combined enterprise may constitute a threat to competition if it concerns a means of production that is important from the point of view of the downstream market. Foreclosure is possible especially when the remaining upstream market suppliers are less efficient, face capacity constraints or decreasing returns from economies of scale. Exclusivity contracts can also be restricting in nature because they block access to the means of production. The incentive to foreclose competitors will depend on the extent to which the downstream units of the merged enterprise can be expected to benefit from higher price levels on that market as a result of adopting the strategy to raise competitors' costs.

The SIEC test, used in assessing non-horizontal mergers, will also partially include the market parameters which are studied in the case of horizontal mergers. Therefore, the elements analysed will include barriers to entry, downstream market buyer power, efficiencies relating to the merger, investment incentives, etc. This also concerns, to a large extent, the assessment of potential coordinated effects.

Vertical mergers may also engender restricted access to customer base which may occur when a supplier integrates with its important customer on the downstream market. Subsequently, this may lead to increases in prices of the means of production (the spillover effect). Conglomerate mergers will require, among other things, to be analyzed from the point of view of the foreclosure effects of tying and bundling, factors concerning the functioning of sales network and the role of the so-called "must stock" branded products.[381]

7. CONCLUSION

In conclusion, this short review of the basic issues concerning merger assessment with relation their market effects, including both the pro-competitive and the anti-competitive ones, shows that the introduction of the SIEC test opened new, broad perspectives to economists dealing with competition. It seems that in the

381 See e.g. case COMP/M.3732 – Procter & Gamble/Gillette (2005) in which the European Commission analysed market effects of the merger with relation to the whole range of products deemed "must stock" brands. Consumer demand for such products (brands like Ariel, Always, Pampers, Oral B, Duracell) is spontaneous in nature, that is why they constitute an attractive, even mandatory element each retailer's offer.

upcoming years, merger control will be performed on the basis of economic tools, which generally has not been the case for far.[382] These tools include, are above, all econometric instruments which make it possible to conduct studies on, for example, the extrapolation of trends while analysing markets of time relevance. Merger efficiencies may be measured by means of methods used to minimize empty mileages in the domain of transport. Estimations can be performed by creating appropriate econometric models. Other statistical tools such as game theory or time series analysis, including, for example, the probability distribution of concrete merger effects, may also be used.

382 See L.H. Röller (2005), *Economic Analysis and Competition Policy Enforcement in Europe*, (in:) Peter A.G. van Bergeijk and Eric Kloosterhuis (eds.) *Modelling European Mergers: Theory, Competition Policy and Case Studies*, Edward Elgar Publishing Limited, p.19; E. Jantoń-Drozdowska (2007), *Ekonomiczne przesłanki antymonopolowej oceny koncentracji*, (in:) C. Banasiński i E. Stawicki (eds.), Konkurencja *w gospodarce współczesnej*, Warszawa, p. 279-285; C. Bongard, D. Möller, A.Raimann, N. Szadkowski, U. Dubejko (2007), *Instrumenty ekonomiczne w prawie konkurencji*, Bonn/Warszawa: UOKiK, p. 37-48.

Walter A. Stoffel

INTERNATIONAL MERGERS: SWISS EXPERIENCE

1. INTRODUCTION

International mergers in Switzerland bring up questions on the relationship between competition policy and international law as well as specific problems linked to the special legal situation of the country in the European context. The principles of the modern legal control mechanisms in the filed of merger control are not disputed anymore, but their implementation in specific transnational settings often is a matter of concern for both the competition agencies and the merging companies.

Switzerland has a population of 7.5 million, compared with the 450 million of the European Union. Twenty percent of the Swiss population are foreign nationals; about a quarter, almost 25 percent, were born abroad. About half of the country's GDP is earned in foreign trade. It is not surprising that international mergers in such circumstances are the rule rather than the exception.

2. GENERAL CHARACTERISTICS OF THE SWISS LAW ON MERGER CONTROL

Two problems exist with respect to cross-border mergers, the substance of the test to be applied, the procedure and implementation of merger control. This piece shall concentrate on the jurisdictional problems, and only briefly mention the aspect of assessment.

2.1 JURISDICTION

Competition law was one of the first areas which gave raise to the application of market rules with respect to companies which did not have their seat within the territory of the State that enacted and applied these rules. The problems were first discussed under the heading of the "extraterritorial" implementation of antitrust law. Today, we generally refer to the notion of "effects doctrine." In Europe, the leading case is the *Wood Pulp* decision,[383] in which the European Court of Justice

383 E.C.J. 27.9.1988, Cases 89, 104, 114, 116, 117 and 125-129/85, A. Ahlström Osakeyhtiö et al. All the wood pulp manufacturers were established in Sweden, Canada, the US and Japan. The Commission investigated the case under Art. 81 (then Art. 85) ECT and fined all the parties of the cartel. The ECJ did not expressly mention the "extra-territorial" effects doctrine, but relied on the very territoriality principle, underlining that restriction of competition was "implemented" within the Common Market. The result is the same.

upheld a fine against wood pulp manufacturers who had concluded a price fixing and market sharing agreement for their imports into the (then) Common Market, despite the fact that all the parties to the cartel had their seat outside of the EU. Similar decisions exist in Switzerland.[384]

The "effects doctrine" thus translates a mutual international acceptance of the right of each State to organize the market, if necessary by coercion, which in turn implies physical presence. Since a company is normally considered to be based at its (legal) seat, a transaction is deemed domestic when the headquarters of merging entities lie within the State, and multinational when at least one of the seats of the parties is outside of the State of the deciding agency. For obvious reasons, small countries are more often confronted with international concentrations than larger economies.[385] Although they have jurisdiction over these transactions, according to the effects doctrine, they are not necessarily best placed to look into all of them.

Concentrations in small economies pose basically the same problems as mergers everywhere. But in addition, they often have effects which go beyond the territory of the country. Legislators and agencies may be tempted to apply specific standards to such domestic mergers, taking into consideration the strength that the (new) inland firm will gain in international markets, possibly at the detriment of the home market structure.

2.2 ASSESSMENT

For the assessment of a concentration, Swiss law imposes on the agency a test which defines dominance as a position that enables the undertaking to *"[behave], as regards supply or demand, […] in a substantially independent manner with regard to the other participants (competitors, suppliers or customers) in the market"* (Art. 4 par. 2 LCart). This is a flexible wording, which leaves room for a reasoning based upon the market structure as well as for an analysis of the conduct of the companies.

384 See in particular: Swiss Federal Court in the *Merial-case*, 24.4.2001, BGE/ATF 127 III 219 ff., below C.2.a. In the field of arbitration, a judgment rendered by the Swiss Federal Court in 1992 required an arbitral tribunal to take European competition law into consideration (Swiss Federal Court, 28.4.1992, BGE/ATF 118 II 193 ff., English translation in 18 Yearbook of Commercial Arbitration 1993 143).The Federal Tribunal held that the arbitrators had to take into account Art. 81 (then Art. 85) ECT for judging the validity of the contract; it considered it to be "normal" to apply the ECT to the undertakings which had their seat within the Common Market. A recent judgment now seems to back away from this holding, at least in part (Swiss Federal Court, 8.3.2006, BGE/ATF 132 III 389 ff.), but in fact, the decision is limited to the refusal to review (not to the fact that competition law is applied).

385 Cf. Competition Law in Small Economies, Report presented at the 8th Annual Conference of the International Competition Network, Zurich 2009.

The Law states, in addition, that the competition authority shall intervene when a merger creates an undertaking which fulfils this independency standard:

> *Article 10 par 2. Assessment of concentrations of enterprises*
>
> *The Competition Commission may prohibit the concentration or authorize it subject to conditions or obligations if it transpires from the investigation that the concentration:*
>
> *a) creates or strengthens a dominant position liable to eliminate effective competition, and*
>
> *b) does not lead to a strengthening of competition in another market which outweighs the harmful effects of the dominant position.*

This provision is based on a classical dominance test. However, the legislator added that the creation or strengthening of a dominant position must be *"liable to eliminate effective competition"*. The courts have interpreted the provisions in a very literal sense. It was considered, in two important cases, that this standard was not met, since competition was limited, but not eliminated, and the court struck down the interventions of the Swiss authority.[386] The reasoning did not pay much attention to the *effectiveness* of the remaining competition, as the law in principle requires. The decisions were criticised, and an evaluation report published in 2009 proposed to modify the legal standard and to adjust it to the European model.[387] For the time being, however, the Swiss dominance test remains and erects a high barrier, indeed, for interventions in the field.

In addition to the dominance test, the provision obliges the agency to take into consideration pro-competitive effects of the merger on "other" markets than the relevant one. The term "other" refers also to foreign markets. Part 4 of the article makes the point clear:

> *In assessing the effects of a concentration of enterprises on the effectiveness of competition, the Competition Commission shall also take into account market developments and the situation with regard to international competition.*

386 Federal Tribunal (2A.325/2006), February 13th, 2007, "Swissgrid", RPW/DPC 2007 p. 324; Federal Tribunal (2A.327/2006), February 22th, 2007, "20 Minuten", RPW/DPC 2007 p. 331.

387 Evaluation in accordance with Art. 59a LCart, Report of 2008, (in:) Annual Report 2008, RPW/DPC 2009 p. 45ss, 55.

This *"international markets-provision"* was and still is politically important. The parties invoke it quite routinely before the Swiss authority. But the practical bearing of the provision is not as important as could be expected. Indeed, the general analysis made by the agency already takes into consideration the international aspects and defines the markets accordingly.

Besides the high threshold for intervention, the substance of merger analysis made by the Competition Commission does not differ significantly from general standards. There is more need and more room for specific standards in the area of procedural mechanisms of merger control.

3. GROUNDS FOR JURISDICTION AND NOTIFICATION THRESHOLDS

There are three grounds for jurisdiction in the field of merger control. They are based on the *effects-principle,* in the above sense,[388] although not all of them have the same support in the competition community. The grounds are:

- *Turnover thresholds:* The intervention takes place whenever certain thresholds measured in annual sales turnovers are reached, irrespective of the possible effects of the merger on competition. This criterion is very rough and often overreaching (sometimes under-reaching), but easy to apply.

- *Structural criteria:* In this case, the jurisdiction is based on the degree of organisational integration (existence of branches or subsidiaries) of one, or both of the merging companies in the market of a given State; this criterion is based on physical presence.

- *Effect on competition:* This criterion calls for a scrutiny only when the transaction has potentially harmful effects on the competition in the given State. This factor is targeted at the final aim of the merger control regime. It is well justified by its substance, but difficult in practise because harder to foresee for the merging parties.

The practical bearing of the criteria depends on the mode of operation used to bring into play the merger control mechanism, particularly on the existence

388 Above 2.1

of a notification regime. If an obligation to notify exists, and if it is coupled with a prohibition to realise the transaction before clearance, the project can only go on, if at all, after a certain time. But there is legal certainty after this period, which is the main reason why the OECD and ICN standards of best practice in merger policy favor mechanisms based on turnover thresholds.[389] If the obligation to notify is not coupled with a prohibition to close, the project can go on, but the concentration may be forbidden afterwards. This is a source of uncertainty, at least at first glance. The same applies when there is no obligation to notify, but the agency can (and must) intervene against a merger with adverse effects on competition, on the basis of its monitoring of the market, or of third party information.

The problem of legal uncertainty in a system without mandatory notification may be mitigated if the scheme is coupled with a voluntary notification regime.[390] In Canada, for instance, parties who choose to notify will receive – if there is no challenge – a *"no action"* letter advising that *"there are not sufficient grounds at this time to initiate proceedings"*.[391] There is a similar system in the UK.[392] Voluntary notification does not guarantee legal certainty, but may provide some comfort, often sufficient in practise. The Australian legislation went one step further by instituting an *"authorisation process"* that allows the parties to trigger off an investigation through a pre-completion, fee-based application, and to receive at the end of the process a decision which will be binding.[393]

4. THE SWISS THRESHOLDS AND ITS EFFECTS

4.1 FORMAL TURNOVER THRESHOLDS

Switzerland has adopted the turnover threshold model, coupled with an obligation to notify and a prohibition to proceed. The system is the same as in the EU.

Article 9 par. 1: Notification of concentrations

389 OECD (1999) Report on Notification of Transnational Mergers, Paris; ICN Recommended Practices for Merger Notification Procedures (www.internationalcompetitionnetwork.org/ mnprecpractices.pdf).

390 Cf. William Rowley, Roundtable Presentation, as well in a larger sense: International Mergers: The Problem of Proliferation, (in:) International Antitrust Law & Policy, 2006 Annual Proceedings of the Fordham Competition Law Institute, Huntington 2007, p. 297-317.

391 Sec. 123 Competition Act.

392 Cf. in detail OFT Mergers – Procedural guidance, p. 8 ff.

393 Sec. 94 and 50 Trade Practices Act.

> *The Competition Commission must be notified of concentrations of enterprises before they are carried out when, in the last accounting period prior to the concentration:*
>
> *a) the enterprises concerned reported joint turnover of at least 2 billion Swiss francs or turnover in Switzerland of at least 500 million Swiss francs, and*
>
> *b) at least two of the enterprises concerned reported individual turnover in Switzerland of at least 100 million Swiss francs.*

These thresholds are formal and once they are reached, each and every merger must be notified, irrespective of the seat of the parties and the possible effects on competition.

The principle has been applied quite thoroughly in practise. The early *Merial* case tested it before the Federal Tribunal (the Swiss Supreme Court). The concentration involved a Swiss joint venture put up by two foreign companies with a turnover well over the 2 billion. The transaction itself concerned a small market of less than 100 million, but the sales into Switzerland of the two parent undertakings exceeded this limit by far. The matter was decided by the Federal Tribunal in the sense of a formal turnover requirement.[394]

The result is a relatively far reaching notification regime. It catches not only joint ventures in Switzerland with a turnover of less than 100 million, like in the Merial case. It embraces also *foreign* joint ventures, with no activity whatsoever in Switzerland, if the parent companies fulfil the condition of a worldwide turnover of more than 2 billion and have substantial sales into the country. Thus, a mineral water joint venture in Indonesia, put up by *Nestlé SA* and the *Coca Cola Company,* had to be notified.[395] The Commission was hesitating in this case, but it came to the conclusion that the *Merial* judgment could not be construed in a different way.

In today's notification practise, concentrations of this kind, i.e. transactions without any structural integration in Switzerland, are not rare. They represent about one third of the merger cases in a given year.[396] Foreign international transactions thus constitute a considerable workload for the parties and the agency, even if the cases are routinely cleared within the first month.

394 Federal Tribunal, April 24, 2001, "Merial", BGE/ATF 127 III 219 ff.

395 Cf. Annual Report 2009, RPW/DPC 2010/I (forthcoming); (unpublished decision).

396 Cf. for details: Walter Stoffel, Internationale Fusionen, (in:) R. Zäch (ed.), Schweizerisches Kartellrecht, Revision und Praxis, Zurich 2002,pp. 85-111.

The legislator was aware that the criteria chosen could be far reaching. As a matter of fact, a solution requiring a structural integration had been discussed before parliament.[397] However, it was finally rejected. Part of the reason was the fear to apply the structural elements in practise. More importantly, the legislator thought that high thresholds would make up for extensive pick-up criteria and alleviate an otherwise quite burdensome system. Yet the solution created another problem.

4.2 HIGH THRESHOLDS COVER MOSTLY INTERNATIONAL MERGERS

As pointed out, the turnover thresholds are high for a small economy: a total turnover of CHF 2 billion worldwide or of CHF 500 million within Switzerland, and a turnover of CHF 100 million realised in the country by at least two of the concerned undertakings.

They are not defined in the same way as in the European Union and cannot be compared exactly with the EU-figures. But by and large, the thresholds amount approximately to a half of the European levels.[398] This is very high, if put into relation with the difference in population (7 million as opposed to 450 million residents). In the practical application, it often leads to double control on the one hand, and to no control on the other.

The first consequence is double control. Most large transactions are embraced by the EU thresholds and by the Swiss limits as well. Indeed, there are only a few mergers big enough to fall under the Swiss notification scheme, but too small to be notified in Bruxelles as well. This means that most concentrations are caught by both systems.

The result is not very satisfactory. The legal framework prevents the Competition Commission to do much about it at this point. A formal coordination would of course be possible, but it would need a "bilateral" agreement which is lacking for the time being.

However, several possibilities in the practical application exist and are used.

397 Cf. for details: Walter Stoffel, Internationale Fusionen, (in:) R. Zäch (ed.), Schweizerisches Kartellrecht, Revision und Praxis, Zurich 2002, p. 94 f.

398 The comparison is not easy because of the system of multiple thresholds in the EU (Council Regulation [EC] No 139/2004 of 20.1.2004 on the control of concentrations between undertakings [EC Merger Regulation]), Art. 1. Simplifying somewhat, it is probably appropriate to compare the Swiss figures with the second European threshold.

They concern the substance of the control as well as the procedure:

- The Competition Commission limits its investigation to the "Swiss" aspects of a merger. It does not look into the entire problem. That means of course that it will accept the outcome of the investigation made elsewhere (mainly in Bruxelles). In turn, the Swiss agency expects, and sometimes requires formally, that the parties will apply possible remedies imposed or accepted in Switzerland as well.

- This approach is pragmatic, and requires practical cooperation from the parties. That means mainly that the notifications be synchronized and that the parties agree that the agencies concerned work together.

This way of operation is communicated and known by the competition community. The system seems to work quite satisfactorily.

4.3 HIGH THRESHOLDS LEAVE MANY INTERNAL MERGERS WITHOUT CONTROL

The second consequence is more troublesome. The high thresholds do not identify numerous concentrations which are potentially harmful for domestic markets. The construction industry may serve as an example.

A recent inquiry into the construction of the new tunnels through the Alps has shown the situations which can develop in such markets.[399] A Swiss undertaking active in the production and sale of an important construction material holds a market share in Switzerland of about two thirds. All its competitors, with the exception of two of them, are small companies. Calls for offers for the supply of the material in question were made periodically, throughout the duration of the construction of the tunnels. It appears in hindsight, that small competitors were able, from time to time, to obtain important contracts. The businesses completed the orders, but sooner or later, they were bought by the market leader and found themselves integrated in this larger undertaking. The market share of the dominant entity thus continued to grow steadily.

399 Competition Commission, Recommendation of June 18th 2007 „Beschaffung von Zement und Beton für Grossprojekte, beruhend auf den Erfahrungen bei der Neuen Eisenbahn-Alpentraversale (NEAT)".

All these concentrations went unnoticed. It is possible that they would have been cleared anyway, notably because the industry as a whole underwent a restructuring. But it is this kind of mergers that antitrust agencies in small economies have to examine with particular attention. The turnovers may be relatively low, but foreign competition does not exercise an appreciable disciplinary effect in these markets, precisely for this reason.[400]

High thresholds, therefore, deprive the authority of a possibility to look into such mergers although they can be of a considerable importance in their markets. Lower thresholds would allow control, but would at the same time catch many more international transactions which are not problematic.

4.4 A VOLUNTARY NOTIFICATION REGIME?

It appears, therefore, that States like Switzerland should not use high turnover thresholds. Firstly, because large mergers are always scrutinized in large jurisdictions, and the agency of a tiny jurisdiction does not have many possibilities of intervening here. Secondly, and more importantly, high thresholds leave small internal concentrations without any control. A transaction which escapes such a regime may be quite detrimental to competition, but cannot be examined at any stage, not even at a later date, because the turnover thresholds leave no room for an effects-based assessment, once the time period for control has elapsed.

The problem of embracing too many mergers could be dealt with by combining the existing turnover thresholds with an additional, (much) lower one to be realised within Switzerland. Under such a regime, an examination of an international transaction would only take place if the concentration had a sufficient connection, based on turnover figures, within the country.[401] The solution would avoid catching too many projects. It would thus resolve a part of the problem only, leaving without an answer the more important question of uncontrolled internal mergers.

However, a merger control system based on the criteria of harmful effects, as described above,[402] would be able to deal with both aspects of the problem.

400 See now also a recent merger project in the particular market of artificial insemination of cattle (Annual Report 2009, RPW/DPC 2010/1 [forthcoming]). The market was small, but the concentration would have been very high; the project was eventually abandoned by the parties.

401 The proposal was made by Franz Hoffet at the "Freiburger Kartellrechtstagung" on September 19, 2008 in Fribourg.

402 Above 3.

Under such a rule, scrutiny would only take place where harmful effects exist, but it would always be applied when this is the case, irrespective of turnover considerations. The problem of catching too many mergers would be avoided as well as the one of leaving internal transactions without any control. The possible shortcoming for the agency as regards obtaining the necessary information in time and the problem of uncertainty could probably be overcome:

- Regarding the timely and adequate information, the agency in a small jurisdiction will normally be able to sort out potentially harmful mergers on the basis of its every-day observations, or on the basis of complaints. It must then be in a position to intervene rapidly, if necessary with provisional measures.

- In order to meet the concern of legal uncertainty, one could consider to introduce at the same time, a voluntary notification regime. The solution could even be combined with a right for the parties to obtain a binding decision under certain circumstances.

On the whole, such a system would probably be more accurate without being overreaching.

5. CONCLUSION

Two remarks to sum up and to conclude. The method of merger analysis used by the Swiss Competition Commission does not differ significantly from general standards. It is true, that the final test for an intervention is higher in Swiss law than in the EU, but this is a matter of substance – surely worth to be discussed – rather than of methodology.

High turnover thresholds, however, may pose a real threat to the effectiveness of merger control in a small economy. They leave small, but internally harmful concentrations without control, while causing an additional burden in larger cases, which have to be cleared by other jurisdictions anyhow. An effect-based merger control system may, therefore, be more appropriate for countries like Switzerland. The concern of lack of legal certainty could be met by allowing for a voluntary notification, combined with a right for the parties to obtain a binding decision under certain circumstances.

Małgorzata Szwaj[403]

THE EVOLUTION OF MERGER CONTROL IN POLAND

1. INTRODUCTION

One of the essential competition law objectives is to protect effective competition between market players and ensure its development. For that purpose, the law provides a range of instruments, among which supervising mergers on the market plays a significant role. This scrutiny, hereinafter referred to as merger control, is implemented – differently than other measures – on an *ex ante* basis and its application is possible due to the fact that undertakings have a duty to notify their intention to concentrate to the competition authority.

After twenty years of the Office of Competition and Consumer Protection's (UOKiK) existence there is a need to reflect on competition policy and competition law enforcement in Poland. This also applies to the experience of enforcing merger control regulations in this country.

This experience has only a slightly shorter history than the Polish competition protection authority itself. Although already the 1990 Competition Act[404] granted the Office some powers as regards "merging, transforming or establishing" business entities, the mergers actually came under the Office's scrutiny after the amendments to the 1990 Act took effect in 1995.[405] Thus, in 2010 not only are we celebrating the twentieth anniversary of the Office's establishment, but also the fifteenth anniversary of the functioning of Polish provisions on merger control, which follow European models.

This article contains a review of case law and changes in legislation over the past fifteen years concerning issues that are material for applying merger control rules, i.e. defining what concentrations are and the notification criteria. Their analysis

403 The author wants to express her thanks to Mr. Piotr Skurzyński, PhD student at Warsaw University's Law and Administration Department, for his help in the preparation of this article.

404 Act of 24 February 1990 on counteracting monopolistic practices and on the protection of consumer interests (Dz.U. No. 14, item 88, as amended).The first post-war "Antimonopoly Act" that existed in the final period of the centrally planned economy, i.e. which was adopted on 28 January 1987 and concerned counteracting monopolistic practices in the national economy (Dz.U. No. 3, item 18, as amended), provided only for an obligation to notify the competition authority about the intention to merge economic units.

405 Act of 3 February 1995 on amending of the Act on counteracting monopolistic practices (Dz.U. No. 41, item 208), amending, among other things, Art. 11 of the Act of 1990 as of 19 May 1995.

will help us to formulate conclusions on desirable further modification of the regulations in force.

2. THE CONCEPT OF CONCENTRATION

"Concentrations", as an economic concept, lead to structural transformations in the market, which consist in merging undertakings' assets, i.e. external growth as opposed to so-called internal or organic growth. Such phenomena may lead to distortions of market competition, which competition law seeks to counteract.

Initially, the 1990 Competition Act regulated the issues of scrutinising mergers in a very broad and imprecise manner. It has caused doubts to be raised from the point of view of the proportionality principle with respect to restrictions of business activity. Such a broad approach was consistently narrowed down by subsequent amendments. Modifications introduced in 1995 were of substantial significance. At that time, a formally closed catalogue was introduced describing situations that constituted a "merger" (pol. *łączenie przedsiębiorców*).[406] It already included all forms of economic operations constituting "concentrations" within the meaning of the 2007 Competition Act[407] currently in force and of the EU provisions on merger control[408], i.e. mergers of two or more independent undertakings, acquisition of control and the creation of joint ventures.[409] The scope of the Office's scrutiny also covered *quasi-concentrations*[410], such as, for example, acquiring shares resulting in exceeding a given threshold of votes at the meeting of shareholders, which did not result in an acquisition of control. Initially, the thresholds were 10, 25, 33 or 50 percent of votes, and under the 2000 Competition Act the Office's consent was required only for acquiring shares resulting in exceeding a 25 percent

406 The catalogue was of a closed nature only formally because the definition of an acquisition of control as a form of concentration was very general and in practice covered an extremely varied range of transactions that only had to aim at an acquisition of control.

407 Act of 16 February 2007 on competition and consumer protection (Dz.U. No. 50, item 331 as amended).

408 Council Regulation (EC) No. 139/2004 of 20 January 2004 on the control of concentrations between undertakings, (O.J. L 24/1, 29 January 2004). The Regulation replaced the previous Council Regulation (EEC) No. 4064/89 of 21 December 1989 on the control of concentrations between undertakings (O.J. L 257/13, 21 September 1990).

409 The obligation to notify the competition protection authority of the intention to create a joint venture was initially based on provisions concerning the intention to acquire 10, 25, 33 or 50 percent of the votes at the general meeting or the meeting of shareholders. After the Act of 22 October 1998 on amending of the Act on counteracting monopolistic practices (Dz.U. No. 145, item 938) entered into force, a separate provision was added to the 1990 Act (Art. 11(2) point 3a) that referred to "obtaining shares of a newly created undertaking".

410 The division into typical mergers and quasi-mergers has been proposed by Ms. E. Modzelewska-Wąchal in her comments on the Act of 2000. As a result of changes introduced by the Act of 2007, this division became less significant.

threshold.[411] The rationale of imposing on undertakings the obligation to notify the Office of the intention to conduct such transactions has been put into doubt because they have had no influence on competition.[412]

After the current 2007 Competition Act entered into force, the obligation to obtain the Office's prior consent was restricted to transactions that constituted concentrations in an economic sense.[413] Its substantive scope practically corresponds to that of Regulation No. 139/2004. Leaving *quasi-concentrations* out of merger control[414] is a sign that the Polish legislator has departed from a methodology based on a detailed catalogue of concentration forms and has adopted the more universal approach functioning at EU level. It is worth noting that Poland did not and still does not have a duty to adopt provisions that are convergent with Regulation No. 139/2004 to such an extensive extent.[415]

In the light of the above remarks, the evolution of the concept of creating a joint venture is interesting as a form of concentration which still has specific differences in Polish law when compared with the Regulation.

At the beginning, the obligation to notify the Office of the intention to establish a joint venture was solely the result of the Antimonopoly Court's interpretation of the 1995 Competition Act.[416] Characteristically, already at that point the Antimonopoly Court used the analogy to the solutions existing in EU law to substantiate its position. Joint ventures came under the Office's scrutiny as late as at the end of the 1990s, while the solutions adopted significantly deviated from EU models. The legislators decided then that the notification is required when the shares in a "newly established undertaking" are acquired, which would result in attaining at least 25 percent of the votes at the meeting of shareholders.[417] Hence, the concept of a joint venture existed separately

411 Act of 15 December 2000 on competition and consumer protection (Dz.U. No. 122, item 1319, as amended).

412 R. Janusz, M. Sachajko, T. Skoczny, *Nowa ustawa o ochronie konkurencji i konsumentów*, „Kwartalnik Prawa Publicznego" 2001, No. 3, p. 193.

413 With the exception of the case discussed below, i.e. "non-full function" joint ventures.

414 T. Skoczny presents a slightly different opinion in this regard: according to him, an undertaking's acquisition of a part of another undertaking's assets (part of or the entire undertaking) constitutes a new type of quasi-concentration. Cf. T. Skoczny (in:) T. Skoczny, A. Jurkowska, D. Miąsik (ed.) *Ustawa o ochronie konkurencji i konsumentów. Komentarz*, Warszawa 2009, p. 799 et seq.

415 In Austria, Germany and Lithuania, for example, there is still an obligation to notify competition protection authorities of an intention to perform a concentration consisting in acquiring a minority package of shares not resulting in an acquisition of control.

416 Judgement of the Antimonopoly Court of 4 February 1998, ref. no. XVII Ama 66/97, LEX no. 56330.

417 Act of 22 October 1998 on amending the Act on counteracting monopolistic practices (Dz.U. No. 145 item 938), in force

from the criterion of joint control, which is decisive for defining a joint venture under EU law.[418]

The only modification in this regard was introducing the term *wspólny przedsiębiorca* into the 2000 Act, which term may be translated into English as a joint enterprise, or joint venture. However, this term was not defined, and the 2007 Competition Act currently in force preserves this state of affairs. The concept of joint control, as opposed to EU law, is expressed in the Act in force only in an indirect way,[419] without explicit linkage to "wspólny przedsiębiorca" ("joint venture") and "capital group". This results in important problems related to interpretation, which case law fails to clarify.

It is unclear, in particular, whether the obligation to obtain the Office's prior consent relates only to cases of establishing an undertaking over which joint control is to be exercised, or whether it also concerns, for example, the creation by a greater number of independent undertakings of a company, over which no one will exercise control. In the related literature there are opinions in support of a wider interpretation which assumes that a "joint venture" should be understood as an entity in the creation of which two or more other undertakings participate, while ignoring the condition of the existence of joint control.[420] This seems to be unjustified from an economic point of view, which leads to excessively extending the scope of transactions remaining under the Office's scrutiny. In practice, with that approach, most newly created companies would be subject to such scrutiny.

The lack of consistency of the provisions on joint control and joint venture is also visible in the specific definition of a capital group under the Act. It describes a capital group as a group of undertakings which are under the control of a "single" undertaking.[421] The consequences of that approach are significant. In many instances the Office found that exercising joint control over an undertaking results in a situation where "that undertaking does not belong to a capital group of any of the undertakings that exercise joint control over it."[422] In this sense,

since 2 January 1999 ("the 1998 Amendment").

418 C.J. Cook, C.S. Kerse, *EC Merger Control*, London 2009, p. 58.

419 Article 13(2) point 2 of the 2007 Act defines the takeover of another undertaking "by one or more undertakings" as a form of concentration within the meaning of the Act.

420 C. Banasiński, E. Piontek (ed.), *Ustawa o ochronie konkurencji i konsumentów. Komentarz*, Warszawa 2009, p. 340.

421 Article 4 point 14 of the 2000 Act and 2007 Act.

422 Cf., for example, the President of the Office's Decision of 28 June 2006, No. DOK 66/06.

a capital group cannot consist of joint ventures, which creates an important inconsistency in the Competition Act. This is because where undertakings remaining under joint control do not belong to any capital group, their activity should not be taken into account in the assessment of the market impact of transactions envisaged by any of the undertakings exercising joint control over them.

The Competition Act's approach to capital groups greatly deviates from the solutions adopted by Regulation No. 139/2004. The resultant risk of not taking into account some joint ventures during the assessment of the market impact of envisaged concentrations is closely related to another important and peculiar aspect of the approach to joint ventures employed by the Polish law.

According to the Regulation, only cases of establishing "full-function" joint ventures, i.e. entities operating on the market in a significantly autonomous way, and independently from their parent companies, should be notified to the European Commission. Therefore, undertakings that are created in order to conduct joint research and development (R&D) works, and those that supply their products solely to their parent companies or act on the market only as a joint sales office for products coming from the entities that exercise control over them, are not full-function joint ventures.

The Act on competition and consumer protection does not distinguish between full-function joint ventures and non-full function joint ventures, which results in the obligation to notify the establishment of both these types. The literature points to a lack of purposeful and systemic justification for imposing preventive scrutiny over cases of creating non-full function joint ventures.[423] According to the EU's experience, it would be reasonable to exclude non-full function joint ventures from ex ante scrutiny on the grounds that they do not cause any permanent change in the market structure, and potentially to subject them to ex post scrutiny under rules applied to assess restrictive agreements.[424]

423 M. Szydło, *Kontrola wspólnych przedsiębiorstw (joint ventures) w prawie antymonopolowym*, „Prawo Spółek" No. 12/2002.

424 Of all the European Union Member States' legal systems, a solution similar to that employed in Poland is present practically only in Lithuania. In Austria and Germany, the obligation to notify an intention to establish a non-full function joint venture results from the fact that all transactions resulting in obtaining 25 percent of the shares are defined as concentrations. In the case of Germany, acquiring the power to exert a significant (but not decisive) influence on the functioning of another undertaking constitutes a concentration. In turn, in Greece the creation of a non-full function joint venture is subject to ex-post notification, in a different procedure than in the case of a concentration. In the UK, concentrations are defined in a manner significantly different to that adopted by Regulation No. 139/2004, and notification is voluntary. This shows how significantly different national provisions and EU law can sometimes be.

As seen above, although Polish lawmakers have consistently been introducing the solutions forged in EU law into national law, in the case of concentrations that consist in creating a joint venture the national solutions are clearly different from those existing in Regulation No. 139/2004. Due to imprecise wording, applying national provisions is often problematic. This leads to the conclusion that it would be advisable to adopt much clearer and, more importantly, already tested solutions taken from the Regulation, at least in order to obtain a more precise description of the relationships between the terms "joint venture", "joint control" and "capital group".

3. THRESHOLDS FOR NOTIFICATION

Polish law, similarly to EU law[425] and to individual Member States' national law, has adopted turnover thresholds of undertakings participating in a merger as the most effective premise for the obligation of notifying envisaged concentrations.[426] A notification obligation based on such an unambiguous criterion permits its automatic application, which is desirable.[427]

The turnover thresholds as a premise for notifying a merger were introduced into Polish legislation for the first time by the 1995 Competition Act. At that time, the thresholds were 5 million ECU (since 1999 – euro) for transactions concerning an acquisition of control and acquisition of shares[428] and 2 million ECU for transactions where the assets of another undertaking were acquired.

Later on, the 1998 amendment resulted in an increase of the thresholds to 25 million euros for transactions concerning an acquisition of control and shares and 5 million euros for assets transactions.

The 2000 Competition Act introduced thresholds that were twice as high as before. Now, transactions in which the total global turnover of the participating undertakings exceeded 50 million euros were subject to notification. For the first

425 Article 1 of Council Regulation (CE) No. 139/2004.

426 In Spain, Portugal and the UK, the notification obligation is established on the basis of turnover and also the market share. Moreover, in Greece and Slovenia the market share may constitute a basis for a national competition protection authority to request notification after the transaction has been carried out.

427 Cf. Justification of the government's 2007 draft Act at: Sejm of the Republic of Poland, 5th term, ref. no. 1110, http://orka.sejm.gov.pl/Druki5ka.nsf/0/06AED0325C1F3B3FC125722600445A4A/$file/1110.pdf.

428 The threshold also concerned transactions that consisted in merging undertakings and merging posts in competing undertakings.

time, the *de minimis* threshold was introduced, according to which an undertaking was exempted from the notification obligation where the turnover achieved by the capital group of the target[429] in Poland did not exceed 10 million euros in any of the two preceding years.[430]

The next important shift in the turnover thresholds was introduced by the 2007 Act. At present, transactions involving undertakings whose aggregate turnover exceeds 50 million euros in Poland or 1 billion euros globally are subject to notification.

During the 1995-2007 period, merger control rules took into account the turnover of the selling party when calculating a transaction's eligibility for notification. This was changed in the 2007 Act, but only with respect to the *de minimis* transactions. The *de minimis* threshold remains nominally unchanged and is still 10 million euros of the target's turnover obtained in Poland. However, the obligation to take into account its entire capital group (including the selling party) was revoked. Only the turnover of the target is taken into account, as well as that of its subsidiaries.

Increasing the notification thresholds was the result of an assessment conducted by the Office over a period of years, concerning market structure changes caused by concentrations, and was intended to eliminate the notification of the transactions with no or a negligible impact on competition.[431] The purpose of introducing higher thresholds, in particular by the 2007 Competition Act, was to enable the UOKiK to concentrate above all on an assessment of transactions involving significant "sector investors", i.e. producers and resellers, rather than "financial" mergers aimed at increasing the capital of a given undertaking in exchange for later profits.[432]

429 At that time, the application of the *de minimis* threshold also concerned transactions consisting in acquiring a minority package of shares that entitled the holder to at least 25 percent of the votes in shareholders' meetings (Article 13(1) of the 2000 Act).

430 In light of the amendment to the 2000 Act introduced by the Act of 16 April 2004 on amending the Act on competition and consumer protection and on amending certain other acts (Dz.U. No. 93, item 891), the *de minimis* threshold was not applied to transactions resulting in creating or strengthening a dominant position in the relevant market (Article 13(a) of the 2000 Act).

431 Cf. Justification of the government's 2000 draft Act (Sejm of the Republic of Poland, 3rd term, ref. no. 1996, available at http://orka.sejm.gov.pl/Rejestrd.nsf/8b78093dea0afb92c125675800366000/0b9ef59fd4813bf7c12568ff00283652/$file/1996.pdf) and justification of the government's 2007 draft Act (Sejm of the Republic of Poland, 5th term, ref. no. 1110, available at http://orka.sejm.gov.pl/Druki5ka.nsf/0/06AED0325C1F3B3FC125722600445A4A/$file/1110.pdf).

432 Changes in thresholds had a significant influence on the number of merger cases investigated by the Office. So, increasing the thresholds (from 5 million to 25 million euros) as of 1999 resulted in a decrease in the number of cases handled from 1872

The justification of the government's draft of what later became the 2007 Competition Act contains a detailed explanation of the reasons for giving up considering the turnover of the target's entire capital group as a criterion for exempting the notification obligation of a transaction due to the *de minimis* turnover of its participants.[433] According to the authors of the draft, the change results from the fact that the turnover of an undertaking which "disposes of its control" over the target company is of no significance for the assessment of the transaction's impact on the market.

As a logical consequence of the above, this fully reasonable approach should be applied to the calculation of the thresholds determining the notification obligation. The present legal situation remains in contradiction to the above reasoning.

In the contrast, both EU[434] law and individual Member States' law do not take into account the seller's turnover.[435] Such an approach is justified by the fact that after the notified transaction takes effect, the seller exits the relevant market. For this reason its economic and financial resources (measured by the total amount of turnover achieved) are of no importance for assessing the transaction's impact on the market and can therefore be disregarded.[436] Thus, the participants of a merger are not viewed from a corporate perspective (identifying undertakings that are parties to the transaction), but from the point of view of impact of their activity on the market (identifying undertakings whose operations will merge after the transaction).[437]

Considering the above, it seems justifiable to put forward a *de lege ferenda* postulate to amend the 2007 Competition Act through the introduction of a uniform method for calculating the turnover for each threshold (global turnover, domestic turnover

in 1998 to 1079 in 1999. The entry into force in 2001 of the Act of 2000, according to which the thresholds were raised to 50 million euros, resulted in a lower number of cases handled: from 1107 in 2000 to 542 in 2001. The last significant modification of thresholds effective as of April 2007 resulted in a decrease of the number of cases from 263 in 2007 to 177 in 2008 (source: reports on the Office's activities in the 1998-2008 period).

433 Article 16 of the 2007 Act.

434 Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No. 139/2004 on the control of concentrations between undertakings, O.J. C 95/01 of 16 April 2008, point 129 et seq.

435 Only German and Austrian legislators provided for the necessity to take into account the seller's turnover where it is in possession of 25 percent of the shares in an acquired company.

436 Cf. The European Commission in the Commission Notice on the calculation of turnover under Council Regulation (EEC) No. 4064/89 on the control of concentrations between undertakings (O.J. C 66/25, 2 March 1998, point 31).

437 Cf. C.J. Cook, C.S. Kerse, *EC Merger Control*, London 2009, p. 98 and G. Drauz, C.W. Jones (ed.), *EU Competition Law*, Vol. II *Mergers and Acquisitions*, Leuven 2006, p. 102. Similarly, the European Commission in the Commission Notice on the calculation of turnover under Council Regulation (EEC) No. 4064/89, op. cit., point 31.

or the *de minimis* turnover of the target company) and excluding the need to take account of the seller's turnover in the calculations.

4. CONCLUSION

The analysis of the changes in merger control rules, as regards the definition of concentrations and the shifts in the notification criteria, allows indicating that we are seeing a progressive evolution of the national provisions and their harmonization with those in force at EU level. The differences present in Polish law do not, in general, significantly deviate in their scope from the differences that exist in the legal systems of other European Union Member States, with the two important exceptions mentioned above. Hence, the legislators should consider both the peculiar method of establishing the jurisdiction of the national competition authority in the merger control cases and the obligation to notify both full-function and non-full function joint ventures. Both of these issues require the introduction of appropriate changes to the Polish Competition Act. At the same time, adopting the solutions functioning at EU level in this respect would be a logical consequence of the evolution of Polish merger control rules which has been taking place since the very beginning of their application.

Wojciech Szymczak

DEFINITION OF THE MARKET AS A KEY ELEMENT IN THE MERGER ASSESSMENT IN THE RETAIL SECTOR

1. MERGER CONTROL IN POLISH COMPETITION LAW

In Poland, merger control as well as the other tasks in the field of competition protection, including the monitoring of State aid, are the responsibilities of the President of the Office of Competition and Consumer Protection (UOKiK). The current merger control rules are set out in Title III of the Act of 16 February 2007 on competition and consumer protection.

Enterprises participating in a merger are subject to scrutiny if their combined worldwide turnover in the financial year preceding the year of notifying the transaction exceeds the equivalent of 1 billion euros or 50 million euros in the Republic of Poland.

Every year the President of the Office of Competition and Consumer Protection examines a few hundred merger notifications. In 2005, the competition authority issued 329 clearances. After that year, the number of the mergers examined fell. In 2006, 266 clearances were issued, and in 2007 – 263. A year later only 177 clearances were issued, which was a result of the coming into effect of the present Act on competition and consumer protection, which changed the rules concerning the notification of the transaction. The previous threshold of combined worldwide turnover of merger participants in the financial year preceding the year of notification, i.e. the equivalent of 50 million euros, was replaced by the two new thresholds, as described above. Raising the thresholds resulted in a decrease in the number of merger cases examined by the competition authority. This way, notifications concerning small mergers of no significant impact on the market were eliminated, which allowed the authority to focus on the assessment of transactions relevant to the economy.

As it is the case of other competition authorities, in Poland, the notification of a merger relatively rarely ends in a prohibition or a conditional clearance. From January 2005 to November 2009, the authority issued eight conditional clearances[438]

438 Two conditional consents in 2005, 2007 and 2008, one in 2006 and one issued during the period between January and October 2009.

and four prohibitions. In April 2006, the Office prohibited the merger of Cari Agri and Jabłonna, since the transaction would result in a significant impediment of competition in the market of flavoured vodkas[439]. During the first ten months of 2009, as many as three mergers were banned by the President of the Office of Competition and Consumer Protection. In March, the competition authority prohibited the merger of Orzeł Biały S.A. and Baterpol sp. z o.o., its only competitor operating in the Polish market.[440] In October 2009, prohibitions were issued with respect to the envisaged acquisition by Cogifer Polska sp. z o.o., producer of railway turnouts, of a company operating in the same sector, Koltram sp. z o.o.[441], as well as an acquisition by Rieber Foods Polska S.A., a producer of instant cakes and desserts of the Gellwe brand owned by one of its main competitors, FoodCare sp. z o.o.[442]

Out of the six conditional clearances issued by the Polish competition authority in 2006–2009 as many as 50 percent concerned the trade and services sector. In June 2007 the competition authority issued a conditional clearance for Carrefour to purchase the Albert and Hypernova retail chains owned by Ahold[443]. In June 2008, UOKiK agreed conditionally to the merger of the two cinema chains – the Multikino chain, owned by ITI, and the Silver Screen chain, its former competitor[444]. In September 2008, the Polish competition authority issued a conditional clearance concerning the takeover by Jeronimo Martins Dystrybucja S.A. (JMD), the owner of the Biedronka discount stores, of the Plus chain owned by Plus Discount sp. z o.o., part of the Tengelmann group.

Despite the number of conditional clearances and prohibitions was very small compared with the whole body of judgments in the field of merger control, as it was mentioned above, it is symptomatic that their number started to increase in the past years. It is also not accidental that as many as two out of all the conditional clearances concern the sector of fast-moving consumer goods, since this area is an excellent illustration of the processes taking place over the last twenty years and characterising the developments in many sectors of economy in Poland as well as in a few other post-Communist countries, where at the beginning of the 1990s a centrally planned economy was replaced with a market economy.

439 Decision of the President of UOKiK of 4 May 2006, No. DOK-41/2006.

440 Decision of the President of UOKiK of 5 March 2009, No. DKK-10/2009.

441 Decision of the President of UOKiK of 8 October 2009, No. DKK-67/2009.

442 Decision of the President of UOKiK of 8 October 2009, No. DKK-68/2009.

443 Decision of the President of UOKiK of 28 June 2007, No. DOK-86/2007.

444 Decision of the President of UOKiK of 19 June 2008, No. DKK-49/2008.

This above all concerns sectors which, after the break-up of monopolies and privatisation in the first years after the transformation, began to consolidate again, this time already in accordance with the principles of economics, requiring more and more attention on the part of the competition authority and development of more advanced analytical tools used by it, particularly as regards merger control.

2. THE RETAIL SECTOR IN POLAND

In Poland, during the period of the centrally planned economy, retail and service outlets, just as the rest of the economy, were mostly controlled by the state. Trade was dominated by cooperatives. The straight majority of groceries operating in towns and cities belonged to a network managed by the food cooperative Spółdzielnia Spożywców "Społem". However, these centrally-managed structures were not very flexible, which, coupled with the low efficiency of the production sector and the consequent constant shortages in supply, caused the food retail to become one of the most acute examples of inefficiency of the entire economic system.

Therefore, it is hardly surprising that after the implementation of the free-market reforms at the turn of the 1980s and 1990s, retail was one of the sectors where the so-called "explosion of entrepreneurship" occurred, with the emergence of great numbers of small firms run by sole entrepreneurs[445]. Spontaneously established small groceries very quickly destroyed the existing structures. First, the national chains split up into a number of smaller and disconnected local networks, but many of them did not withstand competition and declared bankruptcy[446]. As a result, in the middle of the 1990s, the food retail market was very fragmented. This situation is illustrated by the number of shops in Poland, which increased from 237 400 in 1990 to 430 944 in 1995[447], and the number of population per retail outlet, which fell from 81 people in 1990 to 43 in 1995[448]. It should be stressed that at the time there were practically no big retail chains of significance beyond the local level.

445 A. Grzesiuk, *Handel detaliczny w okresie transformacji. Diagnoza i trendy rozwojowe*, a paper for the conference „Transformacja - Integracja - Globalizacja. W poszukiwaniu modelu rozwoju gospodarczego Polski", 15-16 May 2003, Cracow University of Economics, p. 1.

446 See http://kzrss.spolem.org.pl/informacje-o-spolem/kzrss-spolem,3,.html.

447 A. Grzesiuk, *op. cit.*, p. 3; cf. also: H. Powęska, *Zmiany w wiejskim handlu detalicznym na tle tendencji krajowych*, Roczniki Naukowe SERiA, vol. VII, book 3, Poznań 2007, p. 144.

448 A. Grzesiuk, *Zmiany strukturalne w handlu jako element dostosowawczy do wymagań nowoczesnej gospodarki*, (in:) *Państwo i rynek w gospodarce*, D. Kopycińska, (ed.) PTE, Szczecin 2003, p. 160.

Another legacy of the previous system was the very poor state of the retail infrastructure, which had a considerable influence on the quality of services offered in this field. Modern forms of retailing, which became commonplace in market economies around the world over the previous decades, did not practically exist in Poland. That situation may explain the tremendous success of the new private shops whose owners, in spite of the lack of know-how and funds for investments, were able to win customers from the previously existing outlets.

In the next years, enterprises which were the most successful in the local markets started to establish regional and supraregional chains, either by buying the already existing shops or by building them from scratch. This is how the local and regional chains of shops were re-established and consolidated.

At the same time, with the reinforcement of the free-market reforms and the country's opening up to foreign investments as well as progressing privatisation, the leading players in the European retail market relatively quickly became interested in the Polish market. On the one hand a country with the population of 38 million and no modern retailing forms whatsoever presented a challenge for entrepreneurs from developed countries, on the other hand, it was also an unusual chance to get a significant share of the market and to strengthen one's position in the European market.

As early as in 1991 we have started seeing enterprises with a strong European position take interest in the Polish market and take diverse actions aimed at preparing the development of retail chains in this country. Since the middle of the 1990s we have been seeing European chains quickly enter the Polish market, realising that their future success might depend on how quickly they establish their presence here. In 1994, Tesco and the Metro group, among others, appeared in Poland; in 1995 we have seen Ahold, E.Leclerc[449], Netto, Rewe, and Tengelmann enter the market; in 1996 came Auchan, Carrefour, Spar, the Cassino group, and in 1997 – Jeronimo Martins Distribution. During that period the above-mentioned enterprises created chains of large-format stores almost from scratch – they established a network of suppliers as well as educated and took over consumers.

Towards the end of the 1990s the number of new enterprises entering the market considerably decreased; however, further expansion of chains (establishment of

449 In 1995, E.Leclerc opened the first supermarket in Poland.

new stores and expansion into new areas) was observed, as well as diversification of their offer, with new brands and formats being introduced. In general, the success of those actions determined whether a chain decided to stay in the Polish market or not.

Since 2000 we have been dealing with the consolidation of chains of large-format stores in Poland. Indeed, that process was noticed already in the 1990s; however, it is only since 2000 that it had escalated. At that point many companies assessed how much they have achieved their objectives and reviewed their expansion plans. Those of them which estimated their chances in the Polish market as unsatisfactory made a decision to withdraw and sell their stores to former competitors.

Among the most important transactions during that period, the following should be mentioned:
- The takeover of 24 Globi stores by Carrefour in 2000,
- The takeover of 11 Billa supermarkets by Auchan in 2001,
- The takeover of 13 HIT hypermarkets by Tesco in 2002,
- The takeover of 5 Jumbo hypermarkets by Ahold in 2002,
- The takeover of 16 Rema 1000 stores by JMD in 2003,
- The takeover of 11 Hypernova stores by Carrefour in 2003-2005,
- The takeover of 9 Julius Meinl stores by Tesco in 2005,
- The takeover of 19 Geant hypermarkets by Real in 2006,
- The takeover of the Leader Price chain by Tesco in 2006,
- The takeover of further 15 Hypernova hypermarkets and 183 Albert supermarkets by Carrefour in 2007,
- The takeover of all the Plus chain stores owned by Tengelmann by JMD in 2008.

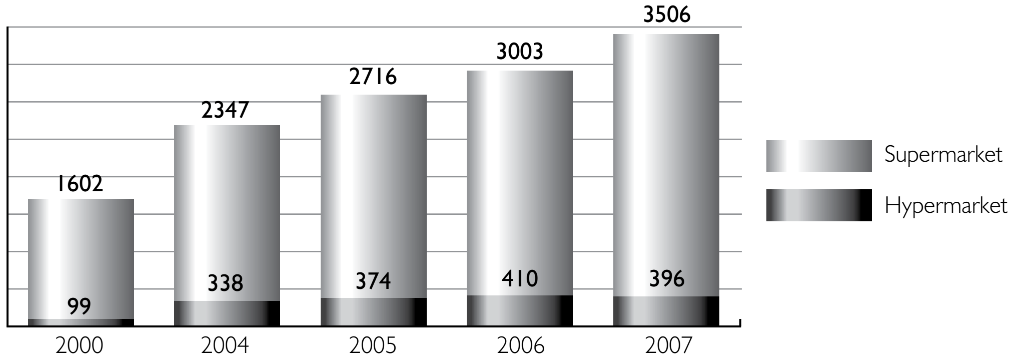
As a result of this series of takeovers, out of around 20 operators of large-format stores that were in business in the 1990s, in 2009 there remained around 10 enterprises running developed nationwide chains, including Jeronimo Martins Dystrybucja (operating under the Biedronka brand), Carrefour (Carrefour and Carrefour Express), Tesco (Tesco and Savia), Metro (Real), Auchan (Auchan), Netto (Netto), Lidl (Lidl), and Kaufland (Kaufland)[450]. One should add to this list businesses operating under franchise agreements, e.g. Intermarche[451].

450 Despite the links of Lidl and Kaufland with the German group Schwarz, both chains do not form a group in Poland.

451 An exact number of chains is difficult to provide, because they differ markedly in terms of the organisation and the profile of activity. Another problem concerning the classification of chains is e.g. the treatment of delicatessen such as Alma or Bomi.

Decrease in the number of chains did not translate in any way into a slowdown of the entire sector. The remaining players still worked on the development of their chains, e.g. by increasing the number of stores.

Figure 1. Rise in the number of super- and hypermarkets in Poland in 2000-2007



Source: Own study based on data obtained from the Polish Central Statistical Office (GUS).

As seen in Figure 1, after 2000 a particularly dynamic growth was noted in the segment of supermarkets and discount stores. Among other things, it was a result of JMD's expansive policy, which located its stores in much smaller urban centres than the hypermarket chains.

The above-mentioned changes resulted in retailing being increasingly concentrated in large-scale establishments. While before 2007, all merger cases investigated by the Polish competition authority resulted in unconditional clearances, both of the big transactions envisaged in this sector in 2007–2008 turned out to be problematic, and ended up with conditional clearances.

The total withdrawal from the Polish market of the Ahold group, which was at that time one of the main players on the HSD sector (hypermarket, supermarket, discount stores), active in its both segments, i.e. supermarkets/discount stores (Albert supermarkets) and hypermarkets (Hypernova hypermarkets), and the subsequent takeover of the group's market share by another major player, Carrefour, lead, for the first time, to a situation where in some locations the position attained Carrefour indicated the possibility of impeding the development of competition. One should note that in the previous years both Carrefour and Ahold had taken over some smaller chains, moreover Carrefour had been already increasing it assets by purchasing single Hypernova hypermarkets precisely from Ahold[452].

In its decision of June 2007[453] the competition authority cleared the transaction consisting in Carrefour Nederland B.V. acquiring the control over Ahold Polska Sp. z o. o., provided that by the end of 2008 Carrefour Nederland B.V. disposes of any rights, including the right of ownership, the right of perpetual usufruct and the right to rent, to eight stores located in Grodzisk Mazowiecki, Jaworzno, Chrzanów, Pabianice, Sochaczew and Zamość.

Even more concerning seemed the concentration notified in 2008 by Jeronimo Martins Dystrybucja S.A. The company expressed the intention to take over the whole Plus chain owned by the German group Tengelmann. Although JMD does not have hypermarkets and operates only one retail chain functioning under the Biedronka brand, it is an indisputable leader in the HSD market in Poland. At the moment of notifying the concentration the company owned 1 045[454] stores in the entire country. In 2008, its share in the national HSD market was close to 20 percent. One of the main rivals of Biedronka in the discount store segment was the Plus chain. Taking into consideration that discount stores are very often shops operating in small urban centres, where they do not compete with hypermarkets, the number of places where the transaction could potentially lessen competition was very large.

During the merger proceedings, for the first time ever, parties to the proceedings criticised the definition of the relevant market applied by the competition authority, both in terms of the product market and the geographic market. The authority carried out a market study covering the area of both enterprises' operations, standing by its definition of the relevant market. In the decision issued in September 2008[455] the authority consented to the transaction consisting in Jeronimo Martins Dystrybucja S.A. acquiring the control over Plus Discount Sp. z o.o., provided that:

452 Decision of the President of UOKiK of 7 February 2009, No. DOK-15/2005.

453 Decision of the President of UOKiK of 28 June 2007, No. DOK-86/2007.

454 As of 31 December 2007.

455 Decision of the President of UOKiK of 24 September 2008, No. DKK-76/2008.

– JMD would permanently and irreversibly dispose of any rights, including the right of ownership, the right of perpetual usufruct and the right to rent, to 38 stores located in 36 different towns and cities, including 25 stores operating under the Plus brand and taken over from Tengelmann and 13 stores previously owned by JMD and operating under the Biedronka brand,
– the retail space in three stores taken over from Tengelmann and located in three different towns be permanently irreversibly reduced and sublet to other traders or service providers, which do not belong to the JMD group.

3. DEFINITIONS OF THE RELEVANT MARKET IN POLISH LEGISLATION IN THE CONTEXT OF RETAIL TRADE

The definition of the relevant market in the Polish competition law is coincident with its definition in the Community legislation. In fact, the wording of that definition has not been fundamentally changed since 2000[456]. The current definition, set out in Article 4(9), reads as follows:

> *"For the purpose of this Act «relevant market» shall mean a market of goods, which by reason of their intended use, price and characteristics, including quality, are regarded by the buyers as substitutes, and are offered in the area in which, by reason of their nature and characteristics, the existence of market access barriers, consumer preferences, significant differences in prices and transport costs, the conditions of competition are sufficiently homogeneous".*

It is a well-known fact that in the case of competition investigations, particularly those concerning merger control, defining the relevant market is of key importance, since it is very often a decisive factor when deciding the case.

While analysing the European case law concerning merger control in the retail of fast-moving consumer goods, one may notice two main moot points. The first one concerns the relevant product market and boils down to the question whether all groceries compete with each other and create one broad relevant market, or whether that market should be divided into two or more markets depending on the size of stores. The second issue concerns the geographic market. In the case of retail trade, i.e. sale directed to consumers, the universally adopted

456 The definition of the relevant market appeared in the Polish legislation in the Act of 15 December 2000 on competition and consumer protection (Article 4(8)). The previous Act of 24 February 1990 on counteracting monopolistic practices did not include this term, although it was applied in the case law in the form that was later included in the Act of 2000. Cf. S. Gronowski, *Ustawa antymonopolowa. Komentarz*, C. H. Beck, Warszawa 1996, p. 73-83.

approach holds that one should distinguish relevant markets with a local range. However, the exact range of such markets is debatable.

3.1 PRODUCT MARKET

The frequent problem to be dealt with by competition authorities in cases concerning modern forms of retailing in fast-moving consumer goods is the issue of their distinctness from the traditional forms. The modern retailing forms are mainly three types of stores: hypermarkets, supermarkets and discount outlets (sometimes jointly referred to as "large-format stores") while the traditional forms include "corner shops". The latter are sometimes associated with small shops in which the shop assistant handles demanded products to the customer[457]. However, in reality it is an extremely diverse group encompassing both the above-mentioned stores and self-service shops of similar size, kiosks and stalls, shops at petrol stations and open-air markets squares.

Notifying their merger, enterprises managing networks of modern shops attempted to prove that they operate within the retail sector in a broad sense that contains both the modern and traditional forms of retailing. This was the case in the Tesco/ Carrefour case (Czech Republic and Slovakia), which was investigated by the European Commission. However, the European Commission again rejected such a point of view, limiting the relevant market solely to modern forms of retailing, that is hypermarkets, supermarkets and discount stores[458]. From the point of view of Poland, this decision is all the more important since it concerns two so-called new Member States that experienced system transformation shifting from centrally-regulated economy to free-market one. It is worth noticing here that parties to the proceedings in this case pointed out that the nature of retailing in the countries of the former post-Communist bloc was more traditional in character[459].

British competition authorities have a particular approach towards the product market in the retailing sector. Although the elements of this approach can be found in the previous decisions, e.g. Somerfield plc/Wm Morrison Supermarkets plc 2005,

457 Such a definition is used in periodic surveys conducted by Pentor RI. Cf. *Zasięg oddziaływania sklepów wielkopowierzchniowych, multipleksów oraz aptek*, Warszawa 2009, p. 6-9.

458 Comp/M.3905 Tesco/Carrefour (Czech Republic and Slovakia).

459 The parties in this case put forward a proposal to include stores of the Cash&Carry format in the relevant market. The Commission rejected such a point of view and indicated that such facilities are in fact small wholesalers and may be used only by persons running business activity, i.e. a small part of the total number of consumers that use standard shops offering fast-moving consumer goods.

their most complete presentation is included in the report from a survey of the retail trade in fast-moving consumer goods, conducted by the UK Competition Commission (CC) in 2006–2008. The CC distinguished three types of stores: "larger grocery stores", "mid-sized stores" and "convenience stores"[460]. However, it came to a conclusion that the two latter groups do not constitute separate markets and that there is only "one way" competition or substitution. This means that in so far as larger stores (hypermarkets) do not have to worry about competitive pressure exerted by the remaining shops, both mid-sized stores (supermarkets/ discount outlets) and convenience shops have to take it into account. Similarly, mid-sized stores, in the opinion of the CC, do not have to take corner shops into consideration. In consequence, we deal with three relevant markets, depending on the type of shops participating in a transaction: the market of larger stores, the market of larger and mid-sized stores, the market of all stores trading in fast-moving consumer goods.[461]

The definition of the relevant market with respect to retailing in the Polish case law underwent a specific evolution. As presented above, retailing in 1990s was very dispersed, modern outlets were present to a small extent and the market was just beginning to develop. That is why there was no need to separate the market of fast-moving consumer goods into smaller markets.

Even in the decision of February 2005 on Carrefour's takeover of 13 hypermarkets ,operating under the Hypernova brand and owned by Ahold[462], the market was defined as "the market of retail trade in fast-moving consumer goods", i.e. encompassing all forms of retail trade in fast-moving consumer goods. Nonetheless, the decision also contained the results of a survey of the HSD market carried out by the competition authority. Since the relevant transaction did not bring about any negative consequences for any of the analysed product markets, the authority decided to use the previous broader definition.

In September 2005, when examining the takeover of the Julius Meinl network by Tesco, the competition authority adopted a similar approach. In that case, the analysis also covered the results of surveys analysing the sector of large-format

460 To simplify slightly, it can be assumed that they are the counterparts of Polish hypermarkets, supermarkets/ discount stores and corner shops. "Larger grocery stores" are shops with an area of over 1 000-2 000 m^2 while "mid-sized grocery stores" are the ones with area between 280 m^2 and 1 000-2 000 m^2.

461 The supply of groceries in the UK market investigation, Competition Commission, London 2008, p. 62-64.

462 Decision of the President of UOKiK of 7 February 2005, No. DOK-15/2005.

stores[463]. However, the authority's maintained its previous position stating that the relevant market in question is the market of fast-moving consumer goods[464].

It was not until the decision of 21 November 2006[465] on the takeover of Leader Price by Tesco that the competition authority came to a conclusion that the modern forms of retailing are already so important and the degree of their evolution is so advanced that HSD market should be distinguished as a separate product market, irrespective of the fact that the particular transaction did not cause a significant lessening of competition on any of the isolated relevant markets.

The authority also distinguished between two relevant product markets in the retail of fast-moving consumer goods (i.e. HSD and corner shop markets) when considering two further transactions already described above, namely Carrefour/ Ahold and JMD/Plus, in which cases conditional clearances were issued.

In both cases, the parties argued (as Tesco did in the above-mentioned case investigated by the European Commission and concerning the Czech Republic and Slovakia) that there is no separate HSD market since all forms of retailing compete with each other. Due to similar reasons as the Commission, the Polish competition authority did not accept these arguments.

In this case, a few words should be said about the types of stores constituting the HSD market. All three types are referred to as large-format stores operating in a retailing chain. They mainly differ as regards the size of the retailing area and the range of products offered. It is assumed that the largest stores in this group, i.e. hypermarkets, have an area exceeding 2 500 m^2. This definition is used both by the Polish Central Statistical Office and part of the market research companies, e.g. GFK Polonia[466], although other figures can also be found[467]. Characteristically,

463 The decision contained an analysis of data included in the report *Koncentracja oraz konkurencja w handlu detalicznym artykułami spożywczymi i artykułami powszechnego użytku ze szczególnym uwzględnieniem sieci handlowych* drawn up by the Department of Trade and Marketing of the Poznań University of Economics in December 2004, and commissioned by UOKiK.

464 Decision of the President of UOKiK of 29 September 2005, No. DOK-118/05.

465 Decision of the President of UOKiK of 21 November 2006, No. DOK-143/06.

466 The Central Statistical Office defines hypermarkets as "stores with a retailing area of over 2 500 m^2, selling mainly on the basis of self-service system, offering a wide range of foodstuffs and other goods that are frequently purchased, usually with a car park" (cf. *Rynek wewnętrzny*, GUS, Warszawa 2008, p. 13). On the other hand, GFK Polonia uses the following definition: "hypermarket – a store with a retailing area of over 2 500 m^2, selling mainly foodstuffs and frequently other consumption goods and manufactured articles" (cf. e.g. http://www.poradnikhandlowca.com.pl or http://strategiebiznesu.strefa.pl).

467 Enterprises running retail chains use different definitions. It happens that their classification is much more complex. For instance, Tesco, in addition to distinguishing between hypermarkets and supermarkets, also identifies compact hypermarkets,

hypermarkets offer a very wide range of products which are not offered by other non-specialist stores dealing in fast-moving consumer goods, namely large household appliances (washing machines, refrigerators), furniture, gardening items, etc. The presence of this type of products results primarily from the very large retailing area they possess.

Supermarkets are self-service stores with a similar organisation as hypermarkets, but with a smaller retailing area (below 2 500 m^2) and, therefore, offering a smaller number of product groups and brands. Discount outlets are stores of a similar size as supermarkets, but they are oriented mainly at offering goods at lowest prices possible. In discount stores, less emphasis is put on the display of goods, which are sometimes sold directly from collective packaging. Striving to keep low prices, discount outlets offer a smaller range of products than supermarkets and are based to a large extent on "own brands", i.e. products manufactured exclusively for them.

There are numerous reasons why competition authorities classify all three types of stores as a single relevant market. Their format is of primary importance in this matter. Despite obvious differences, all of the stores have an average usable area that is much larger than the average area of traditional shops (corner shops). Consequently, they have the possibility to provide a wide range of goods (high number of commodity groups), which in turn determines the type of purchases made in these shops, i.e. the possibility of purchasing large amounts of goods (e.g. supplies for the entire week) "under one roof".

An exceptionally important aspect of the operation of the above-mentioned stores is their network nature. The fact of possessing stores located across the entire country guarantees them a substantial economic power. This in turn results in a strong bargaining position in relation to suppliers and, in consequence, allows them to offer products at lower prices. Another aspect of operation on a large scale is the possibility of introducing own brands, something discount outlets focus on, as mentioned above. The network nature of these enterprises also means that they have much more opportunities in terms of promotion, both sales promotion (various special offers, price reductions, loyalty programmes, etc.) and advertising

defining hypermarkets as stores with area ranging from 3 000 m^2 to 12 000 m^2, offering 20 000-50 000 products, depending on their size; and compact hypermarkets as stores with an area ranging from 2 000 m^2 to 3 000 m^2, offering 10 000-13 000 products, depending on their size. Supermarkets in turn are stores with an area up to 1 000 m^2, offering 3 000-5 000 products, depending on their size (cf. http://www.tesco.pl).

and related tools (bulletins, sponsoring, etc.). Furthermore, the element that distinguishes HSD from other retailing outlets is their effort to ensure logistical solutions that are convenient for the customers such, as good location, car parks and special buses transporting the customers.

In so far as the differences between hypermarkets and the remaining two types of stores are evident and can be relatively well quantified, the differences between supermarkets and discount outlets are much less clear. On the one hand, supermarkets attempt to compete with discount stores by lowering prices and offering own brands while, on the other hand, discount outlets strive to improve the aesthetics of their spaces and offer branded products more and more often. Consequently, consumers are not usually able to precisely tell the difference between these types of stores. Thus, one can conclude that customers perceive them as close substitutes. This is also confirmed by the definitions used by companies and research institutions. The Polish Central Statistical Office does not distinguish discount outlets as an independent category and treats them as "supermarkets"[468]. GFK Polonia distinguishes the two categories and defines them as follows: "Supermarket – a store with a retailing area of over 300 m^2, selling mostly foodstuffs and a limited range of chemical and cosmetic products; discount outlet – a store with a retailing area between 300-1 000 m^2, selling mostly foodstuffs and frequently a limited range of other chemical and cosmetic products"[469]. As presented above, apart from the differences in size, the main difference lies in the range of products offered. This differentiation is thus based on "technical" criteria that may be unnoticeable for an average customer.

Competition authorities also face problems when defining "the lower limit" for classifying stores as supermarkets and discount outlets. The "most handy" criterion is the usable area. However, the problem consists in the fact that none of the applied thresholds: 300 m^2, 350 m^2 or 400 m^2, is completely reliable since there are differences in size not only between stores belonging to different supermarket or discount chains, but also between stores belonging to the same chain. The Polish Central Statistical Office has determined the lower limit classifying stores as supermarkets at 400 m^2.[470] GFK Polonia applies the same threshold – 300 m^2 as

468 *Rynek wewnętrzny*, GUS, Warszawa 2008, p. 13.

469 Cited (in:) L. Grochulski, *Coraz więcej sklepów*, http://www.poradnikhandlowca.com.pl.

470 GUS defines supermarkets as stores with a retailing area ranging from 400 m^2 to 2499 m^2 that sell mainly on the basis of self-service system, offer a wide range of foodstuffs and non-food products that are frequently purchased (Cf. *Rynek wewnętrzny*, GUS, Warszawa 2008, p. 13).

regards both supermarkets and discount stores (see the definition quoted above). We have to mention the Act of 11 May 2007 on establishing and operating large-format commercial facilities that defines in its Article 12 a large-format outlet as a facility whose retailing area exceeds 400 m^2 [471]. Although these are useful points of reference, one has to be aware of the fact that there are facilities operating within chains of discount outlets or supermarkets whose area does not exceed 400 m^2, or even 300 m^2, and that there are also stores that do not belong to any chain and play the role of a corner shop exceeding these thresholds.[472]

That is why, to classifying a given store as belonging to a particular relevant market, beside the usable area, one should also consider other criteria, mainly the fact if it belongs to a chain representing a specified commercial policy. The difference between corner shops on one hand and supermarkets and discount outlets on the other, apart from their size, also lies in the such characteristics of "modern forms of retailing" as the organisation of store and its surrounding so that purchasing larger quantities is possible (e.g. construction of car parks), price policy and promotion strategies that are profitable only within a chain.

As you can see, the criteria referred to above are, to a certain extent, discretionary and hence the position of enterprises claiming that distinguishing between the above-mentioned types of stores is an artificial operation ignoring the existence of high substitutability between corner shops on the one hand and discount stores and supermarkets on the other. Supermarket chains also claim that they have a very limited possibility of competing with hypermarkets, which pose a threat to them – and not vice versa.

In the JMD/Plus case the parties indicated the phenomenon of the chain of substitution occurring in their case and with results in the consecutive segments of the market of fast-moving consumer goods to be mutually substitutable to such an extent that it cannot be divided into smaller markets. However, the Polish competition authority dismissed the argumentation presented by JDM. Having considered the case, the authority decided that the relevant market in this case is the HSD market. The authority decided that although all discount stores

471 Act of 11 May 2007 on establishing and operating large-format commercial facilities (Dz.U. No. 127, item 880) entered into force on 18 September 2007 and was repealed on 11 July 2008 due to the ruling of the Constitutional Tribunal of 8 July 2008, reference number K 46/07 (Dz.U. No. 123, item 803).

472 In its recent proceedings concerning large-format outlets, the Polish competition authority adopted an average of the above-mentioned thresholds, i.e. 350 m^2, as the starting point for analysis.

not a perfect substitute for supermarkets nor, all the more, for hypermarkets, yet the offer of these outlets is substitutable to a sufficient extent for them to be classified as a single relevant market.

This cannot be said about corner shops that cannot be treated as substitutes of outlets from the HSD market although they compete with them to a certain degree. Considering all the above-mentioned features characterising the modern forms of retailing and in particular the usable area and their network nature of operation, it can be said that small corner shops are not able to compete with HDS outlets directly and efficiently. Besides, their offer is different and customers do mainly small everyday shopping there.

It should be pointed out as well what role supermarkets and discount outlets play in the Polish context. These shops, contrary to hypermarkets, are located not only in large cities, but they can also be found in small towns. In these locations they are the only modern forms of retailing available. This alone makes them something different and more attractive than traditional stores located there.

3.2 GEOGRAPHIC MARKET

Competition among retailing chains which offer fast-moving consumer goods in geographic terms may be considered at two levels. Firstly, whole chains are competing. This is seen in promotion campaigns on the national television, own brands introduced in every chain store, etc. This is competition at the national level. The second level is competition in local areas. Despite the fact that many decisions are made top-down by chains for all stores, individual outlets have relatively big freedom in running their operations. They have to react to the actions of local competitors and take into account the preferences of local consumers. Large-format stores have different competitors in every city (even if they belong to the same chain they have different area and location, which to a certain degree determines their character). As we can see, local specificity exhausts the prerequisites stipulated in the statutory definition, which states a relevant geographic market is an area with similar competition conditions. Moreover, competition policy always aims at the protection of consumer interests, therefore, in the case of retail, it seem most appropriate to single out a market where consumers choose from among competing stores.

In relation to the above, relevant market in the case of retail is determined as an area in the vicinity of particular stores. Such approach can be found *inter alia,* in the EU case law, where it is stated that the relevant market in the case of retail is "a territory where the outlets can be reached easily by the consumer[473]".

A two-stage technique is now commonly used for determining a relevant geographic market for retail by European competition authorities. In the first stage, an area around a given store is outlined where the customer can reach the outlet by car in a given time (depending on the assumption – from 5 to 30 minutes). In the second stage, the results of the first stage are verified on the basis of specific local conditions.

One of the main problems regarding this method is the adoption of a proper "radius" for the area, i.e. the time needed for the consumer to reach the store. Different time spans are adopted in various countries and even regions, depending on consumer preferences, dominant means of transport and the geographic characteristics of the land.

In its latest decisions regarding mergers of HSD retail outlets, the Polish competition authority assumed the time to be 20 to 30 minutes. In practice, the authority examined competition with regard to two areas – one determined by the time of travel lasting 20 and the other – 30 minutes.

In the second stage of determining the relevant market, the designated area is examined in terms of population density, urbanisation level, location and convenience of transport routes, location of facilities significant for the population, which cause their travel (e.g. offices, workplaces etc.). Another problem which must be resolved each time at this stage, is connecting markets which belong to particular stores. According to the concept of the chain of substitution, if markets defined for particular outlets are significantly overlapping, they shoul d be considered as one relevant market; this is e.g. the case in urban agglomerations. But what does "significantly" mean in this respect? It seems right to adopt a 50% limit, with the number of people living in a given area or the data on their purchasing power being indicators here.

473 Comp/M.2161 – Ahold/Superdiplo.

3.3 VERIFYING THE CORRECTNESS OF DECISIONS ADOPTED SO FAR

Because the decision in the JDM/Plus case was widely commented, both, as regards the introducing the obligation for JDM to sell selected stores, as well as the definition of the relevant markets, the competition authority decided to conduct a comprehensive study in order to verify the definitions applied, the more so, that there are signals coming from the market indicating that its structure will probably undergo further changes. Moreover, the objective of the study was to verify changes on the market and how it is perceived by consumers.

The study was divided into two stages. The first one consisted in an opinion poll, i.e. a consumer survey, and its results were confronted with results of similar surveys available to the competition authority. The Second stage will be a survey of enterprises' operations, how they act on the ground, plan locations for new outlets and influence new consumers.

The Office finished the first stage. At the time of writing this article, works envisaged in the second stage are in progress, but the results obtained so far allow us to speculate on the further development of the methodology applied in merger cases in the retail sector.

The study, commissioned by the Office and conducted in July 2009 on a representative sample of respondents by Pentor RI, shows that the particular attention paid in recent years by the competition authority to the modern forms of retailing is fully justified. The significance of this type of retailing has increased greatly in the last decade. As many as 72% of the persons surveyed have been buying in hypermarkets or supermarkets. It is worth noting that 56% do their shopping in hypermarkets, which, taking into account that these outlets are located mainly in large cities, seems to be very high percentage.

One of main objectives of the study was to compare how three types of stores, namely corner shops, supermarkets/discount stores and hypermarkets are perceived. The idea was to verify if consumers notice differences between them, and if so, what do this differences concern and to what extent they determine the type of purchases consumers make. The most interesting, from the perspective of verifying the adopted definitions of relevant markets, were not the answers to the question regarding differences between corner shops and hypermarkets, i.e. opposing ends of the market, but between corner shops and supermarkets/discount stores and between the latter and hypermarkets. The idea was to verify whether the differences indicated by consumers would suggest the existence of a common market of corner shops, supermarkets and discount stores, or rather prove the correctness of the current approach, i.e. the existence of a separate HSD market. It was also taken into account that the results would demonstrate the necessity for treating each of the three segments as a separate relevant market.

The study confirmed that customers notice differences between the above mentioned groups. The differences between supermarkets/discount stores and corner shops were more distinct than between supermarkets/discount stores and hypermarkets. The report from the survey states:

> *"Supermarkets*[474]*, according to respondents, are more similar to hypermarkets than to corner shops in terms of: profitability of making big purchases, prices, wide range of products, special offers and non-cash forms of payment. Supermarkets are perceived to be similar to corner shops and hypermarkets in terms of: availability of good quality products, availability of products made by good brands and profitability of doing everyday shopping. Supermarkets are perceived to be more similar to corner shops than hypermarkets in terms of: proximity to the place of residence and profitability of making small purchases (when something is urgently missing in a household)."*[475]

As we can see, consumers noticed what enterprises operating in the segment of supermarkets/discount stores emphasise, i.e. that stores like Lidl or Biedronka are close to their homes (or at least closer than hypermarkets) and that it is possible to make big purchases there, which is the characteristic of HSD, but also a smaller purchases as well. However, this concludes the list of features in the case of which consumers noticed greater similarity between supermarkets/discount stores and corner shops than between supermarkets/discount stores and hypermarkets. In the case of four other features examined (including key features such as the choice of products or prices), consumers indicated greater similarity between

474 In this part of report the term "supermarkets" refers collectively to both types of stores, i.e. supermarkets and discount stores. In the survey, according the methodology chosen, interviewers informed respondents that supermarkets and discount stores belong to the same group.

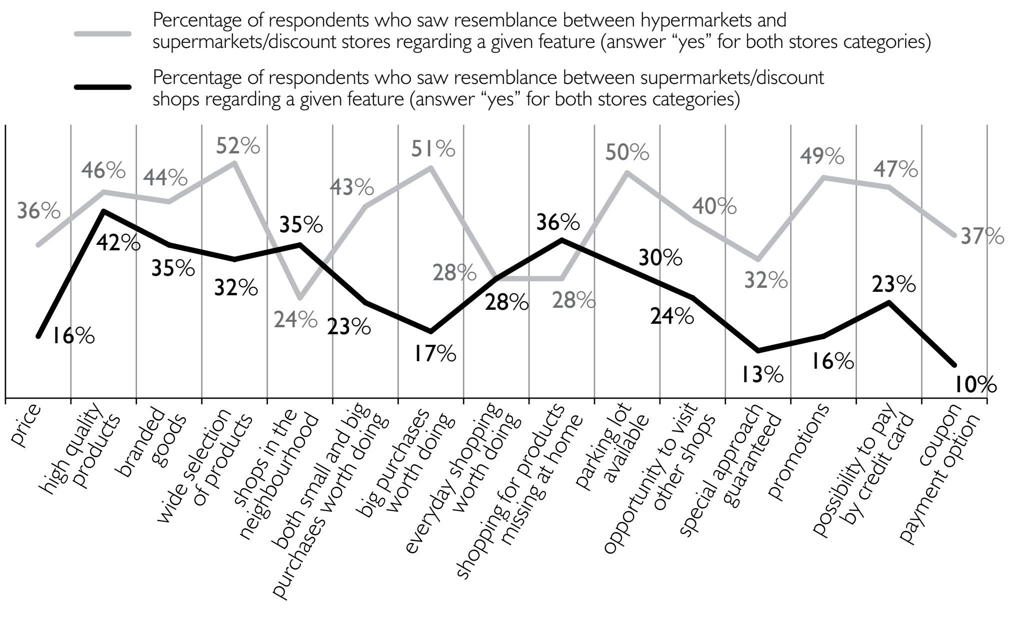
475 *Catchment area of large-format stores, multiplexes and pharmacies*, Pentor RI, Warszawa 2009, p. 18.

supermarkets/discount stores and hypermarkets, and in the case of three other features, differences between supermarkets/discount stores and hypermarkets and between supermarkets/discount stores and corner shops were similar.

It is also worth to point out the issue of the type of purchases made by consumers in particular types of stores. Although a big percentage of consumers (52%) indicated that they make small purchases (when something is urgently missing in a household) in supermarkets/discount stores, it was a significantly smaller percentage than in the case of corner shops (81%). In the case of big purchases, the number of respondents who chose hypermarkets and those who chose supermarkets/discount stores was significantly more similar (79% and 85%), and, interestingly, even higher in the case of supermarkets/discount stores than hypermarkets.

The diagram below shows an overall comparison of the differences in perceiving the three groups of stores.

Figure 2. The scale of similarities in positive associations of hypermarkets and supermarkets/discount stores and between supermarkets/discount stores and corner shops



Source: Catchment area of large-format stores, multiplexes and pharmacies, Pentor RI, Warszawa 2009, p. 50

The consumer survey did not dispel all doubts as to whether in Poland we should treat hypermarkets, supermarkets and discount stores as one market, however, it allows to quite firmly reject the view that supermarkets and discount stores belong to the same market as corner shops. Despite evident similarities, consumers still notice more differences than similarities between these two types of outlets, and what is more important these differences concern vital issues.

The survey shows that in its future concentrations concerning the retail sector, the competition authority should consider treating the segment of supermarkets/ discount stores separately, which would pose many problems of definition nature, or assume, just as the UK Competition Commission did, that competition between hypermarkets and supermarkets/discount stores is only "one-way", i.e. hypermarkets threaten supermarkets and discount stores, which in turn cannot operate "independently" of them. Consequently, according to the statutory definition, they should be classified as belonging to the same relevant market. On the other hand, assuming that supermarkets and discount stores are not a threat for hypermarkets, which can operate independently of them, the market should be limited to hypermarkets only[476].

The consumer survey give grounds for adopting the latter solution. However, a number of hypermarkets' actions, particularly those concerning prices, such as copying them from discount stores and emphasising it in advertisements or displaying on their shelves, undermines the argument that hypermarkets can operate "independently" of supermarkets/discount stores without losing customers to them.

Finally, we should mention that currently, resolving the dilemma between adopting the concept of "one way competition" or standing by the concept HSD market, has smaller practical significance than it would seem. The practice indicates that the competition problems entailed by the recent merger transactions on the HSD market mostly concerned supermarkets and discount stores in small towns, where they were not confronted with competition from hypermarkets.

476 Somerfield plc and Wm Morrison Supermarkets plc. A report on the acquisition by Somerfield plc of 115 stores from Wm Morrison Supermarkets plc, Competition Commission, London 2005, pp. 25-26.

The consumer survey conducted by Pentor RI also concerned the area of geographic market. Two key issues should be singled out here: how much time on average do consumers devote for reaching particular types of stores and to what extent they are inclined to use stores located in another town[477].

The survey showed that in this respect there is a difference between supermarkets/ discount stores and hypermarkets. In the case of the former, the average time of travel was 17 minutes and in the case of the latter 27 minutes.

As regards the inclination of consumers to make purchases outside of their area of residence, in case of both types of stores over 60% of respondents (61% in case of hypermarkets and 67% in case of supermarkets/discount stores) declared that they do not make purchases outside of their area of residence. In both cases, ca. 75% of those who make such purchases said that the main reason for this was that there were no such stores where they lived and they were forced to use stores in another town. It follows that consumers are generally not willing to travel to another town to make purchases if there is a similar store in their town.

The above results confirm, in principle, the correctness of relevant geographic market definitions applied in recent years and assuming that it is an area where the store can be reached within 20-30 minutes. However, the results obtained from the survey may help to make some modifications in relation to particular locations. It seems that maybe the practice of grouping several separate urban organisms into one relevant market should undergo some changes.

3.4 MERGER CONTROL AND THE DEVELOPMENT OF RETAIL TRADE IN POLAND

Merger control regarding retail trade is an extremely important task due to the special role played by this sector in economy. On the one hand, it influences practically all consumers in the country, on the other, it impacts a very big part of the economy – thousands of entities producing fast-moving consumer products.

The most advantageous structure of trade, it seems, is a structure of low concentration, which ensures the coexistence of various forms of trade, i.e. small traditional stores, market places as well as HSD. Although, theses predicting

477 When reviewing mergers concerning stores located in smaller, nearby towns (time of travel from one to another did not exceed 30 minutes) we were often faced with a dilemma whether stores in both towns are substitutable, i.e. whether consumers are in fact willing to travel in order to find a better offer.

complete elimination of small retailers by big chains are not fully and reliably justified, their decreasing role remains a fact. It affects not only the local economy but also the local community.

Excessive increase in significance of HSD affects the diversity of the products offered to consumers. The emphasis on cutting costs and maintaining prices at a low level may lead to decreasing the number of brands within product groups or worse quality of the products offered.

Taking into account the possibility to shape competition policy by the Polish competition authority, the only instrument for influencing the development and preservation of competition in this sector is a meticulous and thought-out review of future mergers in this sector.

Currently, the Polish HSD sector entered a phase when further decreasing of the number of chains will generally threaten competition on particular local markets, which will surely be reflected in merger decisions imposing more and more obligations on the enterprises concerned.

Precise determination of relevant markets is, therefore, extremely important for the process of assessing a transaction, because in these case, more than ever, decisions of the competition authority affects local markets. That is why it is so important at least to determine the market in geographic terms in detail.

It is very important that the definition of product market allows to create a balanced structure of the market, i.e. a structure where large-format stores are confronted with sufficiently strong competition. It would seem that corner shops do not meet this requirement, therefore, returning to evaluating the market of fast-moving consumer goods as a whole is rather ruled out. Whether the HSD market is treated as a separate relevant market or whether the concept of "one-way" competition is applied is of lesser importance.

As regards the geographic market, the competition authority should aim at assessing competition in areas as small as possible, because as the results of the survey show, consumers are not willing to travel more than 30 minutes to a hypermarket, and no more than 20 minutes to smaller stores, and, importantly, in general, they are not willing to travel to another town to do their shopping. Defining markets in broader geographic terms, on the one hand, we would include in the spectrum of the assessment stores which in reality do not compete with the reviewed ones and taking them into account would lead to clearing the reviewed transaction. On the other hand, it may cause the authority to impose obligations which would strengthen the existing disadvantageous structure. If the current definition of the HSD market is further applied, it would seem optimal to take into account the previously described two times of travel. If the concept of one way competition is adopted, it seems necessary to apply different times of travel depending on which types of stores we take into account. In both cases it is necessary to take into account the consumers' limited inclination to travel between towns in order to purchase fast-moving consumer goods.

Finally, it should be remember that when reviewing an envisaged merger, the competition authority evaluates possible changes with respect to the existing situation. Although a decision prohibiting a transaction may prevent further deterioration of the market structure as a result of a merger or takeover, it may not lead to the intensification of competition, nor can it prevent changes in the market structure effected by new outlets belonging to chains already operating in a given area being opened. Such interventions would be against the law and against the principles of market economy.

Stanley Wong[478]

INTERNATIONALISATION OF MERGER REVIEW: SOME CHALLENGES IN DESIGNING AN EFFECTIVE SYSTEM

1. INTRODUCTION

In the past two decades, Poland[479] along with many other countries, be they advanced industrialised, emerging or developing ones, have adopted laws, regulations and rules to review mergers as part of its competition laws. Of note is that China's first competition laws which include merger review, *Anti-Monopoly Law* came into force in 2008 and the merger provisions of India's *Competition Act, 2002* came into force in 2009. This international development can be seen as recognition of the important role of open markets and their proper functioning to the economy.

This article is not intended to provide a detailed examination of this international development. Instead, the paper considers the structure of merger review regimes and, in particular, the link between a requirement to notify certain transactions with the application of an assessment standard. It also explores the challenges in reconciling the objectives of a notification requirement and the application of an assessment standard. The paper then discusses the issue of objectives other than competition policy ones in reviewing mergers and acquisitions.

2. PURPOSE OF MERGER REVIEW

The purpose of reviewing a proposed merger transaction under competition policy is to determine whether as a result of the transaction (where two or more separate businesses cease to be independent of each other) competition is reduced to an unacceptable degree to warrant intervention. The degree of reduction of competition is typically expressed as a test such as "a substantial lessening of competition" ("SLC standard"), "significant impediment to effective competition" ("SIEC standard") or "creation or strengthening of a dominant position" ("dominance standard").

478 The author acknowledges the thoughtful comments of his colleague, Michele Pacillo.

479 *Act on Competition and Consumer Protection of 15 December 2000* which is now replaced by *Act on Competition and Consumer Protection of 16 February 2007.*

Virtually all countries with competition laws have enacted specific statutes to deal with mergers and acquisitions. This should be interpreted as recognition that the competition laws against anti-competitive collaboration as well as the laws against abusive unilateral conduct may not be effective, individually or collectively, to handle most of the competition issues arising from merger transactions.

As with almost all areas of competition laws, the United States is the pioneer in enacting and enforcing competition laws with respect to merger transactions.[480] The present merger provision is section 7 of the *Clayton Act* which was adopted in 1914.[481] It provides the jurisdictional basis to explicitly review mergers and acquisitions under a standard of substantial lessening of competition. It was not until the implementation of the *Hart-Scott-Rodino Antitrust Improvements Act of 1976* that the US adopted a notification system for the review in advance of certain transactions involving the acquisition of assets or voting securities.

The European Union implemented laws to deal with anti-competitive agreements and with abusive unilateral conduct as part of the Treaty of Rome (what are now Articles 101 and 102 of the Treaty on the Functioning of the European Union ("TFEU")). It was not until 1989 that the European Union enacted specific merger control laws: Council Regulation (EEC) No 4064/89 of 21 December 1989 (OJ C 20, 28.1.2003, p.4) ("original EC Merger Regulation"). It has now been replaced by Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings (OJ L 24/1 29.1.2004) ("EC Merger Regulation" or "ECMR").The adoption in 1989 of the original EC Merger Regulation was a direct consequence of the recognition of the unsatisfactory application of Articles 81 and 82 of the EC Treaty (now Articles 101 and 102 TFEU) to review merger transactions. Although the Court of Justice acknowledged that Articles 81 and 82 may be used to deal with competition issues arising from a merger transaction it was felt that a separate legislative basis for merger review should be created: see, *Philips Morris* case[482] (Article 81) and *Continental Can* case[483] (Article 82).

480 For an overview of U.S. merger review laws, see ch. 3, "Mergers and Acquisitions", ABA Section of Antitrust Law, Antitrust Law Developments (6th ed. 2007).

481 Mergers may be reviewed under section 1 of the *Sherman Act* (1890), and section 5 of the *Federal Trade Commission Act* (1914).

482 *British-American Tobacco and R.J. Reynolds v. Commission*, Court of Justice, Joined Cases 142 and 156/84, [1987] ECR 4487.

483 *Europemballage Corporation and Continental Can v. Commission*, Court of Justice Case 6/72, [1973] ECR 215.

Merger review regimes with few exceptions comprise three components:

1. a system for the compulsory notification to the relevant authority of certain transactions before they are completed ("test for notification")

2. a standard to be applied for the assessment of certain transactions (not necessarily the same as those that are notifiable) to decide whether they should be blocked, cleared/authorized, or allowed with conditions ("assessment standard");

3. a link between the test for notification and the assessment standard ("jurisdiction to apply the assessment standard").

Virtually all merger review regimes can be divided into three groups. In the first group are merger regimes with a notification requirement which apply an assessment standard only to transactions that are notifiable. In other words, if a transaction is not notifiable, there is no jurisdiction to apply the assessment standard. Most countries or jurisdictions fall into this group, including the European Union and 25 of its 27 Member States[484], India, China, Russia,[485] Brazil,[486] South Africa.[487]

The second group comprises merger review regimes, also with a notification requirement, which separate the basis for notification from the basis for applying the assessment standard. As a result, transactions that are not notifiable may be reviewed under the applicable assessment standard. In this group there are the United States, Canada[488] and Japan.[489]

In the third group are countries such as the United Kingdom, Australia[490] and New Zealand which do not have a notification requirement but which have an assessment standard for reviewing mergers. A voluntary system (formal or informal) is usually developed as a practice for parties who wish certainty about

484 That is, with the exception of United Kingdom and Luxembourg.

485 *Law on Protection of Competition (2006).*

486 *Law 8.884/94*, in particular, Article 54.

487 Competition Act 89 of 1998.

488 *Competition Act*, R.S. 1985, c. C-34, as amended.

489 *Act on the Prohibition of Private Monopolization and Maintenance of Fair Trade Law* (Law No. 54 of 1947).

490 *Trade Practices Act of 1974.*

whether their transaction may satisfy the assessment standard. For example, in New Zealand section 47 of the *Commerce Act 1986* prohibits any merger or acquisition which would or would likely result in a SLC in a market. In absence of a compulsory notification system, parties to mergers and acquisitions may apply to the New Zealand Commerce Commission for clearance (section 66) or authorisation (section 67).[491]

3. TEST FOR NOTIFICATION

In merger review regimes with a compulsory notification requirement, typically the test for notification consists of one or more of the following components:

1. a definition of the types of transactions which are subject to notification, e.g. defining terms such as 'concentration'[492] or 'merger or acquisition'[493] ("types of transactions");

2. a requirement that there is some connection with the jurisdiction for which notification is made, in the form of a test such as demanding that one or more of the parties carry on business in the geographical territory ("local nexus test");

3. market share[494] or financial thresholds with respect to turnover or sales revenues or assets of parties to the transactions reflecting domestic only or domestic and worldwide activity; thresholds are sometimes supplemented with a requirement that the transaction in issue involves a certain value of assets or level of economic activity ("level of economic activity");

4. extent of integration through a merger of the parties or the acquisition of control, *de jure* or *de facto*, or a material degree of influence of one business over another that would result from the proposed transaction ("test of integration").

491 It should be noted that the United Kingdom and India, which do not have a compulsory notification system, nevertheless have merger laws define what types of transaction are subject to the merger assessment standard on the basis of the level of economic activity involved. In the United Kingdom, relevant mergers must satisfy either or both the share of supply test and turnover test: section 23, *Enterprise Act 2002*. In India, there is a complex definition of transactions (defined as 'combinations') that may be subject to merger assessment: section 5, *Competition Act, 2002*.

492 See, for example, Article 3, EC Merger Regulation and legislation in those EU countries that align their national merger control laws to the EC Merger Regulation. The *Anti-Monopoly Law* of China also adopts a definition of 'concentration'.

493 See, for example, section 16, *Competition Act 2002* (Ireland).

494 The few countries which employ market share thresholds include Brazil, Portugal (*Law No. 18/2003*) and Israel (*Restrictive Trade Practices Law 5748 - 1988*).

A notification system is intended only to apply to mergers whereby two or more previously independent companies are merged or amalgamated and to acquisitions whereby one company makes a purchase of the shares or assets, in whole or in part, of another entity. It should be noted that in some regimes, the terms such as 'mergers', 'mergers and acquisitions' and 'concentrations' are given special meanings, namely, defined as those transactions that are notifiable, that is, incorporating one or more of a local nexus test, a level of economic activity or a test of integration.

The use of a local nexus test is recognition that a country should require notification only in respect of those transactions which have some connection with that jurisdiction. Typically, the test incorporates the requirement that a notifiable transaction involves sales in, from or into the relevant geographical territory. This requirement reflects the concern of merger review with the impact or effects of a transaction on one or more markets in the jurisdiction. This requirement is often coupled with the obligation that one or more parties to the transaction has a physical presence in the territory. The level of economic activity in the form of financial thresholds reflects a policy decision that it would be burdensome to impose on business a requirement to notify all mergers or acquisitions. As discussed, the setting of financial thresholds is arbitrary and cannot be justified on the grounds that transactions falling below these thresholds are less likely to have anti-competitive effects. Some countries also use market share thresholds. While this can be defensible on the basis that a market threshold would exclude transactions which have potentially minimal impact in the affected markets, there is a potential for disagreement about the definition of the market(s) for which market shares shall be computed.[495]

The test of integration is designed to identify those situations, where as a result of the proposed transaction, the parties cease to operate completely independently. Typically countries which use the test as the basis for notification focus on the concept of control. In merger review regimes with a notification system which does not use notification as a basis for the application of the merger assessment standard a test of integration is not essential. For example, the notification system in the United States does not have a test of integration. In merger regimes, which de-couple notification and assessment (for example, the United States and Canada), the number of

495 The lack of objectivity of a market share threshold is discussed in "Recommended Practices for Merger Notification Procedures", International Competition Network, Mergers Working Group, Recommended Practice IIB, Comment 1.

transactions that may be reviewed under the applicable assessment standard is significantly greater than the number that is notifiable. Similarly, in countries without a mandatory notification system such as in the United Kingdom, Australia and New Zealand, virtually all mergers or acquisitions may be subject to review under the merger assessment standard. Conceptually, a notification requirement for merger transaction should be seen as a disclosure system whereby enforcement agencies are given notice of certain transactions before their completion. In deciding which transactions should be subject to notification, a principal consideration is the burden that it would have on business. Similarly, consideration also has to be given to the workload a notification system would place on the enforcement agency. If all merger transactions were notifiable, that requirement would be seen as a heavy burden on business and on the reviewing agency.

The use of financial thresholds as a notification requirement reflects a choice that only those transactions with a significant monetary impact on the economy should be subject to review.[496] By implication those transactions that are below the financial thresholds are deemed to have a less significant monetary impact. It does not mean, of course, that transactions above the thresholds are more likely to raise competition issues than those falling below.

4. ASSESSMENT STANDARD

Most countries have adopted a SLC standard or a SIEC standard, which are considered to be very similar. The SIEC standard of the European Commission Merger Regulation has been adopted by most EU Member States in aligning their national merger review laws with those contained in the European legislation.[497] A notable exception is Germany, an EU Member State, which continues to employ a dominance standard.[498]

The commonality of the SLC standard and the SIEC standard lies in the focus on the effects on competition. This is also evident from the assessment standards that

496 Limiting the notification requirement to large transactions may also reflect the view that such transactions are better able to afford the cost involved in making a notification filing.

497 In the original EC Merger Regulation the assessment standard was the dominance standard: Article 2. The EC Merger Regulation of 2004 changed Article 2 of the original EC Merger Regulation by adopting the SIEC standard which is very similar to the SLC standard; see Article 2(3) which states "A concentration which would significantly impede effective competition, in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position, shall be declared incompatible with the common market".

498 Article 36(1), *Gesetz gegen Wettsbewerbsbeschränkungen* ("*GWB*") (Act against Restraints of Competition).

are used by some countries such as Japan and Korea[499] that do not follow a strict SLC or SIEC standard. Some countries, such as Brazil and Turkey[500] have a standard incorporating both a dominance standard and a SLC/SIEC standard. While all standards pursue the same objective, the SLC/SIEC standard is inherently more flexible than the dominance one in dealing with all types of competition issues arising from a merger transaction including unilateral effects from a non-collusive oligopoly and co-ordinated effects arising in any transaction.[501] This inherent flexibility of the former is acknowledged by the migration in a number of countries from the dominance standard to the SIEC/SLC including the European Union in adopting the EC Merger Regulation in 2004, Australia in 1992 in amending section 50 of the *Trade Practices Act 1974* and New Zealand in 2001 in amending the *Commerce Act 1986*. The United Kingdom adopted a SLC standard in amending its merger laws by Part 3 of the *Enterprise Act 2002*.

5. LINK BETWEEN TEST FOR NOTIFICATION AND APPLICATION OF ASSESSMENT STANDARD

As noted above, in merger review regimes where the test for notification determines the jurisdiction to apply the assessment standard, the scope for the application of the assessment standard is limited to transactions that are notifiable. In countries where the test for notification is de-coupled from the jurisdiction to apply the assessment standard (for example, the United States and Canada) or where there is no compulsory notification system (for example, the United Kingdom, Australia and New Zealand), generally few merger transactions are not in principle subject to merger review.

Merger laws that de-couple a test for notification from jurisdiction to apply the assessment standard reflect the view that a merger transaction may have anti-competitive effects in one or more markets regardless of the size of the parties or their market shares or whether control (or something less such as decisive influence) is being acquired. This view is consistent with the view underlying the laws against anti-competitive agreements and abusive unilateral conduct that anti-competitive conduct may arise regardless of the size of the parties or the markets affected.

499 *Monopoly Regulation and Fair Trade Act*, which was originally enacted in 1980.

500 *Act on the Protection of Competition Act* (No. 4054 of 13 December 1994).

501 For a general discussion about the differences between assessment standards, see "Issues Paper" of the Secretariat for Roundtable on the Standard for Merger Review, with a Particular Emphasis on Country Experience with the Change of Merger Review Standard from the Dominance Standard to the SLC/SIEC Test, Organisation for Economic Co-operation and Development, 9 June 2009, DAF/COMP/WP3(2009)1.

6. MINORITY SHAREHOLDING ISSUE

It is generally recognised that minority shareholding in another competitor may have unilateral or coordinated anti-competitive effects.[502] There are few reported merger cases challenging a minority shareholding.[503]

The ability of merger review regimes to deal with competition issues raised by such minority shareholdings is directly attributable to whether the jurisdiction to apply the merger assessment standard exists only for transactions that are subject to (compulsory) notification. A transaction that results in a minority shareholding with control (*de jure* or *de facto*) is usually treated in the same way as an acquisition of all or a majority of the shares of the target competitor. A transaction that results in less than control (*de jure* or *de facto*) is a challenge for merger regimes in which notification is a pre-condition for the application of the assessment standard. For many regimes in which a transaction can only be reviewed if it is notifiable, a transaction involving the acquisition of a minority shareholding of less than control cannot be assessed. This is certainly the case in the EU and EU Member States that aligned their national merger laws to the EU laws. This limitation under the European Merger Regulation can be illustrated by the 2006 takeover bid by Ryanair, the low-cost airline based in Ireland, of is main rival, Aer Lingus, another Irish-based airline. By Decision C(2007) 3104 of 27 June 2007 in Case COMP/M.4439,[504] the Commission prohibited the takeover bid by Ryanair.

During the proceedings leading up to the prohibition decision, Aer Lingus asked the Commission to require Ryanair to sell its minority shareholding of 25.17 percent stake in former (which was subsequently increased after the decision to 29.4 percent). The Commission in Decision C(2007) 4600 of 11 October 2007 finally rejected the request[505] on the grounds that it had no jurisdiction to do so because the acquisition of the minority shareholding was not a 'concentration' for the purposes of the EC Merger Regulation.

502 See, for example, "Background Note" of the Secretariat for Roundtable on Antitrust Issues Involving Minority Shareholdings and Interlocking Directorates", Organisation for Economic Co-operation and Development, 19 February 2009, DAF/COMP/WP3(2008)1 ("Background Note for OECD Roundtable on Minority Shareholdings").

503 "Background Note for OECD Roundtable on Minority Shareholdings", para. 54. The simple reason may be that few merger review systems take jurisdiction to review transactions involving minority shareholdings below the level of *de jure* or *de facto* control.

504 The decision is under appeal to the Court of First Instance under Case No. T-342/07.

505 Aer Lingus filed an appeal to the Court of First Instance under Case No. T-411/07 R. Its application for interim measure was rejected by the President of the Court in a decision of 18 March 2008.

Under a merger review regime with jurisdiction for a substantive review founded on notification,[506] the solution to the minority shareholding problem is not simply to adopt a rule requiring notification for minority shareholdings exceeding a specified percentage, such as 25 percent as is the case under the German laws.[507] The potential anti-competitive issues are not necessarily more likely if the minority shareholding in a transaction exceeds the above value. If it is accepted that a percentage threshold like 25 percent is seen to be arbitrary, the problem is not solved by extending the notification requirement to transactions below the level of control such as where the acquiring business will achieve 'significant influence' or 'material influence' over the acquired business. Since these terms will not and are not intended to have a precise meaning, the approach would undermine the importance of having certainty about whether a transaction is notifiable or not.

Merger regimes that de-couple its notification system from the application of the assessment standard are more flexible. In such merger regimes, it is not inconsistent to have a precise set of requirements for notification and an assessment standard that may apply to virtually all mergers or acquisitions. The simple reason is that notification is simply a disclosure obligation and not a pre-condition for assessment.

In conclusion, the potential competition issues that arise from minority shareholdings cannot be addressed satisfactorily in merger regimes where the test for notification determines whether the assessment standard may be applied since notification requirements are inherently arbitrary from the perspective of applying the assessment standard.

7. NON-COMPETITION ISSUES IN MERGER REVIEW

In merger review the public interests other than competition issues are often used to justify a transaction.[508] Public interests can arise in several ways.

506 Background Note on OECD Roundtable on Minority Shareholdings for a brief discussion about the consideration of the idea of requiring notification of passive minority shareholdings (not involving control) in the consultation by the Commission to revising the 1989 EC Merger Regulation. The idea was ultimately not adopted in the 2004 EC Merger Regulation.

507 Article 37, *GWB*.

508 For convenience, we use the term 'public interests' to refer to public interests other than competition policy interests.

First, they can be part of the legislation regulating an industrial sector such as telecommunications, media, banking or defence, or laws regarding national security or foreign ownership. In each case, the review is done in pursuit of objectives that are not necessarily consistent with the goals of competition law and policy. The effects of such legislation and regulations and rules made thereunder are that some transactions may have to comply with both a regulatory as well as a competition review. The existence and application of special laws to certain mergers do not necessarily undermine the enforcement of the competition merger laws. It comes from the recognition that there are public objectives other than those pursued by competition laws and policy. However, where the regulatory authority is also authorised to consider competition issues, there is a potential for that agency to come to views that may be inconsistent with those of the body conducting a separate review under competition merger laws.

Second, many countries have provisions in their merger laws that authorise the government to make the final decision on a transaction. For example, under section 58 of the *Enterprise Act 2002* (United Kingdom), the Secretary of State for Business, Enterprise & Regulatory Reform (now Business, Innovation and Skills) may invoke public interests grounds such as national security to clear a deal.[509] Similar provisions in merger laws exist in other countries such as France[510] and Germany,[511] even if such provisions are rarely used.

Under section 7 of the *Credit Institutions (Financial Support) Act 2008* (Ireland), the Minister for Finance may take over from the Competition Authority the role for reviewing a banking transaction which in his opinion raises serious concerns about the stability of the financial system. If the Minister concludes that such a deal will result in a substantial lessening of competition, he may still clear the merger by invoking public interest criteria such as the stability of the financial system, financial institutions or economy.

A provision reserving the right of the government to make the final decision on a merger for non-competition objectives is not necessarily inconsistent with competition policy. Typically the final decision is made by the relevant government minister after the competition agency has completed its review.

509 Section 58 was invoked by the Secretary of State in clearing the Lloyds Bank/HBOS merger: see, Merger Action Group v Secretary State [2008] CAT 34.

510 L-430-7-1, *Code de commerce* (as amended by *la loi de modernisation de l'économie* of 4 August 2008).

511 Article 42, *GWB*.

One may, however, question the wisdom of having the same person or body, as is the case under the Irish legislation, to both decide whether the transaction will or will not lessen competition substantially, and if so, whether to clear the merger on other public interests grounds. Third, a not insignificant number of countries incorporates non-competition public interests into their merger assessment standard. The countries with such a requirement include Poland, Czech Republic,[512] South Africa, Taiwan, China. The Polish agency may consider such non-competition issues as the contribution of the merger on to the national economy and economic or technological development. In South Africa, the impact on employment and investment must be considered. In Taiwan[513] the Fair Trade Commission may take into account the overall contribution to the economy from the transaction. In China, the relevant authority may consider whether the merger was made pursuant to public interests.[514]

While there may be good public policy grounds for giving the agency the powers to consider non-competition goals, one wonders what principles should be applied for balancing the effects of a merger on competition with the promotion of non-competition goals. There is a need to articulate these principles. Otherwise, the value of the competition agency as an independent, expert body may rightfully be called into question.

512 *Consolidated Act on the Protection of Competition (No. 143/2001).*

513 *Fair Trade Law of 1991.*

514 Article 28, *Anti-Monopoly Law.*

Chapter III

GRANTING AND MONITORING OF STATE AID

Barbara Brandtner[515]

STATE AID REFORM – THE STATE AID ACTION PLAN

1. INTRODUCTION

In 2005, the European Commission launched its first ever comprehensive reform of State aid rules and procedures – the State Aid Action Plan (hereinafter also referred to as the "Action Plan"). This contribution will first explore the Commission's reform objectives and methodologies, then present the texts which, in the author's view, represent the Action Plan's main achievements,[516] in three sub-headings: State aids in a Lisbon perspective; Cutting administrative red tape; Procedural simplification, and better enforcement. This article concludes with a first evaluation of the results achieved.

2. THE COMMISSION'S REFORM OBJECTIVES AND METHODOLOGIES

Ever since the Founding Treaties, the purpose of State aids policy has been to preserve the EU Single Market by ensuring that competition therein is not distorted. If targeted at the right objectives, State aid measures can be very valuable tools for Member States to pursue legitimate common interest objectives. On the other hand, unfettered State aid can prevent market forces from rewarding the most innovative and competitive enterprises, and be abused to partition-off the Single Market, or to build market power in the hands of the selected few. This is why State aids control is necessary to preserve a level playing field between undertakings and Member States, and why the Treaty on the Functioning of the European Union (hereinafter referred to as the "TFEU")[517] has charged the European Commission with the task of ensuring that State aid planned, or granted by Member States does not unduly distort competition in the Single Market.

515 The content of this article does not necessarily reflect the official position of the European Commission. Responsibility for the information and views expressed lies entirely with the author. Sincere thanks to Dr. Paul Adriaanse, Leiden University, for his invaluable help and comments.

516 An exhaustive presentation of all texts revised under the SAAP would far exceed the scope of this Article. In this respect, please see e.g. P. Heidhues, R. Nitsche, "Comments on State Aid Reform – some Implications of an Effects-based Approach", EStAL 2006/1, 23-34; Th. Kleiner, "Reforming state aid policy to best contribute to the Lisbon Strategy for growth and jobs", Competition Policy Newsletter 2005, no. 2, p. 29-34; A. Bartosch, "Comments on Commissioner Kroes' New State Aid Action Plan", EStAL 2005, no. 3, p. 391-392.

517 Articles 107–109 of the TFEU (the former Articles 87-89 of the EC Treaty).

In its exercise of this function, the Commission had over time developed a significant number of detailed rules and case practice to guide Member States in the design of their measures. State aids policy, however, was facing two concrete challenges, which led the Commission to announce the Action Plan.

2.1 THE LISBON CHALLENGE

At the very start of President Barroso's mandate, the Commission announced the renewed Lisbon Strategy for growth and jobs.[518] Re-orienting national State aid measures towards horizontal objectives of common interest was recognized as a promising way for Member States to implement this ambitious strategy. The first objective of the State Aid Action Plan was therefore „less and better targeted State aid" – a goal long recognized by successive European Councils.[519] While Member States were thus encouraged to successively reduce overall aid amounts, State aid measures were to be targeted at the specific "Lisbon objectives" – innovation, environmental protection, but also better public services, regional cohesion, human capital, as well as more and better jobs.

In order to achieve this goal, the Action Plan introduced a refined economic approach to State aids analysis[520] as a new tool to better target State aid at horizontal interest objectives. In the first place, this assumes that the existence of market failures, such as externalities, imperfect information, or coordination problems, public goods or market power, may stand in the way of the market achieving by itself certain desired common interest objectives.[521]

518 Communication to the Spring European Council: "Working together for growth and jobs. A new start for the Lisbon Strategy" of 2 February 2005 (COM (2005) 24).

519 Conclusions of the European Council, Lisbon, March 2000, para. 16-17; Stockholm, March 2001, para. 20; Barcelona, March 2002, para. 18; Brussels, March 2003, para. 26; Brussels, March 2005, para. 23.

520 On the refined economic approach, see e.g. H.W. Friederiszick, L.-H. Röller, V. Verouden, *European State Aid Control: an economic framework*, paper, September 28th, 2006; H.W. Friederiszick, L.-H. Röller, "Using economic analysis to assess R&D&I State aid measures", *EStAL* 2007, no. 4, p. 592-604; D. Neven, V. Verouden, "Towards a More Refined Economic Approach in State aid Control", (in:) W. Mederer, N. Pesaresi, M. van Hoof (eds.), *EU Competition Law – Volume IV: State aid,* Claeys & Casteels 2008. See also the Common Principles for an Economic Assessment of the Compatibility of State aid under Article 87(3) of the EC Treaty [now Article 107(3) of the TFEU] (Draft paper for consultation on DG Competition's website (http://ec.europa.eu/competition/state_aid/reform/reform.html).

521 In the area of fundamental research, for example, market players are generally not able to reap the full economic benefits of their discoveries, because they cannot entirely appropriate the resulting general knowledge (positive externality). As a result, the companies concerned will not be willing to invest in research at the level which would otherwise be optimal for society. Unless this imbalance is addressed and an incentive created (by State support or other, e.g. regulatory, means), the free play of market forces will thus produce a sub-optimal outcome (market failure).

The presence of market failures is, therefore, one of the main reasons to justify granting State aid for common interest objectives of an economic nature.[522]

However, the existence of a market failure (or other common interest objective) is insufficient on its own to justify State aid. Therefore, the refined economic approach relies on what has been called the „balancing test"[523] to analyse whether a planned State aid measure is in the common interest and may therefore be approved:

- Does the measure target a well-defined market failure or other common interest objective?

- Is the aid well designed to deliver the common interest objective? In particular:
  - Is State aid an appropriate policy response to the market failure/common interest objective?[524]
  - Is there an incentive effect, i.e. does the aid change the behaviour of aid beneficiaries?
  - Is the aid proportional to the market failure/common interest objective, i.e. could the same effect be obtained with less aid?

- Are the distortions of competition and effects on trade limited, so that the overall balance is positive?

All substantive texts adopted in implementation of the Action Plan incorporate, or at least reflect the application of this approach. Their main content will be presented further below.

522 By far not all common interest objectives are economic in nature. Regional cohesion for example cannot be justified by the existence of market failures (since it is in fact the free play of market forces which 'produces' more or less developed regions). Social (e.g. redistribution, regional development or functioning public services) or cultural common interest objectives are therefore just as important justifications for State intervention as market failures.

523 See point 1.3. of the R&D&I Framework, OJ C 323 of 30.12.2006, p. 1-26; at p. 5.

524 While the Action Plan (para. 8) noted that "State aid does not come for free" (since it has opportunity costs in the sense of possibly diverting scarce public funds from other essential purposes, such as health, education, social protection etc.), this does not mean that the Commission would substitute its own judgment for that of Member States in determining whether State aid may be granted for certain objectives or not. The aim of this condition is to ensure that State aid is one of the possible policy responses to the problem identified, not that it is the only (let alone the "best") one. Only in those rare cases where State aid is clearly not the answer, will a planned measure therefore fail this part of the test. In this respect, see Commission Decision of 9 November 2005 on the State Aid which the Federal Republic of Germany has implemented for the introduction of digital terrestrial television (DVB-T) in Berlin-Brandenburg (2006/513/EC, OJ No L 200 of 22.07.2006); recently confirmed by CFI judgment of 6 October 2009, Case T-21/06, Germany/Commission, n.y.r.

2.2 THE SIMPLIFICATION CHALLENGE

By the time of the Action Plan, the Commission had come to realize that "organic" growth of State aids policy had reached its limits: in shaping State aids policy over the course of decades, the Commission had adopted a long list of State aid rules – frameworks, guidelines, notices, block exemptions, etc. – the increasing number and complexity of which called for streamlining and 'pruning'. The 2004 enlargement, which had brought ten new Member States to the European Union, including Poland, only reinforced this generally perceived need for more predictable and user-friendly rules, more transparency and better governance to ensure effective State aids control across the enlarged EU.

The Commission's second objective was, therefore, one of simplification: devising better rules in order to ensure higher predictability and enhanced transparency, coupled with more effective procedures and better enforcement was recognized as the most appropriate means to ensure that State aids policy would be understood and applied by all stakeholders according to the same standards, and properly enforced when required.

The Commission, however, well realized that the comprehensive State aids reform it had envisaged could not be its responsibility alone. If it was to be successful, this could only be achieved in partnership with Member States and all other stakeholders (industry, small and medium-sized enterprises (SMEs), the legal community, academia, etc.), and in full recognition of the shared responsibility of State aid granting authorities in the proper implementation of State aid rules. In this respect, the Action Plan was in fact an invitation to all interested stakeholders to make a 'deal' with the Commission: on its part, the Commission would do all it could to make State aids law and practice simpler, more transparent and user-friendly – but this required the effective support of Member States and their full commitment to "play by the (new) rules".

As the first instance of this cooperative approach's implementation, the Action Plan was subject to a large public consultation,[525] which raised considerable interest: 134 contributions were received from 23 countries (including 2 non-EU); 20 Member States replied, as did 25 regions, or regional associations, 35 business

525 See http://ec.europa.eu/competition/state_aid/reform/comments_saap/index.html. This lasted from 7 June 2005 (adoption of the Action Plan) to (officially) 15 September 2005. All texts produced under the Action Plan were also submitted to public consultation.

federations, 14 individual companies, 10 trade unions, 9 regional public-private partnerships, 8 law firms or legal associations, 5 non-business associations, 4 institutions, and 4 academics. Overall support came out strong: most respondents explicitly supported the reform, its main objectives and components. Nevertheless, a limited number of proposals did not meet with general support (some even faced outright opposition), and consequently they were not implemented.[526]

3. THE MAIN ACHIEVEMENTS

In keeping with the strong stakeholder support the Action Plan generated, the Commission immediately set out to implement its numerous reform proposals. Over the course of the Commission's mandate (2005-2009), all major State aid texts were therefore reviewed[527] and most of them fundamentally modernized. The sheer magnitude of the reform far exceeds the scope of this commentary. Having the above in mind, this section will review the texts which, in the author's view, constitute the milestones of State aid reform under the Action Plan, and its most lasting contribution to modern State aids policy and practice.

3.1 STATE AID IN A "LISBON" PERSPECTIVE

The main substantive rules adopted by the Commission in implementation of the "Lisbon" objectives – Research, Development and Innovation (R&D&I), Risk Capital and Environmental Protection – probably constitute the best examples of the Commission's application of the refined economic approach in its purest form.

Firstly, all texts reflect clear market-failure logic and contain the types of measures considered most appropriate to remedy the market failures identified. Second, their structure follows economic reasoning, with a "standard assessment" regrouping the types of measures where *ex ante* economic analysis has led the Commission to conclude on their likely compatibility (nowadays mostly

526 The perhaps most prominent example was the Commission's attempt at State aid decentralization: inspired by the very positive experience gained in a pre-accession context with the Competition and State aid authorities of the then Candidate Countries (like UOKiK), the Action Plan (para. 51) announced the Commission's intention to "examine whether independent authorities in Member States could play a role as regards facilitating the task of the Commission in terms of State aid enforcement". But this met with the highest disapproval rate of all reform proposals (with 15 mostly private respondents welcoming the idea, while 28 mostly public respondents questioned or rejected it). This idea was therefore abandoned and private enforcement (before national judges) developed instead (see below part 2.3.3).

527 Latest versions of all State aid texts can be consulted at DG Competition's website (http://ec.europa.eu/competition/state_aid/legislation/legislation.html).

block-exempted, see part 3.2.2 below), and a „detailed assessment" implying full application of the balancing test on a case-by-case basis for the measures whose size or specific design may give rise to serious competition concerns. Finally, and again in keeping with the market failure reasoning, all measures, to the extent they are not limited to SMEs,[528] contain consistent SME bonuses reflecting the varying intensity of market failures faced by small or medium-sized companies;[529] the former „regional bonus" has been abandoned.

3.1.1 THE R&D&I FRAMEWORK

The Commission's traditionally favourable attitude to State aid for research and development (R&D) had long found its reflection in successive R&D Frameworks.[530] Since the renewed Lisbon Strategy had recognized the need to invest more in knowledge and innovation, the Commission had to consider how best to expand the existing rules to these areas. To this effect, the Commission first adopted a Communication on State aid and Innovation.[531] On this basis, a whole series of new measures and novel features was introduced into the 2006 R&D&I Framework.[532]

First and foremost, the traditional stage of "pre-competitive development", which had so far explicitly excluded innovation,[533] was expanded to "experimental development",[534] and now includes all innovative stages in the production or design of new, altered or improved products, processes or services. A much broader category of activities thus becames eligible for State support. In addition, the "standard assessment part" of the Framework now contains five new innovation-related support measures: aid for young innovative enterprises; aid for process and organisational innovation in services; aid for innovation advisory and support services; aid for the loan of highly

528 Like the Risk Capital Guidelines.

529 20 percent SME-bonus for small enterprises, 10 percent for medium-sized ones.

530 Community Frameworks for State aid for R&D (OJ C 83 of 11.04.1986; OJ C 45 of 17.02.1996).

531 Communication on Innovation of 21 September 2005 (COM (2005) 436 final).

532 Community Framework for State aid for Research and Development and Innovation (OJ C 323 of 30.12.2006).

533 See point 2.3 of the 1996 R&D Framework (loc cit.).

534 According to point 2.2 (g) of the 2006 R&D&I Framework "experimental development" means the acquiring, combining, shaping and using of existing scientific, technological, business and other relevant knowledge and skills for the purpose of producing plans and arrangements or designs for new, altered or improved products, processes or services. These may also include, for example, other activities aiming at the conceptual definition, planning and documentation of new products, processes and services. The activities may comprise producing drafts, drawings, plans and other documentation, provided that they are not intended for commercial use.

qualified personnel; and aid for innovation clusters.[535] Existing rules on the financing of research organisations and innovation intermediaries, contract research, and the collaboration of undertakings have been clarified.[536] Finally, in a specific effort to foster cross-border cooperation, the Framework includes a new (unfortunately, so far largely unused) section on R&D&I aid to promote the execution of important projects of common European interest.[537]

3.1.2 THE RISK CAPITAL GUIDELINES FOR SMES

Since the first Communication on State Aid and Risk Capital for SMEs had only been adopted in 2001[538] and already reflected a modern market failure approach, the main modification introduced by the 2006 Risk Capital Guidelines[539] is to increase the "safe-harbour threshold"[540] for risk capital investment in SMEs in their early development stages to 1.5 million euros over twelve months, a 50 percent increase compared to the previous Communication. Above this threshold, and/or if certain "safe-harbour" conditions are not met (e.g. in the case of insufficient private contribution of venture capital), measures will be subject to "detailed assessment".

3.1.3 THE ENVIRONMENTAL AID GUIDELINES

Given the generally recognized common interest objective of supporting environmental protection, successive Environmental Aid Guidelines had governed this part of State aids discipline since 1994.[541] In keeping with the Energy and Climate Change Package presented by the Commission to the 2007 Spring European Council,[542] and the European Council's decision to set ambitious targets for a 20 percent reduction of greenhouse gas emissions,

535 See points 5.4-5.8 of the R&D&I Framework (loc. cit.).

536 See points 3.1 and 3.2 of the R&D&I Framework.

537 See point 1.4 of the R&D&I Framework (based on Article 87(3)(b) of the EC Treaty).

538 Communication on State aid and risk capital (OJ C 235 of 21.8.2001).

539 Community Guidelines on State aid to promote risk capital investments in small and medium-sized enterprises (OJ C 194 of 18.8.2006).

540 The investment amount up to which the Commission considers that aid in the form of risk capital may generally be considered compatible with the Treaty. This corresponds to the level at which the Commission found a market failure for access to risk capital by SMEs in all Member States.

541 Community Guidelines on State aid for environmental protection (OJ C 72 of 10.3.1994; OJ C 37 of 3.2.2001).

542 Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions - Limiting global climate change to 2 degrees Celsius - The way ahead for 2020 and beyond of 10.1.2007 (COM (2007) 2 final).

and a 20 percent share of renewable energy in total EU energy consumption by 2020[543], the 2008 Guidelines[544] considerably expand Member States' possibilities to financially support environmental protection, while staying committed to the polluter pays principle (PPP) and market-based instruments (such as emission-trading).

The Guidelines recognize that there may be situations in which the PPP can not be properly implemented if the costs of pollution are not fully accounted for by industry, and where State aid may therefore be justified as a means to incentivize undertakings to change their behaviour and adopt more environmentally friendly processes, or invest in greener technologies.[545] In particular, State aid may be granted to implement national environmental standards exceeding Community standards, or for their early implementation.[546] Both investment and operating aid may be granted for energy saving, the production of renewable energy, and energy-efficient cogeneration.[547] New rules are introduced as regards aid for district heating, waste management and aid involved in tradable permit schemes.[548]

Very generous aid intensities shall apply,[549] and even 100 percent aid intensities are allowed if a project has been awarded aid following a genuinely competitive bidding process.[550] Finally, Member States may grant long term derogations from certain environmental taxes, as long as the companies concerned pay at least the Community minimum; below the Community minimum, derogations remain possible, subject to detailed assessment.[551]

543 Conclusions of the European Council, Brussels, March 2007, para. 32.

544 Community Guidelines on State aid for environmental protection (OJ C 82 of 1.4.2008), [hereinafter referred to as the "EAG"].

545 See section 1.2, paras. 6-10 of the EAG (loc. cit., p. 5).

546 Section 3.1.1 and 3.1.3 of the EAG (specific rules apply to the acquisition by undertakings of 'green transport vehicles' exceeding or preceding mandatory Community standards).

547 Sections 3.1.5 to 3.1.7 of the EAG.

548 Sections 3.1.8, 3.1.9 and 3.1.12 of the EAG.

549 A range of 50-60 percent as regards investment aid for large enterprises, increased by the usual SME bonuses; where an investment involves eco-innovation, an "eco-innovation bonus" of 10 percent may be added. Operating aid for renewable energy production or cogeneration may cover the full difference between production costs and the market price (see sections 3.1.5.2, 3.1.6.2 and 3.1.7.2 of the EAG).

550 See section 3.1.5.1., para. 97 of the EAG (investment aid for energy saving); section 3.1.6.1., para. 104 of the EAG (investment aid for renewable energy); section 3.1.7.1, para. 116 of the EAG (investment aid for cogeneration); and section 3.1.8, para. 123 (investment aid for district heating).

551 See section 4 of the EAG.

3.2 CUTTING ADMINISTRATIVE RED TAPE

State aid is, in principle, prohibited by Article 107 of the TFEU – unless the Commission finds a measure compatible with the Internal Market, following the aid's notification by the Member State concerned. Member States may not put the aid into effect until the Commission's decision ("standstill obligation", Article 108(3) of the TFEU). In its "pure" form, this system thus requires prior notification of all measures.

If there had been a way to significantly simplify Member States' tasks and thereby visibly reduce the administrative burden it was exempting Member States from prior notification in certain cases. Therefore, already in 1999, the Council adopted the Enabling Regulation[552] empowering the Commission to block-exempt certain well-defined aid categories, on whose basis several block exemptions,[553] and a first formal *de minimis* Regulation[554] were adopted. One of the main objectives of the Action Plan was to consolidate and expand these measures.[555]

3.2.1 THE NEW *DE MINIMIS* REGULATION

The Commission's *de minimis* policy dates back to 1992. It holds that certain State support measures will not be considered State aid in the sense of Article 107(1) of the TFEU, since it is unlikely that they would be able to distort competition, or affect trade because of their limited size. While *de minimis* is thus administrativelyvery convenient for relieving Member States of their

552 Council Regulation (EC) No 994/98 of 7 May 1998 on the application of Articles 92 and 93 of the Treaty establishing the European Community [now Articles 107 and 108 of the TFEU] to certain categories of horizontal State aid (OJ L 142 of 14.05.1998).

553 Commission Regulation (EC) No 1628/2006 of 24 October 2006 on the application of Articles 87 and 88 of the Treaty [now Articles 107 and 108 of the TFEU] to national regional investment aid (OJ L 302 of 1.11.2006); Commission Regulation (EC) No 2204/2002 of 12 December 2002 on the application of Articles 87 and 88 of the EC Treaty [now Articles 107 and 108 of the TFEU] to State aid for employment (OJ L 337 of 13.12.2002); Commission Regulation (EC) No 70/2001 of 12 January 2001 on the application of Articles 87 and 88 of the EC Treaty [now Articles 107 and 108 of the TFEU] to State aid to small and medium-sized enterprises (OJ L 10 of 13.1.2001); Commission Regulation (EC) No 364/2004 of 25 February 2004 amending Regulation (EC) No 70/2001 as regards the extension of its scope to include aid for research and development (OJ L 63 of 28.2.2004); Commission Regulation (EC) No 68/2001 of 12 January 2001 on the application of Articles 87 and 88 of the EC Treaty [now Articles 107 and 108 of the TFEU] to training aid (OJ L 10 of 13.1.2001).

554 Commission Regulation (EC) No 69/2001 of 12 January 2001 on the application of Articles 87 and 88 of the EC Treaty [now Articles 107 and 108 of the TFEU] to *de minimis* aid (OJ L 10 of 13.1.2001).

555 Every text adopted under the Action Plan contains some elements of simplification. See for example the simplified valuation grids for guarantees to SMEs in the Commission Notice on the application of Articles 87 and 88 of the EC Treaty [now Articles 107 and 108 of the TFEU] to State aid in the form of guarantees (OJ C 155 of 20.6.2008). Exploring them all far exceeds the scope of this article.

notification duty in small cases, it has never been the Commission's favoured instrument.[556]

Despite strong Member States' calls for a considerably higher increase of the *de minimis* threshold, and to reflect the economic developments since 2001 (mostly inflation), the 2006 Regulation[557] has doubled[558] the amount of exempted *de minimis* support to 200.000 euros over any period of three years[559]; in addition, and to cater for easy access to guarantees by SMEs in particular, a new specific *de minimis* threshold has been introduced for loan guarantees, where the guaranteed amount of the loan does not exceed 1.5 million euros.[560]

In order to avoid abuses (and in full respect of the refined economic approach), forms of aid whose inherent amount cannot be precisely determined in advance (so-called "non-transparent aid")[561] and aid to firms in difficulties have been excluded,[562] while coupling *de minimis* with other State aid covering the same eligible costs has been prohibited.[563]

3.2.2 THE GENERAL BLOCK EXEMPTION REGULATION (GBER)

By all accounts, this is probably the centrepiece of the State Aid Action Plan.[564] Until the adoption of the GBER, block-exempted measures (14 in total) had been spread out over five block exemption regulations (BERs),[565] each subject to different definitions, eligibility criteria, aid ceilings, cumulation rules, etc. The first and technically most demanding task of the GBER was, therefore, to harmonize the applicable definitions and horizontal rules of all existing BERs and regroup

556 *De minimis* is only defined by its size; it can thus in principle cover investment and operating costs, all sectors, all activities. This increases its practicability – but significantly reduces its value as a State aid "targeting instrument" under the refined economic approach.

557 Commission Regulation (EC) No 1998/2006 of 15 December 2006 on the application of Articles 87 and 88 of the Treaty [now Articles 107 and 108 of the TFEU] to de minimis aid (OJ L 379 of 28.12.2006).

558 The 2001 *de minimis* Regulation had set the threshold at 100.000 euro over three years (see footnote 39 above).

559 Article 2(2) of the Regulation; a reduced ceiling of 100.000 euro applies to road transport undertakings.

560 Article 2(4) (d) of the Regulation; a reduced ceiling of 750.000 euro applies to road transport undertakings.

561 Article 2(4) of the Regulation.

562 Article 1(h) of the Regulation.

563 Article 2(5) of the Regulation.

564 Commission Regulation (EC) No 800/2008 of 6 August 2008 declaring certain categories of aid compatible with the common market in application of Articles 87 and 88 of the Treaty [now Articles 107 and 108 of the TFEU] (OJ L 214 of 9.8.2008). The GBER entered into force on 29 August 2008 (twenty days following its publication in the O.J.).

565 See above footnote 38.

them in a first horizontal part of the GBER[566] to be applicable to, and respected by all future block-exempted measures.

Particularly important in this context are the new rules on incentive effect,[567] a clear reflection of the refined economic approach to State aid policy: while block-exempted aid for SMEs will be considered to have an incentive effect if the beneficiary applied for aid before the start of works on the project, Member States will need to verify the incentive effect as regards large companies before granting the aid concerned, based on documentation prepared by the beneficiaries.[568]

Besides this harmonisation effort, the most tangible added value of the GBER stems from its considerably enlarged scope: 26 types of measures have been block-exempted; they cover all currently „block-exemptable" areas;[569] all of them are open to SMEs, but a significant number can also be used for large companies (in this case the general SME bonuses apply).[570] Within the limits of the existing Enabling Regulation, the Commission has thereby block-exempted most measures subject to „standard assessment" under the major Frameworks and Guidelines adopted under the Action Plan.

566 See Chapter I of the GBER ("Common Provisions"). Apart from the definitions and general eligibility criteria, such as the transparency-requirement of block-exempted aid measures (see text to footnote 46 above), aid intensity and eligible costs, individual notification thresholds and cumulation rules, this Chapter also contains specific publicity, monitoring and reporting requirements: In particular, all block-exempted schemes need to have a national legal basis, publicly accessible as long as the measure is in force (Article 9).

567 See Article 8 of the GBER.

568 The criteria to be considered in this context include a material increase in the size or scope of the project or activity; a material increase in the total amount spent by the beneficiary on the project or activity, or in its speed of completion; and as regards regional aid, evidence that the project would not have been carried out as such in the assisted region concerned without the aid.

569 See Article 1 (1) of the Enabling Regulation (above footnote 37): aid to SMEs; R&D aid; environmental aid; aid for employment and training; and regional aid.

570 The following 17 GBER-measures are open to both large companies and SMEs: regional investment and employment aid (Article 13); investment to go beyond Community standards for environmental protection (Article 18); aid for the acquisition of new transport vehicles going beyond Community environmental standards (Article 19); investment aid for energy-saving, cogeneration and renewable energy (Articles 21-23); aid for environmental studies (Article 24); aid in the form of reductions in environmental taxes (Article 25); aid for R&D projects and technical feasibility studies (Articles 31-32); aid for R&D in the agricultural sector (Article 34); aid for innovation advisory services and innovation support services (Article 35); aid for the loan of highly qualified personnel (Article 37); training aid (Article 39); and aid for the recruitment of disadvantaged and disabled workers in the form of wage subsidies, and for compensating the additional cost of employing disabled workers (Articles 40-42). The remaining 9 measures are SME-specific: aid for newly created small companies in assisted regions (Article 14); SME investment and employment aid (Article 15); aid for small enterprises newly created by female entrepreneurs (Article 16); aid for the early adaptation to Community environmental standards for SMEs (Article 20); consultancy in favour of SMEs (Article 26); aid for SME participation in fairs (Article 27); risk capital measures (Articles 28-29); IPR costs for SMEs (Article 33); and aid for young innovative enterprises (Article 35).

This very generous administrative simplification has not come without checks and balances, however: most noteworthy in this context are the new monitoring rules, by virtue of which the Commission is empowered to subject block-exempted measures to regular *ex post* review. For this purpose, Member States must keep records for ten years after granting the aid, and provide the Commission with all information necessary upon request. In the case of lack of cooperation, the Commission may decide to withdraw the benefit of the block-exemption, in whole or in part.[571]

3.3 PROCEDURAL SIMPLIFICATION AND BETTER ENFORCEMENT

The rules governing State aid procedures are laid down in the 1999 Procedural Regulation (PR)[572] detailing the main procedural steps already set out in Article 108 of the TFEU: both unlawful (non-notified) aid and measures notified to the Commission are first subject to a preliminary examination (largely bilateral between the Commission and the Member State concerned), and then to a formal investigation initiated by formal decision, should the Commission have serious doubts on the measure. [573] In both stages of the procedure, the Commission can request all necessary information from the Member State concerned, if necessary through coercive means in the case of unlawful aid.[574] At the end of its investigation, the Commission can either approve the aid, or find that the measure does not constitute State aid in the meaning of Article 87 of the EC Treaty,[575] declare the aid compatible subject to certain conditions,[576] or declare the aid incompatible with the Internal Market, and order the recovery of unlawful aid.[577] In principle, the Commission has two months to complete the preliminary examination of

571 Article 10 of the GBER. As may be expected, this raised many comments during Member States' consultation. Nevertheless, it could finally be maintained because of its proportionality: Withdrawing the benefit of the whole GBER is clearly an *ultima ratio* in case of complete lack of cooperation; but there is also scope for limited or temporary withdrawal, or for a simple warning in case of more transient, temporary, or minor difficulties.

572 Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty [now Article 108 of the TFEU] (OJ L 83 of 27.3.1999). See further A. Bartosch, "The Procedural Regulation in State Aid Matters. A Case for Profound Reform", *EStAL* 2007, no. 3, p. 474-483; A. Sinnaeve, "State aid procedures: developments since the entry into force of the procedural regulation", *Common Market Law Review* 2007, Vol. 44, no. 4, p. 965-1033; A. Sinnaeve, P.J. Slot, "The New Regulation on State Aid Procedures", *Common Market Law Review* 1999, Vol. 36, no. 6, p. 1153-1194.

573 See Chapters II (notified aid) and III (unlawful aid) of the PR.

574 The Commission has three means at its disposal in this respect: an information injunction (Article 10(3) of the PR), a suspension injunction (Article 11(1) of the PR), and a recovery injunction (Article 11(2) of the PR).

575 Both after preliminary examination (Articles 4(2) and (3) of the PR) or formal investigation (Articles 7(2) and (3) of the PR).

576 "Conditional decision", Article 7(4) of the PR (only after a formal investigation).

577 "Negative decision" (Article 7(5) of the PR), or "recovery decision" (Article 14 of the PR); both are only possible following a formal investigation.

a complete notification; the formal investigation should not exceed eighteen months.[578] Specific (and more lenient) rules apply to existing aid, whose review by the Commission can normally lead only to its abolition or alteration.[579]

The Action Plan well recognized that simplifying only the substantive rules would not be sufficient to achieve the Commission's overall reform objective. In order to be truly effective, this had to be coupled with „more effective procedures, better enforcement, higher predictability and enhanced transparency."[580] In fact, State aids procedures had long been criticized as lengthy and unpredictable by Member States, and as particularly non-transparent, since being largely "bilateral" (Member State/Commission), for private stakeholders. As evidenced by the strong reaction to the Action Plan,[581] procedural reform was thus a necessity.

The Commission soon realised, however, that it had to balance the various conflicting needs and interests at stake (thoroughness vs. speed; privacy of deliberations vs. transparency, publicity and stakeholders' rights), including its own limitations: resource constraints would not allow the Commission to pursue all components of the Action Plan concomitantly and the partnership approach – and political realism – commanded not to antagonize Member States, or to overestimate the scope of the „achievable".[582]

578 See Articles 4(5) and (6) of the PR as regards the preliminary examination (the so-called "Lorenz"-provision reflecting the judgment of the ECJ of 11 December 1973 in Case 120/73, Gebrüder Lorenz GmbH v Federal Republic of Germany and Land Rheinland-Pfalz, ECR 1973, p. 1471), and Article 7(6) of the PR as regards the formal investigation (best endeavours-deadline). These deadlines can often not be respected in practice, however.

579 See Chapter V of the PR (the so-called "cooperation procedure" implementing Article 108(1) of the TFEU). The concept of "existing aid" is defined in Article 1(b) of the PR.

580 See para. 18 of the Action Plan.

581 The Action Plan's procedural reform proposals were addressed in 94 of the 134 contributions received during public consultation, and generated the second-highest response and support rate (after overall support for State aids reform). Nevertheless, this positive score needs to be nuanced in light of the diversity of the comments received: while procedural simplification as such proved largely welcome, the same was not true as regards specific simplification proposals concerning e.g. the linguistic regime to be applied (where the fact that the Commission has to deal with 27 Member States in their own language often causes considerable delay) or the granting of new investigative powers to the Commission (like in antitrust and mergers). On the other hand, increasing the procedural rights of beneficiaries and other third parties – though not part of the Commission's proposals - generated a significant response rate and interesting practical proposals (mostly from private parties).

582 Having to amend a Council Regulation based on Article 109 of the TFEU, subject to qualified majority in Council and simple consultation of the European Parliament, clearly gives Member States' interests a decisive weight in the decision-making process. Also, the time needed to complete all procedural steps required (starting with a compulsory impact assessment and public stakeholder consultation, via a first formal Commission proposal, followed by the negotiation phase in Council and Parliament and likely to include one or more revised Commission proposals) may well exceed the five years life-span of one Commission, even if launched immediately at the start of a mandate.

In slight deviation from the indicative roadmap announced in the Action Plan,[583] the Commission therefore opted for a "step-by-step" approach: first focus on the main substantive rules, then launch procedural reform. In this context, first, the focus is put on "best practices" (i.e. those procedural improvements which do not require legislative action), then on gaining experience in their application, and only later on deciding whether (and how) to reform the Procedural Regulation. The prime objective of procedural reform thus became to match the State aids architecture created via reforming the substantive rules (GBER; straightforward/standard assessment; detailed assessment) by corresponding procedural improvements concerning the conduct of State aid investigations, the fight against unlawful aid, and the effective enforcement of Member States' recovery obligation.[584]

The Commission's main product in this respect has since become known as the Simplification Package: the Simplified Procedure, the Best Practices Code, and the Enforcement Notice. These texts will now be presented in turn.

3.3.1 THE SIMPLIFIED PROCEDURE

The Simplified Procedure[585] is the Commission's procedural answer to the notification of simple, straightforward State aid measures based on the „standard assessment" sections of existing guidelines or frameworks (if not yet block-exempted), or on consolidated Commission decision-making practice (at least three precedents)[586]: if a notified measure meets all the conditions laid down in the Notice, the Commission endeavours to adopt a simplified approval decision within twenty working days after notification.[587]

In order to ease Member States' task of defining the "right" measures, the Notice contains a detailed list of aid categories being „in principle suitable", together with

583 This had in fact foreseen "internal best practices" already for 2005/2006, and a consultation and eventual Commission proposal on possible amendments to the PR in 2007/2008 (see part III and Figure 1, p. 17, of the Action Plan).

584 The 2007 Recovery Notice — Towards an effective implementation of Commission decisions ordering Member States to recover unlawful and incompatible State aid (OJ C 272 of 15.11.2007) is the subject of a separate contribution to this publication (see the article of S. Paschalidou) and will therefore not be further commented here.

585 Notice from the Commission on a simplified procedure for treatment of certain types of State Aid (OJ C 136 of 16.6.2009), hereinafter also referred to as "the Notice."

586 Not all straightforward measures could be block-exempted via the GBER: On the one hand, the Commission is limited by the scope of the Enabling Regulation (see footnote 37), and can thus currently not block-exempt cultural, cinematographic or heritage-related measures. On the other hand, the Commission lacked experience in the assessment of some of the measures newly introduced under the Action Plan (e.g. as regards aid for process and organisational innovation in services or aid for innovation clusters under the R&D&I Framework, see above text to footnote 20), and could thus not block-exempt them either.

587 See point 2 of the Notice.

applicable precedent decisions,[588] and sets out safeguards and exclusions to ensure that the Notice is only applied to truly straightforward cases.[589] Two procedural novelties pursue the same goal: candidate measures are first subject to (largely compulsory) pre-notification to enable the Commission to assess the notification's completeness and the validity of the cited precedents,[590] then published on the Commission's website after formal notification.[591] Thereby, the Notice is also the Commission's first successful attempt at introducing more transparency and publicity into State aids procedure.[592]

3.3.2 THE BEST PRACTICES CODE

The Best Practices Code,[593] in turn, governs all normal State aid procedures concerning notified or unlawful aid.[594] Its main purpose is to make procedures as efficient as possible by providing guidance on the day-to-day conduct of State aid investigations, in a spirit of cooperation and mutual understanding between the Commission services, Member States, and other interested parties.[595]

In furtherance of this objective, the Code contains concrete guidance on all steps of the State aid procedure, to increase the discipline of all actors involved and enhance the procedure's transparency and predictability to the extent possible under the current Procedural Regulation. With this in mind, pre-notification contacts also involving the aid beneficiary are strongly recommended, particularly

588 See part 2 of the Notice.

589 Since the Simplified Procedure is based on notifications, all unlawful aids are excluded. Also excluded are aid measures in the fisheries and agricultural sectors, due to their specificity. Other safeguards concern incomplete notifications or notifications containing misleading or incorrect information, measures raising novel legal or technical issues, concerns as regards compatibility with other provisions of the Treaty, or measures benefiting undertakings still subject to an outstanding recovery order (so-called Deggendorf-issue, in application of the ECJ's judgment of 15 May 1997 in Case C-355/95 P, Deggendorf, ECR 1997, p. I-2549); see points 6-12 of the Notice ("Safeguards and exclusions").

590 See part 3 ('Procedural provisions'), points 13-16 of the Notice.

591 See points 20-21 of the Notice. Publication of the summary of a notification is based on a standard form annexed to the Notice, and interested parties are given ten working days to submit observations.

592 The publicity requirement did not meet outright sympathy during Member States' consultation. Nevertheless, it could be maintained in the final version of the Notice, since use of the Notice is voluntary (Member States may, but are not obliged to opt for the Simplified Procedure). Once again, this reflects the partnership-("deal") approach pursued by the Commission throughout: The Commission will do all it can to expedite its assessment of straightforward cases – but the "price to pay" for Member States is increased transparency and public scrutiny.

593 Code of Best Practice for the conduct of State aid control procedures (OJ C 136 of 16.6.2009), hereinafter also referred to as "the Code".

594 The Code has not been designed to apply to the emergency measures adopted by Member States during the 2008 economic crisis (to which even faster deadlines apply). Also, the specificities of the fisheries and agricultural sectors may require adaptations to, or deviations from its provisions (see point 5, footnote 5, and point 6 of the Code).

595 See point 2 of the Code.

in technically complex, or otherwise sensitive cases;[596] Mutually Agreed Planning is introduced as a form of structured cooperation between the Commission and Member States, especially in those cases where complexity has not allowed the Commission services to provide the Member State with an informal preliminary assessment of the case during pre-notification;[597] and all means at the Commission's disposal are used to speed up procedures during the preliminary and formal investigation phases.[598]

The Code also introduces a staged complaints procedure: within two months of receipt of a formal complaint,[599] the Commission services are supposed to endeavour to determine the complaint's priority status and inform the complainant thereof; unsubstantiated complaints are to be swiftly expedited, while *prima facie* substantiated priority complaints are to be sent to the Member State concerned, together with a detailed request for information. This should allow the Commission to issue a decision as regards priority complaints and send a preliminary assessment letter to the complainant as regards non-priority complaints within twelve months of their receipt.[600]

3.3.3 PRIVATE ENFORCEMENT BEFORE NATIONAL COURTS – THE ENFORCEMENT NOTICE

EU law has granted national courts a particularly prominent role in the fight against unlawful aid: only they can (and must) order the recovery of unlawful aid on the mere basis of its illegality, without being empowered to assess its compatibility (this task being reserved to the Commission).[601] National courts

596 See part 3 of the Code ("Pre-notification contacts").

597 See part 4 of the Code ("Mutually Agreed Planning"). In its context, the Commission services and the notifying Member State should in particular reach a common understanding on the scope and likely duration of the investigation, information still to be provided and the priority treatment of the case.

598 See part 5 of the Code ("Preliminary examination of notified measures"). In this context, "in principle only one comprehensive" information request will be issued. Should the requested information not be provided, the notification may be deemed withdrawn (Article 5 (3) of the PR) or the formal investigation opened in case of serious doubts, and generally after two rounds of questions at most (point 26 of the Code). Similarly, the Commission will strictly enforce all applicable procedural deadlines during the formal investigation (both as regards Member States and interested third parties), and endeavour to take its final decision at the latest four months after the last submission or expiry of the last deadline, in order to actually meet the PR's 18-month indicative deadline (see part 6 of the Code ("Formal investigation procedure")). Mutually agreed and timed suspensions of the investigation remain possible in both phases.

599 Based on a completed complaints form (available on DG Competition's website at http://ec.europa.eu/competition/forms/sa_complaint_en.html) and including a non-confidential version of the complaint in case of need (see point 46 of the Code).

600 See part 7 of the Code ("Complaints").

601 See the judgments of the ECJ in Case C-39/94, SFEI, ECR 1996, p. I-3547; Case C-368/04, Transalpine Ölleitung, ECR

also have important powers as regards interim relief or awarding damages to competitors in such cases. It was thus only natural that in rounding off the State aids reform the Commission recognize national courts (and private claimants) as natural allies.

The object of the 2009 Enforcement Notice[602] is thus to foster private enforcement of State aids law "close to home", by informing national courts and private claimants of the means of redress at their disposal, setting out the applicable jurisprudence of the Community courts and offering practical means of cooperation to national judges called upon to implement EU State aids law in pending cases.[603]

To this effect, the Commission will generally respond to national courts' requests for information on pending cases, in principle within one month from their submission, and provide opinions on issues arising in national State aid proceedings, in principle within four months from the request.[604] To ease national court's access to the Commission, a single contact point has been created[605] and a specific website set up by DG Competition to provide practical information to national courts and claimants.[606] Nevertheless, and in order to preserve the independence of the judiciary, cooperation with the Commission is purely voluntary: national courts are thus not legally bound by the Commission's opinions.[607]

4. STATE AID REFORM UNDER THE ACTION PLAN – A TENTATIVE EVALUATION

In sheer quantitative terms, the "output" of the reform under the Action Plan may well be called impressive: almost all existing State aid texts were reviewed and modernized (or their validity prolonged),[608] and almost all initiatives completed to

2006, p. I-9957 and Case C-199/06, CELF, ECR 2008, p. I-469.

602 Commission notice on the enforcement of State aid law by national courts (OJ C 85 of 9.4.2009), hereinafter also referred to as "the Notice".

603 Compared to its modest (and largely unused) predecessor, the 1995 Cooperation Notice (OJ C 312 of 23.11.1995), the Enforcement Notice has thus considerably expanded its "didactic" scope, building on the very positive experience acquired in the Commission's cooperation with and support to national courts in antitrust and merger cases (see the antitrust notice OJ C 101 of 27.4.2004).

604 See part 3 of the Notice ("Commission support for national courts").

605 Including a mailing address, telephone and fax contact, and dedicated e-mail (see point 97 of the Notice).

606 See http://ec.europa.eu/competition/court/overview_en.html.

607 See point 93 of the Notice.

608 This concerns in particular the Shipbuilding Framework (OJ C 317 of 30.12.2003), the Rescue and Restructuring Guidelines (OJ C 244 of 1.10.2004) and the Cinema Communication (OJ C 43 of 16.2.2002, as prolonged by OJ C 123 of 30.4.2004); the unaltered prolongation of these texts was largely the result of comments received in stakeholder consultation.

the extent that they found stakeholder support, within less than five years from its adoption.[609]

Nevertheless, in the author's view, a mere quantitative appraisal cannot do justice to the depth of the reform achieved: as this article has tried to show, the State aids reform under the Action Plan has systematically and consistently sought to respect and implement its underlying principles. The refined economic approach was firmly established as a prime tool for modern State aid analysis and simplification (both substantive and procedural) pursued to the extent possible under the current legislative setting, and State aid policy thereby re-created as a modern discipline staying true to the founding principles of the Treaty while being capable of adjusting itself to changing times and new challenges.

Sadly, the onslaught of the 2008 financial and economic crisis has somewhat prevented the reform from fully bearing fruit, or at least retarded the reaping of its benefits by all actors.[610] In these circumstances, it is probably still too early to attempt a full evaluation. Nevertheless, in the author's view, this reform will prove to have been a major contribution to the modern State aid doctrine as soon as the general economic climate allows its full practical application. Future Commissions should thus be able to build on its principles and possibly complete its last outstanding elements.

609 Apart from the Procedural Regulation (see above part 2.3.), the only noteworthy exceptions are the 1998 Notice on the application of State aid rules to measures related to direct business taxation (OJ C 384 of 10.12.1998), whose review proposal failed to generate stakeholder support; and the announced consultation document on State aid in different forms of aid (the idea of which was largely supported, but which could simply not be implemented, given its complexity and the Commission's limited resources).

610 Following the collapse of Lehman Brothers in September 2008, both the Commission and Member States had to divert most of their resources to crisis fighting and emergency measures. Attention was therefore somewhat diverted from the more systematic reform pursued by the Action Plan to more immediate needs.

Claudia Dörr

PROVISIONAL LEGAL FRAMEWORK OF THE EUROPEAN COMMISSION FOR STATE AID TO FACILITATE ACCESS TO FINANCE FOR FINANCIAL INSTITUTIONS DURING THE CURRENT FINANCIAL AND ECONOMIC CRISIS

1. INTRODUCTION

Financial service sector: New State aid rules to tackle the current crisis

The failure of two hedge funds managed by investment bank Bear Stearns in the summer of 2007 showed the world that the banking sector was feeling the brunt of the crisis that had been unleashed a year beforehand with the bursting of the US real estate bubble. Of all things, the collapse of the market for subprime mortgages was to rapidly have a knock-on effect across the globe and threaten the existence of numerous financial institutions. Hardly a week went by without new reports of multi-billion dollar write-offs and huge losses in the banking sector. The crisis not only wiped out values, it also increasingly eroded the confidence banks had in one another. By the time of the insolvency of Lehman Brothers in September 2008 at the latest, trust among banks had been visibly shattered.

The volume of transactions on the interbank market became increasingly smaller and the entire global financial system noticeably lost momentum. Sound financial institutions now became victims of the crisis. The time had come for the States to act. As the conventional instrument of the EU State aid legislation did not provide sufficient scope to deal with the extraordinary circumstances posed by the financial crisis, and the no less extraordinary measures to combat the crisis, the European Commission made intensive efforts to rapidly formulate new guidelines to strike a balance between the protective interests of the Member States and the interests of competition. This document deals with these changes to State aid legislation, and how Germany has put these changes to use.

2. ADAPTATION OF THE EU STATE AID LEGISLATION BY THE EUROPEAN COMMISSION

When the Member States adopted conclusions committing to take comprehensive measures to stabilize the banking system in the ECOFIN Council on 7 October 2008, the Commission offered to issue guidance as to the framework within which the compatibility of these measures with State aid legislation could be rapidly assessed. This was necessary, as the measures to save the banks were considered absolutely essential but threatened to fail on account of the strict EU legislation governing State aid.

Up until then, aid to firms in difficulty was assessed by the Commission on the basis of Article 87(3)(c) of the EC Treaty in conjunction with the Rescue and Restructuring Guidelines[611]. These guidelines are not adequate for the banking crisis, however. For example, the ban on structural measures in the rescue phase strictly limited the latitude of the State when it comes to reversible instruments, such as loans and credit guarantees. In addition, the obligation to create a restructuring plan would also not be suitable to the banking crisis given that the stabilisation measures were also geared towards fundamentally sound banks, whose present difficulties stemmed from market conditions and were not the result of endogenous problems. The "one time, last time" condition is ultimately too strict in a crisis of such severity, since the crisis has shown that it is not possible to make reliable projections on the economic state of individual banks, and thus on their need for assistance on the medium term.

From the criteria cited, it is obvious that the guidelines were not designed to address structural economic emergencies of the kind witnessed in the current financial crisis. One particular element that sets this crisis apart from crises in other industries is the threat posed to "systemic" businesses that are "too big to fail", and whose continued existence is critical to the existence of the entire financial system. Such a combination was alien to the previous policy instruments.

Providing aid to systemically important firms can always be regarded as an instrument towards distorting competition and requires careful consideration of the interests of the State as well as the objective of fair competition. In this context, the Commission decided in favour of adapting State aid rules. Instead of altering the interpretation of Article 87(3)(c) of the EC Treaty, the Commission took

611 OJ C 244 of 1/10/2004, p. 2.

almost unprecedented recourse to Article 87(3)(b) of the Treaty. The Commission is of the opinion that given the monumental scale the crisis has assumed on the financial markets, and its possible impact on the economy as a whole, a serious disturbance in the economies of the Member States is taking place. According to the Commission, Article 87(3)(b) of the Treaty is the appropriate legal basis for permitting aid, which is given in the form of a general regulation.

Consequently, the Commission presented four Communications that hammered out the details of the regulation: the Banking Communication of 13 October 2008[612]; the Recapitalisation Communication of 5 December 2008[613]; the Impaired Assets Communication of 25 February 2009[614]; and the Bank Restructuring Communication of 23 July 2009[615]. The first three provide details on how to structure and grant State aid to banks. In contrast to the Rescue and Restructuring Communication, the Communications make a distinction between fundamentally sound banks and distressed banks. While distressed banks, whose flawed business models or business practices were brought to light by the financial crisis, do benefit from the additional rescue assistance permitted under Article 87(3)(b) of the Treaty, their very nature means they will have to implement restructuring measures. On the other hand, fundamentally sound banks that are in difficulty solely on account of the liquidity crisis brought about by general market conditions only have to present a restructuring plan if one of the many exemptions applies to them. As a large number of restructuring processes could be expected, the Commission decided to set forth restructuring regulations specific to banks in the fourth Communication. The main details outlined in the four Communications are presented below.

In its *Banking Communication,* the Commission regards a State *guarantee* as the primary means of stabilising the banking sector and considers such a guarantee permissible under the following circumstances: The guarantee may cover a wide range of liabilities but should be geared towards addressing the specific cause of the problem and be limited to the extent required to rectify the particular aspects of the current financial crisis as it could otherwise delay the requisite adjustment process and present a *moral hazard*. The banks must pay a commensurate rate of remuneration for the State guarantee.

612 OJ C 270 of 25/10/2008, p. 8.
613 OJ C 10 of 15/1/2009, p. 2.
614 OJ C 72 of 26/3/2009, p. 1.
615 OJ C 195 of 19/8/2009, p. 9.

At the same time, behavioural constraints can be imposed on the banks to ensure that the advantage they enjoy due to the State guarantees cannot be used for expansion measures to the detriment of non-beneficiary competitors, such as advertising strategies on the back of a State guarantee.

In addition to guarantees, the Commission also considers the direct use of public funds as part of *recapitalisation* measures to be a permissible form of assistance. The guidelines under State aid legislation are specifically defined in the Recapitalisation Communication. Recapitalisation refers to accepting own resources of a company in return for capital injections. To limit competition distortions, the Recapitalisation Communication demands market-oriented remuneration rates and remuneration conditions that incentivise exit. According to the Commission, the distinction between fundamentally sound banks and distressed, low-performing banks is central to the reconciliation of interests involved. The latter benefit to a particularly large extent from the relaxation of State aid rules and thus have to accept higher remuneration rates than sound banks. In addition, such banks have to present a restructuring plan. A bank is assigned to one of these two groups on the basis of capital adequacy, the extent of recapitalisation, CDS spread and rating.

The third Communication, known as the *Impaired Assets Communication,* deals with asset relief measures for *impaired assets* and creates the framework for the creation of *bad banks*. If the value of the assets of a bank drops, the bank either has to find new equity capital or sell the assets – both unfeasible in markets that have lost considerable momentum. The approvability of State aid regulations calls for the complete ex-ante disclosure of the loss in value suffered by the banks. Furthermore, the costs associated with the aid must be shared by the State, shareholders and creditors. The measures should be aimed, in particular, at toxic assets, which are to be valuated and remunerated at market prices. The assistance regularly associated with asset relief measures comprises the State putting a specific framework in place that allows the transfer of impaired assets for which only prices well below the book value could be obtained in the current market situation, if at all.

The *Bank Restructuring Communication* focuses on defining specifically the examination criteria of the Commission and the requirements for notifying the Commission with regard to restructuring measures. In this respect, the criteria of the Commission include the restoration of long-term viability without (additional) State aid if possible; owners sharing the burden of the restructuring costs; and efforts to largely restrict distortions in competition. Banks are required to stress-test their business to provide evidence of viability forecasts. Projected viability results must also be positive in the long term, even in *worst-case* scenarios.

3. APPLICATION OF THE RELAXED LEGISLATION IN GERMANY

3.1 LAWS AND STRUCTURES

In an unprecedented effort, within less than a week, German lawmakers created a law to rescue banks that implemented the guidelines of the Commission and had a volume of 480 billion euros.

The Financial Market Stabilisation Act (FMStG)[616]came into force on 18 October 2008. The omnibus bill comprises the Financial Market Stabilisation Fund Act (FMStFG)[617] and the Act to Accelerate Financial Market Stabilisation (FMStBG)[618]. The legislative body defined further details in the Financial Market Stabilisation Fund Ordinance (FMStFV)[619], which was announced on 20 October 2008. The Supplementary Financial Market Stabilisation Act[620] came into effect on 9 April 2009 and aimed to facilitate the takeover of businesses in the financial sector. In addition, this Act also introduced an expropriation rule, which has since expired, however. The Act on the Further Development of Financial Market Stabilisation (*Gesetz zur Fortentwicklung der Finanzmarktstabilisierung*), which came into force on 23 July 2009 and provides the framework for the formation of bad banks, is the latest measure put in place to overcome the financial crisis.

The FMStFG created a Special Fund for the Stabilisation of Financial Markets, known as "SoFFin". The newly established Financial Market Stabilisation Institute, a federal institute with legal capacity under public law, has been entrusted with implementing the stabilisation measures with the SoFFin funds. The SoFFin can back guarantees up to 400 billion euros; up to 80 billion euros are possible for equity capital-based measures. Credit authorisation of the Federal Ministry of Finance (BMF) totals 100 billion euros. To date (8 October 2009) the volume of contracts signed for stabilisation aid amounts to 155.6 billion euros, with 127.7 billion euros assigned to the provision of guarantees, 21.9 billion

616 Finanzmarktstabilisierungsgesetz, FMStG.
617 Finanzmarktstabilisierungsfondsgesetz, FMStFG.
618 Finanzmarktstabilisierungsbeschleunigungsgesetz, FMStBG.
619 Finanzmarktstabilisierungsfondsverordnung, FMStFV.
620 Finanzmarktstabilisierungsergänzungsgesetz, FMStErgG.

to equity capital and 5.9 billion to risk transfers under the bad bank model. A total of 24 businesses have already applied for assistance.

3.2 INSTRUMENTS OF THE FINANCIAL MARKET STABILISATION ACTS AND THEIR APPRAISAL UNDER STATE AID LEGISLATION

The following section will explain the structure and design of the instruments for financial market stabilisation in Germany and will assess them in terms of their significance for State aid legislation. Categorisation as aid generally does not pose a problem, nor does the application of Article 87(3)(b) of the EC Treaty as the legal basis. What is relevant is the approvability of the instruments, and thus, whether they are in sync with the guidelines of the Commission. The information presented primarily deals with the programs and their appraisal from the perspective of State aid legislation. Individual SoFFin measures had to be notified in numerous instances, however, as several successive rounds of intervention were necessary at a bank. Up to now, the Commission has provided a positive appraisal of such individual measures throughout.

3.2.1 FMSTFG: GUARANTEE, RECAPITALISATION, RISK TRANSFER

These stabilisation measures are only carried out on request. Businesses do not have the legal right to obtain aid from the fund. A relevant board decides at its discretion, taking into account the significance of the financial enterprise to the stability of the finance market, the urgency and the principle of the effective use of funds. All sound or distressed financial-sector enterprises based in Germany are entitled to apply.

Section 6 of the FMStFG provides for *guarantees* to remedy liquidity shortages. Guarantees can only be requested for new liabilities assumed before 31 December 2010. The term of the liabilities may not exceed five years and may exceed three years only in exceptional cases. Adequate capital resources are a prerequisite to receiving the guarantee. The Commission stipulates a minimum core capital quota of 7 percent but a pledge to meet this quota within three months suffices. Market-oriented remuneration not below 0.5 percent must be provided for the guarantee. Furthermore, a risk premium must be levied for liabilities with terms longer than one year. The SoFFin can impose conditions on the bank, such as the revision of corporate policy and corporate policy sustainability, the abandonment of high-risk operations and the ban on advertising strategies on the back of the State guarantee. If the enterprise avails of the guarantee, or if the bank does not obtain the core capital quota of 7 percent, the bank must present a restructuring plan within six months. The Commission found guarantees to be compatible with State aid rules in several decisions[621]. The Commission drew particular attention to a number of aspects: the time limit on the guarantees; the restriction to new liabilities; and the open nature of the guarantees for liabilities that extend beyond investments from private customers, which gear the measure towards short-term and medium-term interbank funding. According to the Commission, this structure guarantees the measure is limited to the minimum necessary and is problem-oriented. According to the Commission, the strict behavioural constraints ensure that the beneficiary financial institution will not extend its activities to the detriment of its competitors.

Section 7 of the FMStFG provides for *recapitalisation* as the means to boost equity capital. Direct injections of capital aim, in particular, to guarantee lending to the real economy and to reduce the risk of insolvency among banks. The State's participation involves the acquisition of newly issued shares, silent participation or acquisiton other components of the enterprise's own funds against the provision of a contribution. The State's participation is limited to ten billion euros per financial institution. The capital contribution must be compensated in line with market conditions: depending on the risk profile and the structure of the capital instrument, fundamentally sound banks pay between 7.0 percent and 9.3 percent, while distressed, low-performing banks pay at least 10 percent. A lower rate is only permitted if private parties participate to a large extent in the recapitalisation scheme on the same conditions. The FMStFV stipulates priority be given to compensation of State participation. In general, a dividend freeze is enforced for the duration of the recapitalisation measures. A time-limited restrictive dividend policy with a relaxation option only applies to sound financial institutions in order to provide payback incentive. Far more extensive conditions are tied to recapitalisation measures than to guarantees. In addition to the guarantee conditions, banks are also under obligation to provide loans to small and medium-sized enterprises and to limit monetary compensation of its board members and managers to an acceptable level. Annual monetary compensation for such persons is limited to 500 thousand euros and bonuses or similar salary items may not be paid. The Commission also examined the German

621 N 512/2008, N 625/2008, N 330/2009.

recapitalisation model and deemed it admissible. It considered positive the upper limit on participation in own fund items of individual enterprises. Given that the Commission considers recapitalisation to be a final measure, it sets strict conditions in terms of proportionality. According to the Commission, however, graduated remuneration structures, in particular, meet these conditions and regulations governing compensation priority and give sufficient incentive to redeem the capital.

A different situation is presented with regard to the *assumption of risks*, regulated in Section 8 FMStFG, to relieve the write-down pressure on financial-sector enterprises. Here, the Commission took a critical view of the original regulation. The intention behind the assumption of risks proposed by German legislators was for the State to permanently acquire – against the transfer of debt certificates – toxic assets. Asset in this sense means in particular receivables, securities, derivative financial instruments, rights and obligations from loan commitments or warranties and participations, in each case together with corresponding collateral. This kind of assets must be acquired by financial-sector enterprises before 13 October 2008 in order to provide the beneficiary banks with liquidity and permanently remove the risk of these assets from their balance sheets.

In decision N 625/2008, the Commission made it clear that it would only allow risks to be assumed if the conditions provide for the repurchase of the risk positions after 36 months at the latest and demanded that any loss in value incurred in that period be counterbalanced by the financial institution selling the risks. This way, the assumption of risk was still a suitable method of providing banks with liquidity but the measure could no longer achieve the desired effect of balance sheet relief. As the transfer was not permanent and loss in value had to be compensated, the risk of loss in value or failure was still borne by the selling bank that still had to enter these items in the balance sheet in accordance with International Financial Reporting Standards (IFRS). A transaction, as envisaged by the Commission, does not, in effect, result in any relief for the financial-sector enterprise. Given the less attractive nature of this measure, it has yet to be used by any financial institution.

Guarantees and recapitalisation schemes proved successful in Germany – they prevented bank insolvency and gradually revived interbank trading. Balance sheet risks persisted, however, and the creation of a bad bank remained on the agenda given the failure of the risk assumption measure. Lawmakers were required to create a new model that complied with the State aid guidelines of the EU Commission.

3.2.2 THE LATEST DEVELOPMENT: THE BAD BANK ACT

With the Act on the Further Development of Financial Market Stabilisation of 17 July 2009, German lawmakers attempted to provide a bad bank solution that met the guidelines of the Impaired Assets Communication. The regulation offers two different bad bank options, namely the special purpose vehicle model (SPV model) and the agency model (also known as the Austalt in der Austalt model) with federal-law or state-law resolution agencies. Both versions aim to *relieve* the bank balance sheets by transferring various risk positions. By providing the opportunity to spin off non-strategic business segments, the agency models also enable banks to *reduce* their balance sheets.

In the agency model, units within the financial market stabilisation agency (FMSA), which have partial legal capacity and are independent from the economic and organisational perspective, assume the role of the bad bank. All risk positions purchased until 31 December 2008, as well as business segments that are not necessary for strategic purposes, can be transferred to these bad banks. The transfer is effectuated either through a legal transaction or through a spin-off or hive-down. The owners of the transferring bank have ownership shares in the agency, but the FMSA has the basic and ultimate responsibility for the bank. The agencies are not regarded as credit or financial institutions, and as such they do not have to comply with minimum regulatory capital requirements. As a result, the capital can remain in the transferring company and be available for the sound business transactions of the bank.

Furthermore, they prepare their accounts in accordance with the rules of the German Commercial Code (*Handelsgesetzbuch*) and not in line with IFRS standards. Consequently, the risk positions do not have to be entered in the books on the basis of current market values and the agencies avoid valuation risks. At the same time, the principle of complete owner responsibility applies to the agency model and the owners must assume an obligation to compensate for losses and make further contributions proportionate to their level of participation. The Commission did not provide across-the-board approval for this version; such cases must be notified individually to the Commission.

The special purpose vehicle model differs greatly from the agency model. This option focuses solely on the transfer of structured securities and related hedging transactions which the bank acquired on or before 31 December 2008. Applications for this measure must be made by 22 January 2010. Under this measure, the bank establishes a special-purpose vehicle to which it transfers the structured securities via a legal transaction. In return, the bank receives debt securities (bonds) at the transfer value which are guaranteed by the SoFFin.

As a result, this removes valuation risks stemming from value loss or fluctuations in the structured securities from the balance sheet of the transferring bank. The transfer value is either based on the actual economic value, or on 90 percent of the book value as of 30 June 2008 or 31 March 2009, depending on whichever value is the highest. The bank has to make a market-oriented *compensation payment* to the SoFFin for the debt certificate, which is calculated from the difference between the transfer value spread over the term of the guarantee and the fundamental value. The fundamental value is the actual economic value of the securities to be disclosed by the banks, minus a deduction for risks of future unexpected losses. If the annual losses exceed the compensation payment calculated this way, the law makes provisions for *run-over liability*. The owners of the bank are not directly liable for the loss but the loss is to be compensated solely from the dividends of the remaining business. Beyond this, the risk is borne by the State. For this reason, the model presents a form of aid that was approved by the Commission in its decision of 31 July 2009[622]. The Commission considers that limitation to the minimum necessary has been effectuated through the caps of the measure, both in terms of time and scope, and regards the burden-sharing and payment conditions as acceptable. In the Commission's opinion, a restructuring plan is required if the 10 percent deduction cannot be borne without falling below the core capital quota of 7 percent, or if the aid received exceeds 2 percent of the risk-weighted assets, or if rescue measures had already been adopted.

4. CONCLUSION

The European Commission and the German Federal Government have proven they have the will and ability to work in close collaboration to swiftly meet the challenges posed by the financial crisis. The Commission demonstrated flexibility in times of crisis and made urgently needed adaptations to the EU State aid

622 N 314/2009.

legislation. Germany made use of this additional latitude. The speed at which the Commission has approved the German measures to date indicates that the Federal Government and the Commission work well in partnership, even in times of crisis. As the aid program for the real economy appears to be following a similarly positive course, it can be hoped that the impact of the financial crisis on the global economy will soon ease.

Furthermore, to prevent future disruptions on the EU banking market and associated negative consequences for bank customers, the EU Commission presented a Communication for discussion on 20 October 2009 concerning the path to be taken in the future to deal with transborder banking crises and bank insolvencies in the EU. The Communication draws on the lessons learned from the current crisis and integrates them into a kind of contingency plan for banks. It is hoped that correct and effective solutions will be found.

Leigh Hancher

THE TEMPORARY FRAMEWORK AND THE REAL ECONOMY

1. INTRODUCTION

This contribution examines the role of the European Commission in managing the application of the state aid rules to "the real economy" in the wake of the financial crisis as Member States announced national recovery plans to get their economies through the credit squeeze. Indeed, according to the Commission, most European economies are now "officially" in recession (two consecutive quarters of negative growth). Europe is facing a period where consumer confidence, consumption and investment are shrinking sharply, households are under pressure and businesses' order books are down. The forecasts for the EU economy for 2009 were negative with rising unemployment across Europe. Although the Polish economy has fared better than some of its European counterparts, it too has not been immune from the impact of the global slowdown.

In early November 2008, the European Union's Heads of State and Government agreed on the need for a coordinated response to the crisis. The Commission responded with the European Economic Recovery Plan[623], a plan intended to contain the scale of the downturn, to stimulate demand and confidence, and to boost long-term competitiveness. It proposed a countercyclical macro-economic response to the crisis in the form of an ambitious set of actions to support the real economy. Some of the proposed measures included a recognition that State aid measures would be required. But not all would be automatically viewed as acceptable.

According to the Commission, "the challenge for the Community is to avoid public interventions which would undermine the objective of a level playing field for European companies, and avoid protectionism disrupting the Internal Market. Some Member States may be tempted to adopt protectionist measures to safeguard their domestic industries at the potential expense of others. This entails the risk of escalation, Member States outbidding each other to attract economic activities, ultimately leading to a subsidy race. Past experience shows that individual action of this kind is not effective and could seriously damage the Internal Market."[624]

623 Commission (EC), "A European Economic Recovery Plan" (Communication) COM(2008) 800 final, 26 November 2008.

624 Commission (EC), "State Aid Scoreboard, Spring 2009 Update, Special edition on state aid intervention in the current financial and economic crisis" (Report) COM(2009) 164, 8 April 2009, p. 22.

Has the Commission succeeded in meeting this objective? Has it succeeded in promoting what it terms a "flexible response" to the crisis without sacrificing the principles on which the EU state aid regime is based? And even if it has been successful in this aim, is there any assurance that in the hope that normality is soon restored, it can revert once again to "business as usual" when it comes to the implementation of the European state aid regime?

This short contribution will assess the results so far and assess their implications for the future of state aid policy and law.

2. THE EC STATE AID REGIME

The scope for Member States to grant aid to undertakings is defined in terms of Articles 87 and 88 of the EC Treaty, together with a host of implementing guidelines, and more recently regulations. These provide that in principle aid granted by a Member State, or through state resources, which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods, is incompatible with the Internal Market insofar as it affects trade between Member States. Article 87 and 88 became fully applicable in Poland upon its accession to the European Union in 2004, albeit that complex transitional procedures were applied to aid measures granted before accession which continued to apply thereafter. The application of the rules can be strict, as Poland was to experience in respect of the restructuring of its shipyards in Gdynia, Gdansk and Szczecin.

3. THE SAAP

Although state aid is not prohibited outright, the exemptions set out in Article 87(2) and (3) EC allow some forms of aid, but essentially restrict Member States from protecting "national champions", or maintaining an economic lifeline for firms in structural difficulties and without prospect of a return to viability in the longer term. As a result of the substantial modernisation of the state aid rules over the last years, spearheaded by the adoption of the State Aid Action Plan,[625] in 2005 (hereinafter referred to as the "SAAP"), the Commission generally considers that Member States currently dispose of an appropriate framework to better target public support towards sustainable goals such as stimulating research,

625 Commission (EC), "State Aid Action Plan: Less and better targeted State aid: a roadmap for state aid reform 2005–2009" (Consultation document), COM(2005) 107 final, 7 June 2005.

development and innovation, making risk capital available to SMEs and start-ups, training, regional development, and environmental protection. In addition, following the adoption of the General Block Exemption Regulation[626], Member States are in a position to grant no less than 26 different types of state aid without having to notify individual measures to the Commission and with minimum administrative burden.

And so it could perhaps have been assumed that, confronted with the unfolding economic crisis in 2008, the Commission was well equipped to deal with national measures taken to assist firms in difficulty. Guidelines for assessing the compatibility of various types of aid had been modernised and streamlined, and the procedures for notifying and assessing aids had become more transparent. The early financial sector rescue cases emanating from the UK and Germany were indeed assessed under the "conventional" regime – that is the Commission's Rescue and Restructuring Guidelines[627] of 2004 based on Article 87(3)(c) EC.

4. THE FINANCIAL CRISIS

Although initially sticking to its guns, and insisting that even complex financial sector rescues could be dealt with under the regular state aid framework, the Commission eventually was forced to concede there was a real prospect that large scale banking failures could trigger a "serious disturbance" in the economy of a Member State, that might warrant a change of approach. A new regime was needed to ensure that national rescue measures would not fall foul of the EC state aid rules while at the same time maintaining the basic principles of state aid discipline in place. Hence the Commission invoked another Treaty provision – Article 87(3)(b) which allows Member States to take – and the Commission to approve – measures that "remedy a serious disturbance in the economy of Member State". This provision had been relied upon only on rare occasions in the past and indeed the Commission had refused to apply it to certain rescue measures for ailing banks notified to it in 2007. In late 2008 and early 2009, the Commission published four sets of Guidelines to provide targeted advice to Member States on how to grant compatible aid. The Banking Communication[628] of October 2008

626 Commission Regulation (EC) No 800/2008 of 6 August 2008 declaring certain categories of aid compatible with the common market in application of Article 87 and 88 of the Treaty (General block exemption Regulation) [2008] OJ L214/3.

627 Commission Communication (EC) Community guidelines on State aid for rescuing and restructuring firms in difficulty [2004] OJ C244/2.

628 Commission Communication (EC) The application of State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis [2008] OJ C270/8.

was followed up by a Recapitalisation Communication[629] of February 2009 and an Impaired Assets Communication[630], also in February 2009.

The Commission's decision to invoke Article 87(3)(b) EC was initially expected to apply only to the financial sector and not to any other sector of the economy. The Banking Communication noted that "the use of Article 87(3)(b) cannot be envisaged as a matter of principle in crisis situations in other individual sectors in the absence of a comparable risk that they have an immediate impact on the economy of a Member State as a whole".[631] Even if a serious disturbance was likely to emerge, the Commission reasoned that recourse to this Article is not to be open-ended, but could only be justified as long as the crisis situation justified its application. However, in December 2008 the Commission acknowledged that the crisis could indeed impact on the real economy, and as such warranted an exceptional policy response.

5. THE TEMPORARY FRAMEWORK

In view of the dimension of the crisis and the difficulties to find credit faced by all types of companies (SMEs and large companies), the Commission adopted the *Temporary Community framework for State aid measures to support access to finance in the current financial and economic crisis*[632] (the "Temporary Framework") granting Member States additional ways to deliver finance to enterprises affected by the credit squeeze.

As the Temporary Framework states in its opening recitals, these additional possibilities are justified to remedy a serious disturbance in the economy and may be declared compatible with the Internal Market on the basis of Article 87(3)(b) of the EC Treaty. The aims of the Temporary Framework are intended to unlock back lending and facilitate access to finance, and to encourage companies to invest in sustainable growth.

The Commission nevertheless remains in favour of a horizontal approach which

629 Commission Communication (EC) Recapitalisation of financial institutions in the current financial crisis: limitation of the aid to the minimum necessary and safeguards against undue distortions of competition [2009] OJ C10/2.

630 Commission Communication (EC) on the treatment of impaired assets in the Community banking sector [2009] OJ C72/1.

631 The Banking Communication (n 6) para. 11.

632 Commission Communication (EC) Temporary Community framework for State aid measures to support access to finance in the current financial and economic crisis [2009] OJ C16/1.

benefits the whole economy. Consequently, the Commission holds that the proposed aid instruments are the most appropriate ones to achieve the general objectives and that there is no need to single out a sector. Accordingly, apart from the exclusion of fisheries and primary agricultural production from the limited amount of aid, the Framework makes no such distinction.

To avoid distortions in the market, the Temporary Framework only applies to companies whose difficulties did not pre-date the crisis and firms with structural difficulties due to their own inefficiencies are expected to restructure in accordance with the standard rules – i.e. 2004 Rescue and Restructuring Guidelines. In addition, all measures approved under the Temporary Framework must be necessary, appropriate, and proportionate to remedy a serious disturbance of the economy, as well as respecting in full the various supplementary conditions set out in the Framework itself – see Box 1. Several of the permitted aid measures had in fact been anticipated by the European Economic Recovery Plan, including aid to support EU objectives, such as R&D, innovation, ICT, transport and energy efficiency, while others reflect the Commission's ongoing commitment to small and medium sized enterprises as the home of successful innovation. Such measures were considered not to "unduly" distort competition.

5.1 BOX 1 – THE TEMPORARY FRAMEWORK OF 17 DECEMBER 2008

The temporary measures are applicable until the end of 2010 and pursue two objectives:

- to unblock bank lending to companies and thereby guarantee continuity in their access to finance; and

- to encourage companies to continue investing in the future, in particular in a sustainable growth economy, including the development of green products.

The specific aid instruments that will assist Member States to meet those objectives include:

- a lump sum of aid up to 500,000 euros per company;

- State guarantees for loans at a reduced premium;

- aid in the form of subsidised interest rate applicable to all type of loans;

- subsidised loans for the production of green products involving the early adaptation to or going beyond future Community product standards.

In addition to the new measures, the Framework provides for:

- a temporary derogation from the risk capital guidelines in order to increase the tranche of finance per target SME (from 1.5 million to 2.5 million euros) and a reduction of the minimum level of private participation (from 50 to 30 percent); and

- a simplification of the requirements of the Export Credit Communication[633] to use the exemption that allows temporarily non-marketable risks to be covered by the state.

On 25 February 2009, after having gained some experience with the application of the Temporary Framework, the Commission has introduced some further technical adjustments.[634] In particular, with respect to the conditions of compatibility for guarantees, the Commission has adopted a new grid which adjusts the guarantee safe-harbours according to different levels of collateralisation. Moreover, in addition to the reduction of the annual guarantee premium of 2 years, the revised safe-harbour premiums contained in the grid could be applied for another 8 years without reduction.

5.1.1 INDIVIDUAL DECISIONS

The Commission has ensured rapid decisions in cases where the notifications were complete and the conditions of the Temporary Framework respected. By April 2009, the Commission has authorized 24 measures under the Temporary Framework:

- 8 schemes for aid up to 500,000 euros per company proposed by Germany, France, Latvia, Luxembourg, Hungary, Portugal, the United Kingdom and Austria;

633 Commission Communication (EC) to the Member States pursuant to Article 93 (1) of the EC Treaty applying Articles 92 and 93 of the Treaty to short-term export-credit insurance [1997] OJ C281/4, with further amendments [2001] OJ C217/2 and [2005] C325/22.

634 The Consolidated version of Temporary Framework is published in [2009] OJ C83/1.

- 4 schemes for subsidized loan interests in Germany, Hungary and France;
- 3 risk-capital schemes in Germany, France and Austria;
- 3 schemes offering reduced interest loans to businesses investing in the production of green products in France, the United Kingdom and Spain;
- 6 guarantee measures in Belgium, Germany, France, Luxembourg, Hungary and the United Kingdom.

In recent months the Commission has also approved a number of export-credit insurance schemes, including a Dutch measure to provide insurance coverage to exporters who are unable to obtain cover from the private market as a result of the current financial crisis. The Commission found the measure to be in line with its Temporary Framework. In particular, the measure requires market-oriented remuneration, and is focused specifically on the problem of the current unavailability of short-term export credit insurance cover in the private market. The Commission authorised the measure until 31 December 2010.

5.1.2 POLAND

The European Commission has authorised under the EC Treaty rules on state aid a Polish scheme aimed at providing relief to companies encountering financing difficulties as a result of the credit squeeze in the current economic crisis. To this end the scheme allows aid in the form of direct grants and debt conversions concluded by 31 December 2010. The scheme was deemed to meet the conditions of the Commission's Temporary Framework. In particular, the scheme is appropriate to remedy a serious disturbance in the entire Polish economy, is limited in time, respects the relevant thresholds and applies only to companies that were not in difficulty on 1 July 2008. It was therefore deemed compatible with Article 87(3)(b) of the EC Treaty. Competition Commissioner Neelie Kroes said "The measure was designed to help maintaining employment and preventing bankruptcy. We are satisfied that it encourages business investment and economic recovery, without unduly distorting competition."[635]

635 Commission Press Release IP/09/1483 of 8 October 2009.

The Polish authorities had demonstrated that the scheme is necessary, proportional and appropriate to remedy a serious disturbance in the entire Polish economy.

5.1.3 GREEN PRODUCTS

An interesting feature of the Temporary Framework is the special provision made for production of green products. Three schemes were approved for France, the UK and Spain, the latter scheme being aimed specifically at the car sector. The French scheme was notified on 9 January and approved on 3 February, while the UK scheme was approved on 27 February, some 17 days after notification. The Spanish scheme, notified on 3 March was approved on 30 March. The speed with which such schemes have met with approval even considering the substantial sums involved – the two UK measures for guarantees and interest rate subsidies for production of green products allowed for a combined risk exposure of 8 billion euros – has prompted concerns of mere rubber stamping. At the same time press reports at the time indicated that the French and Spanish auto rescue plans required further clarification, although the extent of the required amendments were not reported.

Finally, it should be noted that the Temporary Framework contains additional rules on cumulation. The aid ceilings set out in the Framework are applied regardless of the source of the aid – i.e. whether it is financed by national or Community resources. At the same time the temporary aid measures may be cumulated with other compatible aid, or other forms of Community financing providing that the maximum aid intensities indicated in the relevant guidelines or block exemptions are respected.

6. PROCEDURAL REFORMS

The various measures to deal with the financial crisis as well as its impact on the real economy not only depart from the "standard" substantive principles which have been developed in Commission Guidelines issued under Article 87(3)(c), but have also entailed a number of procedural reforms.

6.1 THE FINANCIAL CRISIS AND ITS IMPACT

In its response to the financial crisis, the Commission is aware of the importance of delivering quick decisions in close cooperation with Member States in order to contribute to restoring financial stability and to providing legal certainty. The Commission quickly demonstrated that it could adopt decisions on emergency rescue measures in short time periods. In contrast, when assessing restructuring plans, the Commission must ensure that the envisaged restructuring is capable of restoring the long-term viability, that state support is limited to the minimum necessary and decide whether compensatory measures should be put in place to minimise potential distortions of competition created by the aid. The analysis of State interventions of such magnitude usually require longer time than certain emergency rescue measures.

The early experiences in 2007 and the first half of 2008 showed that the Commission can deal with cases in a rapid, efficient and flexible way. A fast track assessment of support measures to financial institutions was particularly necessary in view of the considerable impact of the crisis on individual financial institutions and the interdependence between them, requiring immediate measures to avoid a melt-down of the entire financial sector. However, the deepening financial crisis required a further streamlining of the processes.

The Banking Communication sets out the steps the Commission took in order to ensure the swift adoption of decisions upon complete notification, if necessary within 24 hours and over a weekend. In particular, the following arrangements were put in place:

- Simplified consultation procedure within DG Competition and quicker consultation of other services;

- Use of an urgent written procedure or a temporary empowerment of a Member of the Commission;

- Simplified linguistic requirements.

The Member States' agreement to be notified of decisions in one of the working languages of the Commission has also helped to speed up the procedures. In addition, Member States' cooperation is necessary for the Commission to guarantee swift decision making. Experience has shown that early informal contacts and the involvement of the Commission at an early stage contribute significantly to the adoption of decisions within short timeframes.

During the last quarter of 2008, 18 decisions on banking schemes and 16 decisions on individual banking cases were adopted. Of the 22 banking schemes decided until March 2009, the Commission took in 9 cases its decision in less than a week.

6.2 THE REAL ECONOMY

Accelerated procedures apply also to measures under the Temporary Framework. Accordingly, the Commission has set up the necessary arrangements, similar to those adopted for the banking sector, so that notifications based on the Temporary Framework can be dealt with rapidly provided that Member States supply all relevant information. Any measures proposed must be notified to the Commission in the standard manner. Furthermore, in order to provide guidance on the application of the Temporary Framework in practice, the Commission has set up an Economic Crisis Team to serve as a first point of reference. For other urgent measures falling outside the scope of the Temporary Framework but linked to the financial and real economy crisis, the Commission has also applied, insofar as possible, accelerated procedure.

Although these procedures have proved capable of producing rapid decisions, it should be noted that in all cases the measures have been approved without opening a formal investigation in accordance with Article 88(2) EC and Regulation 659/98[636]. This means that discussions have been conducted between the notifying Member State and the Commission with little opportunity for comment from third parties – including competitors. This has led to criticism that the Commission has sacrificed legal certainty and procedural guarantees. The Framework does, however, include a separate section on monitoring and reporting. In particular, Member States must provide the Commission with an interim review, including lists of schemes put in place on the basis of the Framework and must ensure that detailed records concerning aid granting are maintained for a period of 10 years and are to be provided to the Commission on request. A report on measures put in place must be provided to the Commission by 31 October 2009. The report should provide the Commission with elements indicating the need to maintain the measures after 30 December 2009, as well as details on the environmental benefits of subsidised loans. [To assist Member States in compiling these reports a questionnaire on the necessity and scope has been published on DG Competition's website].

636 Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty [1999] OJ L83/1.

7. PARALLEL ASSESSMENTS FOR FIRMS ALREADY IN DIFFICULTY BEFORE THE CRISIS

If a measure is targeted at a rescue and/or restructuring operation for a firm that was not in difficulty before 1 July 2008, the standard Guidelines for Rescue and Restructuring Aid apply. The application of these rules is illustrated by a recent Polish case.

On 26 February 2009, Poland notified a rescue aid to Diora Swidnica Sp. z o.o.[637] (hereinafter referred to as "Diora"), an undertaking active in the manufacture of sound systems (boxes, speakers, concert hall products and televisions set stands). The Commission noted that more than half of the registered capital in Diora disappeared in the year preceding the notification and the planned granting of the rescue aid. The loan is to be granted to the beneficiary by a public entity, ARP, in one instalment upon being approved by the Commission. The loan is to be repaid within six months of its disbursement, i.e. after the sum is paid to the company's bank account. The interest was to be charged at the rate of 7.78 percent, which is 100 basis points higher than the reference rate established by the Commission for Poland. The company provided collateral to secure the loan.

The Commission considered that Diora was a company in difficulty under point 10(a) of the Guidelines and is eligible to receive rescue aid. Diora, the beneficiary of the rescue aid, is located in a region of Dolnoslaskie, a Polish region eligible for regional aid under Article 87(3)(a) of the EC Treaty. The company operates on the market from 1991 and employs 160 workers. In 2007 the company's turnover amounted to PLN 12.2 million (2.7 million euros) and the balance sheet totalled PLN 6.0 million (1.3 million euros). With these figures the company meets the SME thresholds. However, Diora is owned by 68 percent by the state-controlled Industrial Development Agency (Agencja Rozwoju Przemysłu S.A., hereinafter referred to as "ARP"), therefore, it had to be classified as a large enterprise. In addition, the remaining shares of the company, 32 percent, are held by a Polish private company UNITRA THP S.A. (hereinafter referred to as "UNITRA"), which holds also shares in seven other companies. For this reason Diora could not be considered as an independent undertaking, but forms part of a larger business group.

The Commission held that the loan in favour of Diora constitutes State aid pursuant to Article 87(1) of the EC Treaty. The loan in favour of Diora is provided

637 Commission Decision (EC) N 116/2009 of 20 April 2009.

by ARP, which is a public entity over which the state excises control, and, therefore, the loan is granted from state resources and is imputable to the State. The loan constitutes a selective advantage since it will provide Diora with access to credit that, being in a difficult situation, the company would not be able to obtain on the market. Furthermore, as there is trade between the Member States in sounds systems which Diora manufactures, the measure is apt to improve the competitive position of the beneficiary in relation to its competitors in Poland and the EU, and it, consequently, distorts (or threatens to distort) the competition and affects trade between the Member States.

The Commission considers a rescue aid compatible with the Internal Market, pursuant to Article 87(3)(c) of the EC Treaty if it complies with the criteria under the Guidelines which in chapter 3.1 spell out the rules as to the eligibility of the firm for the aid (only firms in difficulty are eligible), the form of aid, interest rate and other conditions. Diora is regarded as belonging to a business group. According to point 13 of the Guidelines, a company that is part of a group is only eligible for restructuring aid when it can be demonstrated that the company's difficulties are intrinsic and are not the result of an arbitrary allocation, or its difficulties are too serious to be dealt with by the group itself.

It had to be therefore determined if the minority shareholder UNITRA is able to provide financial resources necessary to rescue Diora. UNITRA holds only 32 percent of shares in Diora, thus, is not obliged to prepare a consolidated financial statement. UNITRA holds shares also in seven other companies; two of them are in liquidation and one of them suspended its economic activity. Although in 2008 UNITRA managed to make a profit of PLN 0.27 million (0.06 million euros), the company does not have the necessary financial resources in order to rescue Diora. Furthermore, since Diora does not have any trade relations with UNITRA or any other company linked to UNITRA, the Commission considered that the difficulties of Diora were intrinsic and are not a result of arbitrary allocation of the costs within the group.

According to point 9 of the Guidelines, the Commission considers a firm to be in difficulty where it is unable, whether through its own resources, or with the funds it is able to obtain from its owner/shareholder or creditors, to stem losses which, without outside intervention by the public authorities, will almost certainly condemn it to go out of business in the short or medium term. Additionally, point 11 of the Guidelines clarifies that the usual signs of a firm in difficulty are increasing losses, diminishing turnover, growing stock inventories, excess capacity, declining cash flow, mouthing debt, rising interest charges, and falling or nil assets value.

8. COMPATIBILITY OF RESCUE AID

First, the notified aid to Diora, in line with point 25(a) of the Guidelines, is a loan. The loan is limited to a period of six months from being disbursed to Diora. In addition, Poland has provided assurance that the loan is granted at an interest rate above the reference rate adopted by the Commission for Poland. The interest rate amounts to the reference rate applicable to Poland as of 1 March 2009 (6.78 percent) increased by 100 basis points.

Second, the aid is, in line with point 25(b) of the Guidelines, warranted on the grounds of serious social difficulties and has no unduly adverse spill-over effects on other Member States. In fact, if Diora ceased its operations, this would have serious consequences in terms of employment in a region which is an assisted area under Article 87(3)(a) of the EC Treaty. In addition, taking into consideration the low overall turnover of the company, the Commission finds that the aid will not create unduly adverse spill-over effects on other Member States.

Third, the rescue aid is, in line with point 25(c) of the Guidelines, limited to six months as Poland has undertaken to communicate to the Commission, not later than six months after the rescue aid is authorised, a restructuring plan, a liquation or proof that the loan has been repaid in full.

Fourth, the notified aid amount of PLN 1,200,000.00 loan (0.27 million euros), is in line with point 25(d) of the Guidelines, the amount needed to keep the firm in business for six months. According to the Guidelines, the amount necessary should be based on the liquidity needs of the company stemming from losses; in determining that amount regard needs to be taken to the outcome of the application of the formula set out in the Annex of the Guidelines. As the notified aid amount is lower than PLN 1.8 million, it complies with the formula set out in the Annex.

Finally, the Polish authorities confirmed that Diora has neither received rescue nor restructuring aid in the past. Therefore, the notified aid complies with the "one time, last time principle" as laid down in point 72 et seq. and point 25(e) of the Guidelines.

As is evident from this summary of the Diora decision, the application of the Rescue and Restructuring Guidelines requires a fairly rigorous investigation of the measure and the application of strict criteria. The second phase – the restructuring phase, which was not considered in this case, is also subject to strict conditions, many of which are difficult to apply in the current economic climate. Rescue aid is a temporary assistance to keep a firm in financial difficulties afloat for the time it is needed to work out a restructuring and/or a liquidation plan. Restructuring aid, however, must be based on a feasible, coherent and far-reaching plan to restore a firm's long term viability. It usually involves different elements, such as the reorganisation and rationalisation of the firms' activities on a more efficient basis, the restructuring of those existing activities that can be made competitive again, diversification towards new and viable activities, financial restructuring, and the adoption of measures to limit distortion of competition. In principle repeated rescue and restructuring aid should be given on the basis of the "one time last time" principle.

9. THE COMMISSION'S COMMUNICATION ON RESPONDING TO THE CRISIS IN THE EUROPEAN AUTOMOTIVE INDUSTRY AND ITS FOLLOW-UP

How have sectors which have traditionally enjoyed state support over prolonged periods of time faired in current climate? The European automobile sector is of course no stranger to state support, but it has proved to be doubly exposed the downturn – given that many companies were also engaged in selling financial services to car buyers.

On 4th February 2009 Commissioner Kroes stated that "we must not lose sight of the fact that overcapacity in the car sector existed already before the crisis, and that European car makers will need to restructure anyway if they want to compete in global markets"[638]. Three weeks later, the Communication on "Responding to the crisis in the European automotive industry",[639] issued on February 25, 2009 ("Communication") was adopted to outline the Commission's overall strategy to tackle the woes of the European car sector. In fact, at least in terms of volume of aid received, the European car industry has proved to be one of the main beneficiaries of various national measures approved under the Temporary Framework.

638 Commission Press Release MEMO/09/50 of 4 February 2009.

639 Commission (EC) "Responding to the crisis in the European automotive industry" (Communication) COM(2009) 104 final, 25 February 2009.

In general, despite the problems, the Commission takes an optimistic stance – the long-term global outlook for the sector is good and that, therefore, measures are needed to help the industry "*weather the downturn*" in order to "*be ready to take advantage when demand returns*"[640] The Communication essentially distinguishes between, on the one hand, traditional State aid measures, and, on the other hand, State aid that is directly linked to the financial crisis.[641]

- Traditional State aid measures include environmental aid, aid for Research and Development and Innovation, regional aid, aid in form or risk capital, and, finally rescue and restructuring aid. Highlighting the importance played by regional aid in the sector, it is noteworthy that, since the adoption of the Communication, the Commission has approved under the Regional Aid Guidelines the following projects: Mercedes-Benz's investment in Hungary[642]; Ford's investment in Spain[643]; and Fiat's investment in Sicily.[644]

- State aid measures linked to the financial crisis are those listed under the Temporary Framework for State aid measures to facilitate access to finance, including subsidised interest rates, and, in particular subsidised loans for the production of green products. Measures of this kind that have received Commission approval include a UK scheme providing interest rate subsidies for businesses investing in the production of cars that meet high environmental standards[645], and a similar scheme launched by Spain[646].

- The positive attitude towards subsidies for more environmentally friendly cars underlies also "scrapping schemes", where Member States grant a financial benefit for scrapping an old vehicle when a newer one is acquired that meets the relevant environmental standards.[647]

640 Communication (n 19) p. 4.

641 Communication (n 19) Annex 2, available at http://ec.europa.eu/enterprise/automotive/pagesbackground/competitiveness/index.htm.

642 Commission Press Release IP/09/1147 of 16 July 2009.

643 Commission Press Release IP/09/958 of 18 June 2009.

644 Commission Press Release IP/09/660 of 29 April 2009.

645 Commission Press Release IP/09/333 of 27 February 2009.

646 Commission Press Release IP/09/499 of 30 March 2009.

647 Communication (n 19) Annex 3, available at http://ec.europa.eu/enterprise/automotive/pagesbackground/competitiveness/index.htm.

Finally, with respect to the international dimension of the crisis affecting the sector, the Communication underlines commitment to fair competition in open markets, promising to fight trade restrictions created by third countries.

10. THE GM RESTRUCTURING: A EUROPEAN PROBLEM IN SEARCH OF A EUROPEAN SOLUTION

Faced with the risk that national aid might not save national production capacity, some policy makers have thought about territoriality requirements. The Commission has firmly opposed such measures. Already in the Communication, the Commission mentioned the need for "*coherent, efficient and co-ordinated*" measures[648], in order to safeguard the essential link between State aid and the Internal Market.[649] The Commission's role in co-ordinating national aid to address the difficult situation of GM has dominated the press in the months after the Communication was issued. In particular, on March 13, 2009, an informal meeting was held between GM representatives, Commissioners Verheugen, Kroes and Špidla, and ministers from relevant Member States (Austria, Belgium, Czech Republic, Germany, Spain, Hungary, Luxembourg, Poland, Portugal, Romania, Sweden). Those present agreed that no national measures should be taken without prior information and coordination with other involved countries, thereby also acknowledging the role of the Commission as the "facilitator" to achieve a coordinated solution.[650] The Commission's attempt to reach a coordinated solution for the GM restructuring is a significant development for State aid policy.

In assessing a planned aid measure, the Commission's role is essentially limited to verifying whether the measure fits within one of the categories that give rise to an exception – normally as provided in Article 87(3)(c) EC and more recently, as discussed above, within the scope provided by Article 87(2) EC. Accordingly, the dialogue between the Commission and the Member State is one where – in formal terms – the latter is asking the former for derogation from a general rule. In February 2009, the French President indicated that car manufacturers would be required to invest in France, or to buy their components from suppliers located

648 Communication (n 19) p. 5.

649 Communication (n 19) p. 2 ("It is therefore essential that state aids and other measures are well directed, working to build the future strength of the industry rather than introducing short-term distortions that will damage long-term competitiveness.").

650 Commission Press Release MEMO/09/108 of 13 March 2009.

in France in return for aid, i.e. to use territoriality requirements.[651] By objecting to the imposition of territoriality requirements,[652] the Commission ensured respect of the general prohibition against incompatible State aid.

In the GM restructuring saga, the Commission played a different role. The Commission sat together with the Member States concerned to design a suitable aid measure. Thus, the Commission has been able to carve out for itself the role of a European authority coordinating national aid measures, rather than acting as the mere policeman. This development is especially significant insofar as it represents one of the few attempts to overcome the limited ability of the Commission to use State aid rules when truly pan-European issues arise. When faced with issues of a cross-border scale, national aid is often a sub-optimal solution. If a plant remains open at a given location because of an aid measure subject to territoriality requirement, both the workers in the country giving the aid and the workers in neighbouring countries will be worse off. The latter are obviously penalized because they lose their jobs. With respect to the former group, if a rescue is not based on sound economics, the aid will simply postpone their problems, without solving them. The Commission's apparent willingness to act as the broker of an agreed-upon, coordinated multi-country State aid measure is in many ways a welcome development in the field of State aid. Nevertheless, as the subsequent debates about the merits of the proposed German aid package to rescue Opel have confirmed, the Commission has found itself in a political hot seat and its role as facilitator will depend on its ability to reach a fair deal for all concerned.

11. OLYMPIC AIRWAYS

In addition to the car sector, the Commission has reviewed other industries where restructuring efforts were already under way but which required a different approach as a result of the crisis. In the airline sector the Commission approved, in October 2008, the launch of a selection procedure for a private investor to purchase various assets from Olympic Airways and Olympic Airways Services. After a prolonged series of investigations and recovery actions, the Greek government had decided to privatise its national flag carrier and therefore went to some lengths to ensure that these companies could be sold off without the risk

651 Commission Press Release MEMO/09/50 of 4 February 2009.

652 Commission Press Release MEMO/09/90 of 28 February 2009.

of giving aid to the Olympic companies or to the private investor purchasing the assets. Care also had to be taken to avoid the transfer of existing state liabilities to an potential purchaser. Having concluded an unsuccessful open tender procedure in late 2009, the Greek government sought Commission approval for a negotiated sale of the assets in question at market price to a private investor. The failure of the original open tender process was largely to be attributed to the impact of the financial crisis and the willingness and ability of potential investors to acquire these assets. Hence a direct negotiation was approved as this was still deemed to secure a market price and would therefore satisfy the conditions for the application of the "private investor" process.

12. CONCLUSION

The aid measures approved under the Temporary Framework are expected to have a limited shelf life, and are supposed to be targeted at a specific set of problems. Unlike the rescue aid measures approved with what some might consider indecent haste under the various Communications for the financial sector, the measures approved under the Temporary Framework will not be subject to detailed scrutiny because they have not been linked to an obligation for detailed future review. An interim review is required and presumably if the Commission is unsatisfied with the results, it could require the Member State to withdraw the measure, given that it has powers, together with the Member State in question, to keep all existing aid measures under review. At the same time and as indicated in this contribution, large amounts of aid have been approved under the Temporary Framework. It must also be borne in mind that not all States have the capital to finance large-scale bail outs so that the Commission's goal of avoiding protectionism and distortions of global markets is not always easy to realise if at the same time it is required to approve large-scale subsidy schemes in individual States. The guiding principle which has informed the SAAP – and has led to the modernisation of the European state aid policy – has been, after all, the desire to achieve "less and better targeted aid". Given the scale and complexity of the current crisis, this may have become an impossible goal. Every crisis produces winners and losers. It is certainly not the purpose of the state aid rules, nor the job of the Commission, to separate out the one from the other. But if the Commission is able to ensure a co-ordinated response and to prevent the resurgence of what became known as economic patriotism then at least it can be said with some assurance that the European state aid regime can emerge intact and for the real economy at least, that return to business as usual is not an impossible dream.

Hanna Jahns

THE COHESION POLICY OBJECTIVES AND THE STATE AID CONTROL IN THE CONTEXT OF USING STRUCTURAL FUNDS IN POLAND

1. INTRODUCTION

The main objective of cohesion policy implemented by the European Community, provided for as far back as the Treaty establishing the European Community, is to reduce disparities between individual regions and the backwardness of the less developed areas, in other words to achieve economic and social cohesion. Interventions implemented from the Community budgetary resources through the Structural Funds and the Cohesion Fund are the instruments of cohesion policy.

At the same time, the Community legislation on the granting of State aid aims at protecting competition in the Single Market from distortions and disruptions resulting from State intervention, because competition policy rests upon the idea that a market-based economy provides the best guarantee for raising living conditions in the European Union[653].

This simple comparison of the main principles underlying cohesion and competition policies already shows certain opposition of the objectives pursued by these policies.

2. PRINCIPLES OF STATE AID POLICY AND PRINCIPLES OF COHESION POLICY

The basis for recognising the aid granted from State resources as State aid is included in Article 87(1) of the Treaty establishing the European Community (TEC), which stipulates the following:

> *"Save as otherwise provided in this Treaty, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to*

653 For more information on State aid in the context of the cohesion policy interventions please see the guidelines prepared by the Ministry of Regional Development, i.e. *Pomoc publiczna w programach operacyjnych 2007-2013*, March 2008.

distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the common market."

Therefore, aid is considered to be State aid if it meets four conditions: a transfer of State resources takes place in any form; the beneficiary gains an economic benefit which is impossible to obtain through normal business activity; the measure is used selectively and granting it may have a potential impact on competition and trade between Member States. In principle, such aid is prohibited within the Single Market, although certain exceptions to this rule are possible and will be discussed further in this article.

At the same time, Article 158 of Title XVII "Economic and social cohesion" of TEC provides that the Community shall pursue its actions leading to the strengthening of its economic and social cohesion and, consequently, it aims at reducing disparities between the levels of development of the various regions and the backwardness of the least favoured regions or islands, including rural areas. Therefore, regional aid through concentration on specific regions is assumed to be selective aid[654].

Exceptions to the general prohibition on granting State aid are contained in Article 87(2) and (3) of TEC. Article 87(2) defines State aid that is automatically considered to be compatible with the common market, while the conditional exceptions defined in Article 87(3), are relevant from the point of view of this publication as they allow granting State aid if the conditions specified therein are met.

The following may be considered to be compatible with the common market:

- aid to promote the economic development of areas where the standard of living is abnormally low or where there is serious underemployment;

- aid to promote the execution of an important project of common European interest or to remedy a serious disturbance in the economy of a Member State;

654 Vademecum *Community rules on State aid* of 30 September 2008, prepared by Directorate General for Competition of the European Commission.

- aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest;

- aid to promote culture and heritage conservation where such aid does not affect trading conditions and competition in the Community to an extent that is contrary to the common interest;

- such other categories of aid as may be specified by decision of the Council acting by a qualified majority on a proposal from the Commission.

Derogations from the general prohibition on granting State aid allow to seek the overriding Community objective, i.e. "*a harmonious, balanced and sustainable development of economic activities, (...) a high degree of competitiveness, (...) the raising of the standard of living and quality of life, and economic and social cohesion and solidarity among Member States*". One should however note that on account of the fact that granting State aid is considered to be an exception to the general prohibition on providing State assistance for entities competing in the market, its admissibility is interpreted strictly, and consequently relatively restrictive criteria are imposed on entities benefiting from the measures.

3. IMPLEMENTATION OF COHESION POLICY AND RESTRICTIONS ON THE GRANTING OF STATE AID

Systems established in Member States for the implementation of programmes financed with structural funds have to comply not only with the relevant rules and principles concerning the management and control of the use of funds, but also with a number of regulations originating in other cross-section, or horizontal policies, including State aid policy. Therefore, compliance with the requirements on State aid is one of the aspects of implementing cohesion policy.

The scale of the impact of State aid policy on cohesion policy can be illustrated with the example of allocations under structural funds available to Poland in the financial perspective 2007-2013. In this period, Poland will allocate 85.6 billion euros (i.e. 67.3 billion euros of EU funds and 18.3 billion euros of national funds) for the achievement of cohesion policy objectives. At the same time, it is assumed that a considerable part these funds, i.e. about 40 billion euros may be subject to the State aid regime. Almost 400 out of over 500 measures envisaged in the operational programmes under the National Strategic Reference Framework (NSRF) 2007-2013 encompass the implementation of projects using State aid.

4. LEVELS OF POSSIBLE ASSISTANCE FROM STRUCTURAL FUNDS AND ALLOWABLE STATE AID CEILINGS

In the financial perspective 2007-2013, the European Regional Development Fund (ERDF), the European Social Fund (ESF) and the Cohesion Fund pursue the following three objectives:

1. Convergence,
2. Regional competitiveness and employment,
3. European territorial cooperation.

Under the Convergence objective, the regions covered by it will be able to receive support from the Community budget at the level of 85 percent of eligible expenditure. In 2007-2013 (similarly to the previous financial perspective 2004-2006), Poland benefits from the maximum level of co-financing from the EU funds under Objective 1 and in addition it also implements programmes covered by Objective 3.

Allowable State aid can be divided into regional, sector and horizontal aid. The prevailing type of State aid granted under the operational programmes in the period 2007-2013 is regional aid granted in regions that are lagging behind in their economic development (in accordance with Article 87(3)(a) of TEC). It is considered that these are regions where the gross domestic product *per capita* is lower than 75 percent of the average GDP in EU-25.

In the period 2007-2013, the whole territory of Poland has been covered by the above-mentioned derogation. According to the regional aid map[655], the higher GDP *per capita* of a given region, the lower allowable aid intensity (understood as a percentage of eligible expenditure covered by State aid). In Poland, "regions" are areas classified at NUTS[656] II level, that is, *voivodeships* (provinces).

655 Regulation of the Council of Ministers of 13 October 2006 on regional aid map (Journal of Laws No 190, item 1402).
656 Nomenclature of territorial units for statistics (NUTS).

According to the regional aid map the allowable aid intensity must not exceed:

- 30 percent of the gross grant equivalent (GGE) – for regions where the GDP *per capita* is lower than 75 percent of the EU-25 average GDP *per capita* (the area of the capital city of Warsaw as well as the Mazowieckie Voivodeship in the period from 1 January 2011 to 31 December 2013),

- 40 percent of the GGE - for regions where the GDP *per capita* is lower than 60 percent of the EU-25 average GDP *per capita* (the following voivodeships: Pomorskie, Zachodniopomorskie, Dolnośląskie, Wielkopolskie, Śląskie as well as the Mazowieckie Voivodeship, excluding the capital city of Warsaw, in the period from 1 January 2007 to 31 December 2010),

- 50 percent of the GGE - for regions where the GDP *per capita* is lower than 45 percent of the EU-25 average GDP *per capita* (the following voivodeships: Lubelskie, Podkarpackie, Warmińsko-Mazurskie, Podlaskie, Świętokrzyskie, Opolskie, Małopolskie, Lubuskie, Łódzkie, Kujawsko-Pomorskie).

At the same time, some entities, particularly small and medium-sized enterprises, benefit from preferential treatment. The regional aid map provides for an increase in aid levels for small and medium-sized enterprises by 20 and 10 percentage points, respectively.

It is hard not to notice that the allowable assistance under projects with State aid is significantly lowered in comparison with the level of assistance available to be granted in accordance with Objective 1 of Cohesion Policy, especially in the case of regions where the GDP *per capita* reaches values which result in including them in the lowest ceiling.

5. PROCEDURE FOR NOTIFYING STATE AID MEASURES

Another difficulty in achieving the objectives of cohesion policy resulting from the need of compliance with the State aid regime is the lengthy and complicated course of notification procedures regarding the aid measures which require acceptance from the Commission.

At the Community level, the notification procedure is governed by Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty.[657] This procedure consists of two phases, namely preliminary examination and the formal investigation procedure. In accordance with Article 4(5) of the Regulation, the preliminary procedure before the European Commission lasts up to two months from the receipt of a complete notification. If the case is not resolved at this stage, the formal investigation procedure is initiated, during which *"the Commission shall as far as possible endeavour to adopt a decision within a period of 18 months from the opening of the procedure."*

The wording of the relevant provisions and the rules on the calculation of time limits may cause the notification procedure to be prolonged considerably. At the same time, Article 3 of the Regulation introduces a standstill clause, i.e. a rule that "*aid notifiable pursuant to Article 2(1) shall not be put into effect before the Commission has taken, or is deemed to have taken, a decision authorising such aid*". The time limits guarantee that any notifiable assistance measure will be fairly and thoroughly evaluated, and the aid granted will not be unlawful. On the other hand, if often prolonged, the procedure may delay the mobilisation of funds available for the implementation of projects subject to the State aid regime, which requires the notification of the assistance scheme in order for the assistance to be granted.

6. THE REFORM OF STATE AID POLICY AND ITS IMPACT ON THE IMPLEMENTATION OF COHESION POLICY

The European Council of March 2005 encouraged Member States to limit the overall level of State aid. All the same, the Council called for redirecting aid towards horizontal objectives such as research and innovation, optimisation of human capital, development of renewable energy, counteracting climate change and other measures in the field of environmental protection. In this spirit, in 2005, the European Commission initiated the reform of State aid policy to rationalise and simplify granting such aid as well as to ensure its greater transparency.

In accordance with objectives included in the State Aid Action Plan of 7 June 2005[658], in order to simplify and rationalise the granting of State aid Commission Regulation (EC) No 800/2008 declaring certain categories of aid compatible with the common market in application of Articles 87 and 88 of the Treaty (General Block Exemption Regulation – GBER) was adopted on 6 August 2008.

657 OJ L 83, 27.3.1999, p. 1–9, as amended.
658 COM(2005)107 final.

The Regulation gathered and harmonised the rules which were previously included in four separate Regulations. GBER replaced the existing provisions concerning block exemptions in the following areas:

- regional investment aid,
- aid to small and medium-sized enterprises (SMEs),
- training aid,
- employment aid.

Furthermore, GBER has extended the scope of block exemptions to cover five types of aid, i.e.:

- environmental aid,
- innovation aid,
- aid for research and development for large enterprises,
- aid in the form of risk capital,
- aid for enterprises newly created by female entrepreneurs.

Measures serving any of the goals specified in by GBER meeting the conditions and criteria detailed therein do not need to be notified to the European Commission, which means that Member States may apply these measures on the basis of assistance schemes adopted at national level without the need to obtain a decision of the European Commission.

Therefore, granting of State aid under block exemptions may take place immediately after the Member State has established the assistance measure – there is no waiting for the position of the European Commission because it is not required. For this reason, while developing assistance measures, Member States attempt, if possible, to make them eligible for block exemptions. This also applies to assistance schemes prepared by the Polish government for the purposes of the implementation of operational programmes in the period 2007-2013.

In Poland, the granting of state aid under the Structural Funds and the Cohesion Fund is at present regulated by the total of 32 assistance schemes.

In particular, 21 assistance schemes have been opened to date under block exemptions, providing support for:

- In the Innovative Economy Operational Programme – investments of great importance for the economy, innovation, the creation and development of e-economy, the development of broadband access to the Internet, research and development, business environment institutions and innovation centres, investments in tourist products;

- In the Infrastructure and the Environment Operational Programme – business investments in water and sewage management and fresh air protection, high-efficiency energy generation, production of energy from renewable sources;

- In the Human Capital Operational Programme – broadly understood assistance for the labour market (including training, consulting services for SMEs, professional activation of the unemployed);

- In the Regional Operational Programmes – investments (various types of activity), training, consulting services for SMEs, business environment institutions;

- In the Eastern Poland Development Operational Programme – the development of congress tourism and trade fair travels, innovation, the development of business cooperation networks.

It needs to be emphasised that not all types of activity are covered by the exemption from the notification requirement. If aid is granted on different basis, e.g. Community guidelines setting the conditions for State aid in a given field, or pursuant directly to a relevant provision of the Treaty, the assistance scheme or individual aid measure is subject to the notification procedure. Under the implementation system for the NSRF 2007-2013 in Poland, to date, seven assistance schemes have been drawn up on the basis of Community regulations other than block exemptions (and therefore they are subject to the notification procedure which is described in the further part of this publication). Those schemes regulate granting assistance for: the development of risk capital funds, business activities aiming to improve the environment protection and to rationalise the use of resources, the development of airports (both at the national and regional levels), the development of intermodal transport[659] (both at the national and regional levels).

One should also note that all operational programmes for 2007-2013 provide for the possibility of *de minimis* aid, i.e. aid limited, in principle, to 200 thousand euros (or 100 thousand euros in the road transport sector) for one enterprise during three fiscal years. It is assumed that on account of its limited size, this aid does not influence the trade and competition between Member States (therefore not all conditions defined in Article 87(1) of the Treaty are met).

In the context of implementing the NSRF 2007-2013, assisting enterprises in the form of *de minimis* aid has the same advantage as aid granted on the basis of exemptions – assistance schemes regulating the granting of *de minimis* aid do not have to be notified to the European Commission, which means that the regulations adopted at the national level are sufficient for the mobilisation of funds, thus avoiding possible delays.

Under the operational programmes for 2007-2013, four separate assistance schemes concerning exclusively *de minimis* aid have been adopted to date; moreover, some assistance schemes drawn up on the basis of exemptions also include *de minimis* aid.

An example of State aid of the same type, but based on different Community regulations, is regional aid, which is, in principle, the most important type of State aid granted under the operational programmes 2007-2013. It can be granted both under the conditions provided for in the block exemptions and with the use of recommendations included in the Guidelines on national regional aid for 2007-2013 published by the European Commission in December 2005.[660] The Guidelines cover a broader scope of aid than the General Block Exemption Regulation. Unlike the latter, the Guidelines provide also for granting operational aid to enterprises, which is, in principle, prohibited, but may be granted on the condition of contributing to regional development. However, the Guidelines as such cannot be the basis for declaring certain types of aid to be compatible with

659 Transport of cargo by more than one mode of transport.

660 OJ C 54, 4.3.2006, p. 13, 2006/C 54/08.

the common market and exempted from the requirement of notification to the Commission – they only describe criteria that must be met by regional assistance schemes in order to be considered – after prior notification – as allowable State aid. Therefore, the decision whether aid is allowable is made by the European Commission, which requires completing a complex and often prolonged notification procedure.

Considering the above, in the State aid system there may be some duality of the Community regulations constituting the basis for the adoption of national assistance schemes. It means that different assistance schemes with partly divergent regulations may apply to the same type of aid, even in the framework of the same operational programme.

Probably the most characteristic example of such duality are the two assistance schemes drawn up under the regional operational programmes which regulate the granting of regional investment aid. One of them was developed based on block exemptions in the field of regional investment aid and the second on the basis of the Guidelines on national regional aid for 2007-2013. Since these national legal acts were based on different Community regulations, their provisions are perforce divergent to some extent (first of all this concerns the so-called incentive effect, i.e. defining the moment when the beneficiary can begin working on the project, which is relevant in the context not only of expenditure eligibility, but also, or maybe above all, of the lawfulness of State aid). As a result, in this situation, institutions granting aid under the NSRF 2007-2013 will need to apply two legal regimes in parallel, so to speak, possibly with reference to many very similar projects.

7. THE LISBON STRATEGY IN STATE AID POLICY AND COHESION POLICY

Reforming State aid policy, the European Commission has also taken actions aimed at including State aid policy into process of implementing the Lisbon Strategy, as the reform aimed at encouraging Member States to redirect aid towards stimulating growth and jobs.

Discussing exceptions provided for in State aid regulations, it needs to be noted that priority was also given to entities and actions which implement the Lisbon objectives. One of the manifestations of this approach is the fact of including new categories of aid under block exemptions (which was mentioned above) and the preferential treatment of small and medium-sized enterprises by adopting regulations that enable SMEs to benefit from higher aid intensity levels.

The Lisbon Strategy is also one of the cohesion policy priorities. While preparing the National Strategic Reference Framework (NSRF) which defines the priorities of interventions under the Structural Funds and the Cohesion Fund in 2007-2013, Poland was the only new Member State which took up the challenge of transferring at least 60 percent of the funds to Lisbon goals. They include, among others, increasing and improving investment in Research and Development, extending and deepening integration within the Single Market, expanding and improving European infrastructure and more investments in human capital through better education. According to calculations as of April 2008, nearly 64 percent of allocations for 2007-2013 under operational programmes which implement the Convergence objective (i.e. 16 regional operational programmes and four national programmes) implement the Lisbon Strategy objectives at the same time.

Operational programme	**The programme's objectives which are conducive to the Lisbon Strategy and may involve State aid**
Innovative Economy	Increased innovativeness of enterprises to keep the economy on the track of fast development and to create new and better jobs by means of: assistance for innovative undertakings, support for new investments, consulting services and training essential to investments, assistance for the creation of new and innovative enterprises.
Human Capital	Increased employment level and quality of education in the society as well as adjusting labour resources to the changing situation in the labour market by means of: investments designed for the human capital development, the improvement of quality and availability of consulting and training services supporting entrepreneurship, assistance for staring new businesses and the promotion of entrepreneurship activities.
Infrastructure and the Environment	Aid in three areas – environment, transport and energy: assistance for investments related to the best available techniques, renewable energy sources, waste management, and water and sewage management.
Eastern Poland Development	Support for innovation and the development of tourist infrastructure by means of: establishing close cooperation between academia and economic entities; assistance for infrastructure required to run innovative business activity; the construction, modernisation and development of trade fair and congress centres.

We are well aware of the significance of the impact of the requirements related to the implementation of horizontal State aid policy on the implementation of cohesion policy. This impact is illustrated both by the above mentioned data on potential State aid to be granted under the operational programmes for 2007-2013 and the described legal and procedural complexities. The effects of overlapping requirements connected with the implementation of cohesion policy and State aid policy are felt by institutions responsible for the implementation of structural funds, as well as individual beneficiaries. The most significant among them is a decrease of aid intensity as regards measures implemented under operational programmes which are subject to the State aid regime and additional obligations concerning the procedures governing State aid. In spite of the simplifications introduced by the European Commission as part of the State aid policy reform, the procedures are time-consuming, also on account of the complexity of the cases, contributing to delays in the initiation of part of the resources benchmarked for the cohesion policy implementation. This was the case of programmes implemented in Poland in the financial perspective 2004-2006 and is also observed in the current allocation for 2007-2013.

On the other hand, State aid legislation invokes the general principles governing all the Community policies, namely the principles of transparency, proportionality, cohesion, and subsidiarity. The principle of cohesion, also known as the principle of European solidarity, consists in the EU's aspirations to eliminate disparities in development between its Member States and regions. At the same time, this principle underlies also the EU cohesion policy.[661]

Therefore, contrary to seemingly opposing objectives, the principles underlying both policies are common. Institutions responsible for programming further development of these policies should strive to find common grounds so that complementary actions aimed at effective reduction of development lags in some regions can be taken. Such actions should respect restraints of free-market economy by the state which are absolutely indispensable under the competition policy, yet, at the same time, these actions should manifest European solidarity. An extensively restrictive approach towards State aid should not obstruct efforts aiming at an effective reduction of backwardness of the EU regions and stimulating their development, since its main driving force lies in entrepreneurship.

661 I. Postuła, A. Werner, *Prawo pomocy publicznej*, LexisNexis, Warszawa 2008, p. 103 -105.

Magdalena Kąkol

ECONOMIC RATIONALE FOR SUPPORTING ENTERPRISES FROM PUBLIC RESOURCES – ECONOMIC EFFICIENCY ASSESSMENT

1. INTRODUCTION

State aid is one of state policy instruments for the implementation of social and economic, and occasionally political, objectives. In accordance with neoclassical economics, markets are largely capable of self-regulation and they retain a high competition level and produce efficient results if allowed independent operation, without state intervention. Therefore, in the view of the proponents of neoclassical theory increasing economic (essentially allocative) efficiency is the main criterion justifying the use of state aid. They notice a contradiction between the implementation of the efficiency objective and the objective to provide a more even distribution of income within the society (redistribution/equity objective), which is often state-preferred for social reasons. According to the neoclassical approach, measures aimed at the improvement of redistribution cause side-effects in the form of economic efficiency reduction.[662] Therefore, there is a need to select an objective we want to achieve, since it is impossible to attain them both simultaneously.[663]

Other schools of economic thought are not that rigorous and do not require the separation of both objectives. According to Keynes, increasing efficiency, being the condition for the economic growth, is compliant with a more even distribution of income. This is so, since financial resources are obtained by persons with greater propensity to consume than the better-off ones. They allocate a larger part of their income for consumption and thus stimulate economic growth.[664] Keynes' supporters maintain that markets are, by nature, not stable and state intervention

662 Mankiw and Taylor emphasise that redistribution of income from the rich to the poor causes the decline in producer remuneration, and as a result, the producers are less willing to work, which is followed by a lower goods and services level. N.G. Mankiw, M.P. Taylor, *Economics, Thomson Learning*, London 2006, p. 5.

663 For more, cf. H.W. Friederiszick, L.-H. Röller and V. Verouden, *European State Aid Control: An Economic Framework* (in:) P. Buccirossi (ed.), *Handbook of Antitrust Economics*, The MIT Press, Cambridge, MA, London 2008, p. 635 and C. Kaupa, *The More Economic Approach – a Reform based on Ideology?*, „European State Aid Law Quarterly", No. 3, 2009, p. 312 and 317.

664 J. Keynes, *The General Theory of Employment, Interest and Money*, London 1967, p. 23. Cited after C. Kaupa, The More, op. cit., p. 317.

may contribute to an improvement in their functioning and achieving more efficient outcomes. Such opinions gain popularity during the economic and financial crisis experienced today by the global economy.[665]

The aim of this study is: 1) to present the most important economic arguments justifying the use of state aid from a theoretical perspective, 2) to characterize the EU approach to economic efficiency criterion at assessing state aid measures, 3) to evaluate the legitimacy of state aid provided by selected countries from the point of view of economic efficiency and potential influence on distortions of competition and 4) to identify the efficiency conditions of state aid policy.

2. ECONOMIC ARGUMENTS FOR AND AGAINST STATE AID FROM A THEORETICAL PERSPECTIVE[666]

State aid is a topic of research in several fields of economics, including above all public economics, theory of competition and theory of international trade.[667] One of the tasks of public economics is to specify whether state intervention is effective for the national economy; the theory of competition concentrates on assessing the impact of state aid on competition (i.e. the level of competition on a given market and its efficiency, as well as on the competitive position of aid beneficiaries and their competitors); while the theory of international trade sees applying aid by specific countries as the possibility of their expansion onto international markets.[668]

Welfare economics equates economy (or market) efficiency with allocative efficiency, that is, according to Pareto, such a way of allocating resources that makes it impossible to improve an individual's situation without simultaneously worsening the situation of somebody else (by reducing his/her welfare or utility).[669] This means that economy (market) should achieve: production efficiency, efficient production structure and exchange efficiency (see Figure 1). The Pareto criterion is met in perfect competition conditions, in the state of general equilibrium.

665 See e.g. L.R. Wray, *The rise and fall of money manager capitalism: A Minskian approach*, „Cambridge Journal of Economics", Vol. 33, No. 4, 2009, p. 808.

666 For more on that topic, see M. Kąkol, *Czy istnieje ekonomiczne uzasadnienie stosowania pomocy państwowej w Unii Europejskiej?*, Annales UMCS, Vol. 43, Wydawnictwo UMCS, Lublin 2009. Point 2 includes exerpts from this study.

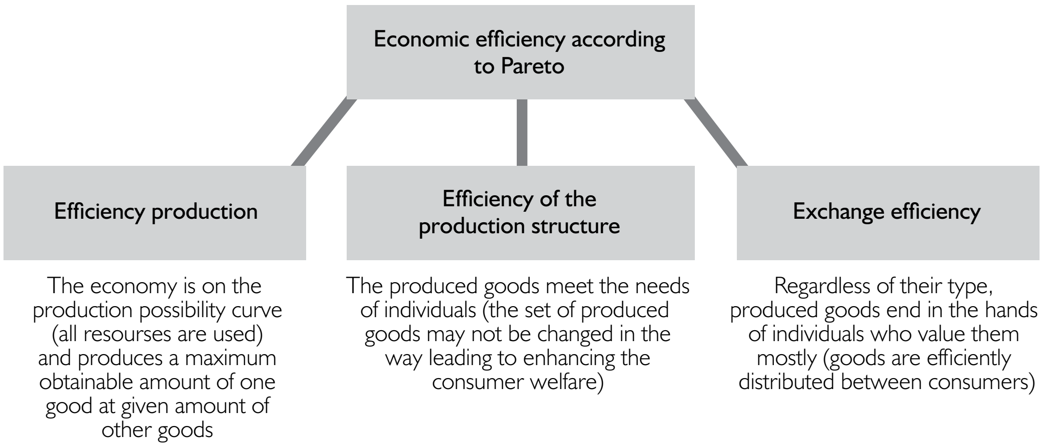
667 H.W. Friederiszick, L.-H. Röller and V. Verouden, European, op. cit., p. 631.

668 Cf. ibid.

669 J.E. Stiglitz, *Ekonomia sektora publicznego*, Wydawnictwo Naukowe PWN, Warszawa, 2004, p. 69-70.

Currently, the so-called dynamic efficiency, related to technological progress and acceleration of conomic growth, plays an ever more vital role. According to L. Peeperkorn[670], it is defined by the changes in overall social welfare over a longer period, due to the introduction of innovative products and processes.

Fig. 1. Economic efficiency from the Pareto perspective



Source: Prepared on the basis of J.E. Stiglitz, Economy, op. cit., p. 76-87.

From the point of view of the enterprise, economic efficiency means using production factors in a way that minimizes product cost per unit.[671] Improvement of such efficiency, every so often as a result of obtaining subsidies, leads to the rise in: sales volume and market share, profits, productivity (mainly labour productivity and total factor productivity[672]), and if activity is under development, this might also involve employment growth in the enterprise. Therefore, increased efficiency means better competitiveness.

Economic efficiency is most frequently analysed in terms of the total welfare function, i.e. the sum of consumer surplus (the difference between the amount the consumer is prepared to pay and the amount he actually pays) and producer surplus (profit) on a given market.[673] State intervention should take place when

670 L. Peeperkorn, *Dynamic Welfare Analysis of Market Power* (in:) J. Faull, A. Nickpay (eds.), *The EC Law of Competition*, Oxford University Press, 1999, s. 39.

671 D.C. Colander, *Economics*, Irwin, Homewood, Boston 1993, p. 469.

672 *Total Factor Productivity* is a measure most of all allowing the contribution of technological progress into economic growth.

673 By the term "total social welfare" the author understands producer and consumer surplus, but she does not refer to redistribution issues, which is the question of valuation.

the increase in social welfare is higher than the intervention's cost.[674] Government intervention may enhance efficiency and improve markets' functioning (pass the welfare test), if, when left alone, the markets are unable to deliver efficient outcomes in the form of appropriate prices, output level and allocation of resources. Such situations are described as market imperfection or failure.[675] In the view of Rod Meiklejohn, as regards state aid, nine market failures justifying its application should be taken into account:[676]

- existence of public goods, the access to which cannot be limited, e.g. street lamps, radio;
- the need to deliver merit goods, the consumption of which falls below a desired level in the free market conditions, such as education, culture, health services;
- growing economies of scale, leading to a monopolistic or an oligopolistic market structure, and thus higher prices and lower than optimal production levels;
- external effects, e.g. knowledge spillovers (dissemination of knowledge being the result of research activity), vocational training, environmental pollution;
- imperfect or asymmetric information;
- institutional rigidities (employment protection rights, minimum wages, unemployment benefits);
- imperfect mobility of production factors;
- frictional (structural) problems regarding the adjustment to market changes (justifying restructuring aid);
- subsidisation of foreign competitors.

Although market failures constitute economic justification for aid, its efficiency depends, in fact, on a range of factors. Subsidies may lead to sub-optimal results due to the following reasons:[677]

674 H.W. Friederiszick, L.-H. Röller and V. Verouden, *European*, op. cit., p. 632.

675 Ibid., p. 632-633. For more, cf. J.E. Stiglitz, *Ekonomia*, op. cit., p. 91 et seq.

676 European Commission, State Aid and the Single Market, „European Economy", No. 3, 1999, p. 25-31.

677 H.W. Friederiszick, L.-H. Röller and V. Verouden, *European*, op. cit., p. 637 and I. Hashi, D. Hajducovic, E. Luci, *Can*

- difficulties in measuring market failure in quantitative terms, e.g. external effects are not an object of market transactions and not only it is hard to assess their range, but also to assign a specific value to them. In fact, it is only the qualitative assessment that is usually possible, i.e. establishing whether a failure exists and if it is significant;

- the benefit resulting from the aid should be higher than its costs, i.e. the alternative cost of allocating public resources to a different use and the cost of raising funds by taxing the society. Even if we assume that aid has been appropriately used in appropriate circumstances, it may not turn out to be efficient if its impact is smaller than expected, e.g. if it addresses a minor failure, while its costs are high;

- subsidies affect the functioning of the market and may cause anticompetitive side effects, the ultimate costs of which are incurred by consumers. Some of these effects may be limited to the domestic market, yet some may also affect neighbouring countries' enterprises and consumers;

- one of the objectives of granting aid is to redistribute income and to raise the living standards of the poorest members of the society. This objective often contradicts economic efficiency. Moreover, it can be better achieved via direct income support and it will not influence the structure of consumption and production as strongly as state aid;

- for political reasons, including elections. Politicians remain under pressure of various interest groups, which prevents them from undertaking economically justified interventions and allowing them to take actions only if they are a result of a compromise between their coalition partners, on whom the legislative process depends;

- once started, an intervention is difficult to cease – it is hard to quit if it serves a given interest group;

- as long as enterprises receive state aid, they are protected against competition and lack incentives to improve efficiency.

Government Policy Influence Industrial Competitiveness: Evidence from Poland and the Czech Republic, Project „Changes in Industrial Competitiveness as a Factor of Integration: Identifying Challenges of the Enlarged Single European Market" funded by 5th Framework Programme of the EC, coordinated by A. Wziątek-Kubiak, CASE Foundation, Warszawa, End-of-Project Conference, Work Package 2, Brussels, November 2005, p. 7.

H.W. Friederiszick, L.-H. Röller and V. Verouden[678], who concentrated their research on state aid control policy in the European Union, emphasize that even if the purpose of public resources is to eliminate market failures, they may still contribute to significant distortions of competition in the market, when other failures appear as a result of their application. They distinguish four types of distortion of competition resulting from granting state aid in the common market. These concern:

- supporting inefficient production, which helps inefficient enterprises stay on the market and, in consequence, leads to decreased production efficiency and the lower efficiency of the economy as a whole (total welfare);

- distorting the dynamic investment incentives for enterprises, which results in the reduction of dynamic efficiency and total welfare in the long-run;

- the increase in the beneficiaries' market power, leading to the exclusion of current or potential competitors from the market, if the aid granted helps create entry barriers to this market and;

- distorting decisions concerning location of production across Member States, which may result in inefficient allocation of production factors and production structure in the EU.

The first three types of distortions refer to lessening of effective competition between enterprises, and the last one shows the impact that state aid may have on competition between member countries.

The above presented arguments suggest that state aid is not the best way to eliminate market failures and increase economic efficiency, at least not in every single case, and before we decide to apply state aid, we should think of other policy instruments that might potentially be used (e.g. regulation, taxation) and be more effective in a given situation.[679] The most important issue is thus to adjust the intervention's range and form to the size and type of the problem faced.

678 H.W. Friederiszick, L.-H. Röller and V. Verouden, *European*, op. cit., p. 652-654.

679 For more on the alternative state intervention forms, see Ch. Buelens, G. Garnier, R. Meiklejohn and M. Johnson, *The economic analysis of state aid: Some open questions*, European Commission, „European Economy. Economic Papers", No. 286, September 2007, p. 12.

If aid granted by EU Member States contributes to increased competitiveness of domestic enterprises, sectors or industries of the national economy, and improves their position in international trade, then we can be certain that the aid was economically justified and was appropriately used. Not only does this lead to the growth in domestic welfare, but also to the improvement of the economic position of the entire grouping in the global economy. Such argumentation has been eagerly used by proponents of a strategic trade policy. They try to explain in what circumstances a country or a group of countries can benefit, at the expense of their competitors in the international markets, from foreign trade due to state intervention, including subsidies. In this case an intervention is justified by failure in international markets, which most frequently take the form of oligopolies.[680] However, state intervention does not always lead to the social welfare growth in the global scale. For example, in A.Cournot's duopoly model (quantitative competition), export subsidy results in the decline in consumer prices and the growth of domestic and global welfare; while in J. Bertrand's model (price competition), in order to gain advantage in the international market, authorities are forced to impose export taxes, which leads to the increase in (domestic and foreign) prices and, in the end, to the reduction of global welfare.[681] The concept of strategic trade policy may be applied both to trade policy theory and the theory of competition, and in particular to non-cooperative game theory.[682]

3. EUROPEAN UNION POLICY TOWARDS AID GRANTED BY MEMBER STATES AND ITS APPROACH TOWARDS THE ECONOMIC EFFICIENCY CRITERION

As a member of the European Union, Poland must conform to the competition rules, including state aid rules, binding within the EU's entire area. Despite a general ban on granting state aid which distorts competition and has an impact on trade between Member States (Article 107(1) of the Treaty on the Functioning of the European Union, previously Article 87(1) of the Treaty establishing the European Community), there are several exemptions to this rule. Article 107(2) TFEU (formerly Article 87(2) of the EC Treaty) presents circumstances authorising

680 For more, see Ch. Van Marrewijk (in cooperation with D. Ottens and S. Schueller), *International Economics. Theory, Application, and Policy*, Oxford University Press 2007, p. 228-235.

681 Cf. ibid., p. 228-231.

682 For more, see M. Kąkol, *Pomoc państwowa w polityce konkurencji w Unii Europejskiej*, Biuletyn Europejski 2006/2007, scientific editor of the series B. Mucha-Leszko, Wydawnictwo UMCS, Lublin 2007, p. 60.

the use of aid by virtue of law[683], and Article 107(3) TFEU (previously Article 87(3) of the EC Treaty) mentions situations when aid may be deemed acceptable upon the decision of EU authorities.[684] Therefore, primary law allows EU institutions to authorise potential distortions of competition resulting from state aid if they help achieve other EU objectives – of economic, social and political nature.[685] In practice, it is the European Commission (a supranational institution) which controls aid granted by EU Member States. Traditionally, four types of state aid monitored by the Commission may be distinguished, each characterized by a different capacity to distort competition in the Internal Market: horizontal, regional, sectoral, and rescue and restructuring (R&R) aid (see Table 1). Regional, sectoral and R&R aid distort competition since they favour one enterprise, industry or region at the expense of others in the same country or other EU countries.

Table 1. Types of state aid granted by EU Member States as regards their potential to distort competition in the Internal Market

Type of aid	Characteristics
Horizontal	General aid which is likely to benefit all sectors of the economy, supporting all enterprises meeting specific criteria. It aims at: stimulating research and development (R&D), raising employment, enhancing qualifications via vocational training, supporting small and medium-sized enterprises (SMEs), bolstering venture capital, protecting the natural environment, etc. It is most commonly justified by the need to eliminate market failures. Aid for horizontal objectives is generally treated by the Commission as distorting competition to a smaller extent. It does not affect competition between enterprises negatively since all entities meeting specific conditions are recipients of the aid. Moreover, this type of aid generates beneficial external effects (including the effect of knowledge spillover), which can increase a country's and EU's long-term competitiveness.

683 The following types of aid have been acknowledged as compatible with the Internal Market and allowed by the Treaty: a) social, b) aiming at the removal of the effects of natural disasters and other exceptional occurrences and c) for certain areas of the Federal Republic of Germany, affected by the division of the country.

684 The following types of aid can be acknowledged as compatible with the Internal Market: a) facilitating economic development of areas where living standards continues to be abnormally low or areas with a high unemployment level, b) supporting the implementation of important undertakings in the common European interest or aiming at managing serious disturbance in the economy of a Member State, c) facilitating the development of certain economic activities or certain economic areas, d) promoting culture and heritage. Moreover, the European Council has been authorised to acknowledge other types of aid as compatible with the Internal Market.

685 For more on this topic, see M. Kąkol, *Pomoc*, op. cit., p. 128 et seq.

Regional	Aid for supporting economic development and enhancing economic cohesion of regions, granted on the basis of Article 107(3)(a)(c) TFEU (previously Article 87(3)(a)(c) of the EC Treaty). It attracts investors to the less-developed regions or those characterized by temporary economic problems, as well as to the economic zones which were specially established by (mostly new) Member States. It is often accompanied by additional support in the form of structural funds, by means of which the EU co-finances schemes implemented by Member States. Regional aid aims at providing: 1) redistribution of productive potential and even infrastructure development between different areas (regions) of the economy; 2) equal living conditions across the regions. Using financial incentives to encourage enterprises operating in prospective industries to relocate to structurally backward regions characterized by high unemployment, is supposed to increase the labour demand and lead to other side effects, such as economies of agglomeration. There is a risk, though, of a decline in overall economic efficiency on the national scale as a result of the competition between regions willing to attract investors and a lower productivity level in the less-developed regions.
Sectoral	Direct financial support for specific sectors or industries, granted on the basis of Article 107(3) TFEU (previously Article 87(3) of the EC Treaty), or on the basis of other specific provisions of the Treaty, regulating particular areas of the economy. It could be divided into 3 categories: 1) aid granted on the basis of specific sectoral regulations – for agriculture, fisheries and transport (it needs to be stressed, though, that the process leading to covering the transport sector with general provisions concerning state aid has already begun); 2) aid to the so-called sensitive industries exposed to serious problems due to structural changes in the economy, including the coal, steel, synthetic fibres and shipbuilding industries; 3) aid to sectors and industries exposed to particularly strong market competition (especially if they had not experienced it before), such as financial services, air and martime transport and the automotive industry. The principal objective of sectoral aid is a one-off adjustment of a given area of the economy to exogenous structural changes influencing the functioning of the market. This type of aid has a high potential to distort competition in the common market, due to its selective nature.
To rescue and restructure enterprises (R&R)	Direct support for enterprises in financial difficulties caused by systemic changes or the lack of capacity to face domestic or international competition. An enterprise in financial difficulties is defined as one being unable, without government intervention, to stem losses that will almost certainly force it to exit the market in a short or medium term. Aid for restructuring is granted only once and on condition that a restructuring plan is developed, as it has a great potential to distort competition. However, this is rescue aid for enterprises which constitutes the most serious threat to competition. It consists in providing support for a period of time that is necessary to prepare a restructuring plan or liquidate the business. The purpose of such aid is often to maintain employment, appropriate incomes for employees or prices of certain products. R&R aid often causes significant side effects, mostly in the form of: 1) incorrect pricing signals in product markets, which contributes to distortion of competition and benefits the subsidized enterprise; 2) incorrect signals concerning the income level, which encourages workers to remain in an industry with no perspectives of future development. Such aid delays or eliminates necessary adjustment processes, the result of which is an even greater decline in economic efficiency.

Source: Prepared on the basis of: J. Gual, S. Jódar-Rosell, Vertical industrial policy in the EU: An empirical analysis of the effectiveness of state aid, "la Caixa" economic papers, No. 1, June 2006, p. 7-8; I. Hashi, D. Hajducovic, E. Luci, Can Government, op. cit., s. 8-9; Monopolkommission, "The More Economic Approach" in European State Aid Control, Bonn, November 2008, p. 10 and 31.

State aid's potentially strong impact on competition and market structure has resulted in the EU striving to limit the overall level of aid granted by Member States and to redirect it towards horizontal objectives.[686] The results are quite significant. The total aid (excluding railways) in EU-15 declined from 85.7 billion euros in 1992 to 57.7 billion euros in 2007, and in relation to GDP, from 1.14 percent to 0.51 percent.[687] In 2007 it amounted to 64.8 billion euros in EU-27, which constituted 0.53 percent of GDP.[688] More aid was also granted to meeting horizontal objectives: its share in total aid increased from 68 percent (annual average) in 2002-2004, to 81 percent in 2005-2007.[689] It needs to be emphasized, though, that the bulk of aid formally allocated to horizontal objectives is in fact awarded to particular economy sectors (or industries), and it is hard to estimate its real destination and impact on competition.[690]

The state aid policy reform which took place in the EU in 2005-2009 was also supposed to introduce a more economic approach in assessing aid measures and to base this assessment on economic outcomes, particularly changes in economic efficiency. C. Kaupa[691] is of the opinion that the main result of the reform is the Commission abusing the efficiency criterion and social welfare standard, applying them in each case, also with respect to measures whose main objective is income redistribution and provision of social equity. In his view, the changes introduced by the Commission shift the state aid policy towards the neoclassical approach, with economic efficiency being the most important criterion, and are thus at variance with the primary law, which promotes an approach based on market structure and provides for the possibility to grant aid for non-economic reasons. The EC Treaty (now TFEU) does not treat increased efficiency as a necessary outcome of applying state aid measure. It simply requires that aid does not distort competition and intra-EU trade. The current economic and financial crisis put the Commission in an awkward position, when it agreed that Member States grant considerable aid to financial institutions, contrary to the rules proclaimed.[692]

686 Fundamental changes in state aid policy have taken place since the adoption of the Lisbon Strategy (March 2000) and are aimed at enhancing EU competitiveness on international markets.

687 European Commission, DG Competition, State Aid control, Studies and reports, Scoreboard - Data on State aid expenditure, Total State aid by Member State in million Euro, Total State aid by Member State as a percentage of GDP (1992 – 2007), http://ec.europa.eu/competition/state_aid/studies_reports/expenditure.html, 27.09.2009.

688 Ibid.

689 European Commission, DG Competition, State Aid control, Studies and reports, Scoreboard - Data on State aid expenditure, State aid to horizontal objectives as percentage of total aid (1992-2007), http://ec.europa.eu/competition/state_aid/studies_reports/expenditure.html, 27.09.2009.

690 For more, see J. Gual, S. Jódar-Rosell, *Vertical*, op. cit., p. 16-17.

691 C. Kaupa, *The More*, op. cit., p. 311, 313 and 318-319.

692 For more, see Ibid., p. 319-322. Between 2002 and 2007 the EU-27 states allocated the total of 26 billion euros to rescuing

4. STATE AID EFFICIENCY ASSESSMENT IN THE EU AND SELECTED COUNTRIES

4.1 EFFICIENCY ASSESSMENT OF CERTAIN TYPES OF AID

Studies assessing economic efficiency of state aid usually concern specific types of aid, particular sectors or industries, and sometimes the impact of total aid on the economy. Part of them is limited to domestic markets, other try to assess the influence of state aid on the competition in the Internal Market and the efficiency of the EU economy.

The so-called vertical aid, targeted at rescuing and restructuring enterprises and awarded to selected sectors or industries, is considered the most damaging.

R. Chindooroy, P. Muller and G. Notaro[693] examined the efficiency of rescue and restructuring aid approved by the European Commission in 1995-2003, assuming the survival of enterprises as the main efficiency criterion. From 86 enterpises covered by the study, 34 received rescue aid and 52 restructuring aid. The rescue aid was granted to companies suffering from liquidity and solvency problems, whereas the restructuring aid was awarded to economic entities with heavy financial burdens (e.g. accumulated debts). The results of the study were the following:

- approximately 50 percent of beneficiaries of rescue aid did not survive, while in the case of restructuring aid the bankruptcy rate was 20 percent.[694] Most frequently, the fall of companies that received rescue aid took place within three years of the start of the aid, while those that obtained restructuring aid folded businesses within three to six years;[695] chances of survival increased by 30 percent if an enterprise had problems due to market decline and/or poor management.[696] High demand growth in the industry also improved the probability of survival;

and restructuring enterprises, and 55% of this aid (14.3 billion euros) was awarded to financial services sector. European Commission, DG Competition, State Aid control, Studies and reports, Scoreboard - Data on State aid expenditure, Rescue and restructuring aid, by Member State in million Euro (2002-2007) (of which R&R aid to the financial sector), http://ec.europa.eu/competition/state_aid/studies_reports/expenditure.html, 28.08.2009. For more on aid to financial sector in the time of crisis, see R. Luja, *State Aid and the Financial Crisis: Overview of the Crisis Framework*, „European State Aid Law Quarterly", No. 2, 2009.

693 R. Chindooroy, P. Muller, G. Notaro, *Company survival following rescue and restructuring State aid*, „European Journal of Law and Economics", Vol. 24, 2007, p. 165-186.

694 Ibid., p. 176.

695 Ibid., p. 179.

696 Ibid., p. 183-184.

- keeping afloat on the market depended on the individual characteristics of the aid-receiving company and of the industry where it operated, while the features of the restructuring plan (e.g. capacity reductions, cost cutting, fiscal consolidation, undertaking new investments, sale or closure of plants or assets etc.) had no impact on the survival of enterprises;[697]

- aid for rescue and restructuring was efficient as regards sales and employment growth in approximately half of the cases, whereas in ¾ of the enterprises it contributed to improved profitability and labour productivity;[698]

- the biggest number of beneficiaries received aid in: Germany (26), Italy (16), France (12) and Spain (10).[699] All French companies survived, compared to ¾ of the German and only around half of Spanish and Italian ones.[700] Studies on sectoral aid concern particular sectors or industries of the economy, or focus on the total aid granted to the manufacturing industry.

The Danish Competition Authority analysed the performance of the shipbuilding industry in Denmark, which received practically the entire domestic sectoral aid in 1995-2005. It turned out that turnover, employment and the number of shipyards all declined with the increase in subsidies. Danish shipbuilding was characterized by a lower productivity growth than other manufacturing industries, the wages of shipyard workers were by 8-20 percent higher than those in the metal and iron industries, while profits remained low.[701]

In turn, F. Bergström[702] examined the impact that subsidies awarded to the manufacturing industry in Sweden exerted on the total factor productivity and its growth. He compared the results of 78 enterprises receiving state aid between 1989 and 1993 with the results of 884 businesses deprived of financial support. He concentrated his analysis on regional aid, that is aid earmarked for enterprises in the less-developed regions and available to them upon application. It was assumed

697 Ibid., p. 184.

698 Ex-post Evaluation of the Impact of Rescue and Restructuring Aid on the International Competitiveness of the Sector(s) Affected by Such Aid, Final Report to the European Commission – Enterprise Directorate General by London Economics, June 2004, p. 105-106.

699 R. Chindooroy, P. Muller, G. Notaro, *Company*, op. cit., p. 185.

700 Ibid., p. 176.

701 Danish Competition Authority, "Danish Competition Review 2002", Chapter 9. Cited after J. Gual, S. Jódar-Rosell, Vertical, op. cit., p. 12-13.

702 For more, see F. Bergström, *Capital Subsidies and the Performance of Firms*, „Small Business Economics" Vol. 14, 2000, p. 183-193.

that the obtained aid would be used primarily for investments in machinery and buildings. In the short term, the productivity of the subsidized firms grew faster than the one of those that did not receive aid, however, after three years the relative productivity of aid beneficiaries was lower than the productivity of the non-susidized companies. In the opinion of F. Bergström, such outcomes may indicate a side effect of state aid (in this case a substitution effect), which led to increased allocative inefficiency or the so-called technical X-inefficiency[703], as a result of rent-seeking activities.

Unlike vertical aid, horizontal aid is commonly considered as less harmful to competition and having potential to enhance economic efficiency. One of its objectives, raising relatively least doubts, is supporting research and development activity as well as innovation. For many years now, innovation has been recognised as a vital factor of economic growth and, in practice, subsidies for R&D constitute the most important instrument of innovation policy. Due to external effects, e.g. knowledge spillover, enterprises investing in R&D cannot capitalize on all the profits they generate for the benefit of the society or other enterprises, hence, the need to co-finance such projects with state resources.

In the opinion of O. Toivanen, subsidies for R&D have, nevertheless, certain weaknesses, which impede their efficient use:[704]

- they require active decision making from the agency administering them (unlike tax reliefs that may also be used to increase R&D investments), which is contrary to their alleged horizontal nature;

- decision making is accompanied with uncertainty concerning both inputs and the output of R&D;

- they are highly heterogeneous, which means that a policy aiming to achieve the Pareto-like economic efficiency must vary not only across different enterprises, but also within the same enterprise, depending on the R&D project undertaken. This means that the policy should be homogenous ex ante (equal

703 If the lack of competition in a given industry results in the production decline and its inefficiency, then there appear losses in the form of decreased welfare. This problem of unused capacity and production inefficiency due to the lack of competition is described as the so-called X-inefficiency. For more, see H. Leibenstein, *Allocative Efficiency as X-Efficiency*, „American Economic Review", Vol. 56, No. 3, June 1966, p. 392-415.

704 O. Toivanen, *Innovation and research policies: two case studies of R&D subsidies*, „EIB Papers", Vol. 11, No. 2, 2006, p. 55-61.

conditions for receiving subsidies for all) and heterogenous ex post (the actual volume of subsidies will vary considerably depending on the type of project and innovation);

- they can have impact on private R&D investment (foster own investments of enterprises), but there is also a risk of crowding out;
- they may influence other enterprises (via spillovers) and their behaviour.

Due to the aforementioned reasons it is hard to design an optimal policy of stimulating innovation by means of subsidies.

Studies on the efficiency of R&D subsidies granted in Finland and Norway in the 1980s and 1990s deliver interesting observations. These two countries are comparable in terms of wealth, economic structure, high taxes, well-educated and well-paid workforce. They support higher education institutions as part of regional policy and are actively involved in R&D activities and their planning. In both countries R&D projects are dominated by a few large enterprises – e.g. in Finland top ten enterprises with biggest R&D investments spend approximately 2/3 of all private expenditures on R&D, while in Norway the figure is over 70 percent.[705] For more on the innovation policy and innovation support systems in both countries, see Table 2.

705 Ibid., p. 63.

Table 2. Characterisation of innovation support policy in Finland and Norway

Finland
Finland has got an innovation support system consisting of many institutions, including special agencies employed by the government. Different institutions get involved on different stages of the innovation process and use various instruments: grants, loans, capital injections or business consulting services. Financing for R&D covers basic research, for which approximately half of the funds is allocated, applied research, product and process development, and product and process commercialisation. One of the sources of subsidies for R&D in Finland is the National Technology Agency of Finland – Tekes, which grants around 400 million euros in subsidies annually. Finland has also a large number of qualified engineers and scientists, which is the key factor for innovation activities The analysis of Tekes' decisions concerning subsidies shows that they are rarely influenced by the enterprise's characteristics, apart from its size. This is important, since large enterprises receive larger subsidies for similar R&D projects (percent of R&D expenditures) than small firms. The profitability of R&D expenditures is higher, all other things being equal, in companies with a higher added value of production and those whose executive director is not the chairman of the board at the same time. Due to the fact that other characteristics of the enterprise do not have effect on the profitability of R&D, they are not taken into account, although profitability varies across industries and regions (e.g. it is higher is the telecommunications industry than in the food industry, and higher in the southern regions than in the eastern ones). There is, however, no evidence of Tekes treating enterprises in different industries in a different way. Instead, it makes its decisions horizontally. The subsidy depends primarily on the project's characteristics – if it constitutes a considerable technological challenge, the subsidy is increased; if it involves a higher commercial risk, then the subsidy is lowered. Small enterprises receive subsidies around 8 percent higher (up to 60 percent of a project's costs), although their absolute value is much greater in larger enterprises (especially the ones with high employment), due to stronger R&D spillover effects. Studies indicate that the costs of applying for a subsidy (the manager's working time, which he or she could have devoted to R&D activity) significantly influence enterprises' behaviour and their decision to apply for subsidy, therefore, they needs to be taken into account. These costs rise with the quality of R&D projects. Between 2000 and 2003, out of the 11 thousand firms (potential applicants), only around 1 thousand applied for subsidies. 30 percent of those applications were later turned down.
Norway
Innovation support policy in Norway is characterized by large state involvement in the development of general-purpose technologies, i.e. breakthrough technologies which create new possibilities. The state finances around 40 percent of this kind of research carried out by universities and government laboratories. In order for the projects to bring about positive outcomes, they initially require very big investments. R&D subsidies granted in the 1980s and 1990s were highly concentrated. They were absorbed by the IT industry and by large enterprises forming part of it, including Norsk Data (around 12 percent of all funds available to firms).

Source: Prepared on the basis of O. Toivanen, Innovation, op. cit., p. 65-72; T. Takalo, T. Tanayama and O. Toivanen, Selection or self-rejection? Applications into a treatment program: The case of R&D subsidies, „HECER Discussion Paper", No. 76, 2005 and T.J. Klette and J. Møen, From growth theory to technology policy – coordination problems in theory and practice, „Nordic Journal of Political Economy", Vol. 25, 1999, p. 53 et seq.

Despite visible similarities between both of these economies, Finland is an example of efficient innovation policy and R&D subsidizing, while in Norway the outcomes have been unsatisfactory. Studies regarding Finland indicate that R&D subsidies have had a positive impact on the economy:

- they spurred private investments in R&D a year after they had been granted;[706]
- they enhanced the enterprises' productivity (especially of SMEs), including total factor productivity (TFP);[707]
- they fostered increased employment in R&D activity (with a one-year delay), although they remained without impact on the general employment level in enterprises;[708]
- the social R&D subsidy rate of return amounted to approximately 9 percent[709] and was higher than the interest rates on the Finnish government bonds.

Studies concerning Norway revealed that subsidies for R&D had not produced efficient results. Either they were granted to enterprises with low profitability and productivity, or even worse – they led to sub-par performance. In the short run, they had a negative impact on sales, profits, labour productivity, total factor productivity; and in the long run, they contributed to a decline in R&D intensity and profits of the beneficiaries. Spinn-off firms that spun off from subsidised enterprises also generated lower profits than other companies.[710] The only positive finding, unveiled by some of the studies, was that enterprises invested much more in R&D after the subsidy period than it would have been if they had not received support.[711]

O. Toivanen tried to address the question why the outcomes of state aid to R&D in both countries had been so different. He indicated the following reasons:[712]

- there were considerable differences as regards administering the subsidies between both countries. Norway concentrated its aid, and supported national

706 J. Ali-Yrkkö and M. Pajarinen, *Public R&D financing and its impact on companies: An analysis of metal and electronics firms*, „The Research Institute of the Finnish Economy Discussion Paper", No. 846, 2003. Cited after O. Toivanen, Innovation, op. cit., p. 68.

707 H. Piekkola, *Public funding of R&D and growth: Firm-level evidence from Finland*, „Economics of Innovation and New Technology", Vol. 16, Issue 3, April 2007, p. 196, 207-208.

708 For more, see J. Ali-Yrkkö, Impact of public R&D financing on employment, „The Research Institute of the Finnish Economy Discussion Paper", No. 980, 2005, p. 7-10 and 14.

709 T. Takalo, T. Tanayama and O. Toivanen, *Selection*, op. cit., p. 2 and 35.

710 For more, see T.J. Klette and J. Møen, *From growth*, op. cit, p. 59-68.

711 T.J. Klette and J. Møen, *R&D investment responses to R&D subsidies: A theoretical analysis and a microeconometric study*, University of Oslo, Norway 1998, mimeo. Cited after O. Toivanen, Innovation, op. cit., p. 73.

712 O. Toivanen, *Innovation*, op. cit., p. 75.

champions and enterprises operating in the same, or related, sectors as the leading companies. Finland applied a more horizontal policy. Targeting may be efficient, but it is up to the government to select the right aim;

- Norwegian IT industry (especially Norsk Data) focused upon minicomputers and could not be saved by innovations, since, as a result of IT development, it had been left behind and replaced by a completely new technology.[713] This industry would have failed anyway with or without subsidies;

- Norway followed the "winner takes it all" rule, relied on supporting innovation (hoping for profits) in one field and, as it often happens, it turned out it had financed the wrong technology.

Concluding the overview of studies concerning the efficiency of various types of aid, it is worth to mention the research by L.-H. Röller, H.W. Friederiszick and D. Neven, who analysed state aid in EU-15. They calculated that an increase in annual state expenditures by 1 euro *per capita* brings about the following outcomes:

- in the case of R&D aid – an increase in private R&D expenditures *per capita* by nearly 2 euros in five consecutive years;[714]

- in the case of aid for SMEs – a 1.2 percent increase in their turnover share in five consecutive years by;[715]

- in the case of regional aid – lowering by 0.72 percent the coefficient of variation of the value added generated in these regions in five consecutive years, although aid for the poorest regions (granted on the basis of Article 107(3)(a) TFEU, previously Article 87(3)(a) of the EC Treaty) does not influence convergence.[716]

Studies on various types of state aid confirm that its efficiency lowers while its amount increases. Moreover, various aid schemes may mutually complement

713 Norsk Data was a Norwegian company seated in Oslo, active between 1967 and 1992, which produced minicomputers and software. It was known for many breakthrough technological solutions, especially in the 1970s and early 1980s (e.g. the first 32-bit minicomputer). Problems of this uniquely innovative company began in the early 1990s, with the development of cheaper open standard personal computers IBM-PC, working in the MS-DOS operating system, as well as due to increased competition from the producers of workstations based on UNIX system.

714 L.H. Röller, H.W. Friederiszick, D. Neven, *Final Report: Evaluation of the Effectiveness of State Aid as a Policy Instrument*, OJ S 144-28/7/2001-144/098945, 2001, p. 57.

715 Ibid., p. 89.

716 In the case of poorest regions, the aid from EU funds has greater impact than state aid. Ibid., p. 111.

each other and e.g. funds for SMEs may also lead to a rise in R&D. The same amount of aid may not be equally effective across particular Member States – at least due to different aid granting systems.[717]

4.2 ASSESSMENT OF THE IMPACT OF STATE AID ON SELECTED ECONOMIES

Studies aiming at identifying the impact of aid granted by certain states on competitiveness and economic efficiency also provide interesting conclusions. J. Hashi, D. Hajducovic and E. Luci[718] conducted an econometric research concerning the influence of governmental policy, including the use of subsidies, on industrial competitiveness in Poland (1996-2003) and the Czech Republic (1997-2003). The research covered around 90 industries treated as a whole. It turned out, that subsidies in the Czech Republic had not contributed to changes in competitiveness, either in the domestic market, or in the EU market. In Poland, they had generated no impact on the competitiveness on the EU market, but they had caused a decline in competitiveness on the domestic market. Such results seriously undermine the legitimacy of granting state aid, at least from the economic perspective.

A comprehensive study of state aid, assessed from the point of view of its economic efficiency, was conducted in Slovenia as part of the programme "Competitiveness of Slovenia 2006-2013". Studies covering the aid granted between 1998 and 2006 indicated that the support for SMEs, R&D and employment growth had been most efficient. Vocational training aid and regional aid had been far less efficient, whereas funds allocated for rescuing and restructuring enterprises and to particular sectors of the economy had been inefficient (see Table 3).

717 Cf. R. Nitsche, P. Heidheus, *Study on methods to analyse the impact of State aid on competition*, „European Economy. Economic Papers" No 244, European Commission, February 2006, p. 66.

718 For more, see I. Hashi, D. Hajducovic and E. Luci, *Can Government*, op. cit.

Table 3. Efficiency of state aid granted by Slovenia in 1998-2006 according to types of aid

Aid for SMEs	The most efficient, since it helped increase the employment level, sales and productivity of beneficiaries. Aid awarded to technology-intensive sectors and industries proved most efficient, similarly to aid granted to enterprises with a relatively high level of sales per employee or those employing only a couple of workers.
Aid for R&D	It had a positive, albeit short-term, impact on the availability of funds for R&D. Unlike their competitors who were not granted aid, its beneficiaries increased their investments in R&D. The additionality effect on research expenditure was higher among large enterprises (in terms of total sales), whereas small firms would have probably implemented their R&D projects without aid as well (substitution effect). Continuous, repeated receipts of aid negatively influenced the companies' own investments in R&D.
Employment growth aid	It was efficient during the first three years after the subsidy was given, but the efficiency considerably declined with each new subsidy granted to the same enterprise. On average, the aid was more efficient in enterprises of larger sales volume.
Training aid	It caused a modest rise in wages in beneficiaries (by 8-16 percent of average gross salary between 2003 and 2006). There is no evidence, though, that it contributed to increased labour productivity. The probable reasons for this were very small amounts of aid and inadequate programmes it was allocated to.
Regional aid	It had a positive effect on sales, employment and added value per employee, but only in the first two years after the subsidy was received. It could have probably had a more positive impact on efficiency, but the funds had been improperly distributed among beneficiaries. This type of aid was more efficient in advanced technology sectors and its efficiency declined with each consecutive portion of aid.
Rescue and restructuring aid and sectoral aid (for mining, energy and transport)	The aid was inefficient in boosting sales, creating new jobs and enhancing productivity. Considering that the beneficiaries operated in sectors which are greatly exposed to international competition, it cannot be expected that state aid could save them from decline.

Source: Prepared on the basis of Slovenian Institute of Macroeconomic Analysis and Development, "Economic Issues 2008", *August 2008, p. 41-42*

Most of all, the structure of state aid allocated to particular beneficiaries raises concerns. It was oriented at rescuing bad enterprises, and the majority of funds for the manufacturing was awarded to businesses operating in low and medium-low technology industries.[719] Consequently, subsidies did not help to facilitate the necessary structural changes in the economy and enhance its competitiveness. Although in 2006 the share of horizontal aid in Slovenia amounted to 88 percent,[720] these data do not take into account the aid allocated to the railway sector

719 In accordance with a widely accepted OECD classification. This organization distinguishes four industry groups according to technological advancement level: high, medium-high, medium-low and low technologies. See more OECD Handbook on Economic Globalisation Indicators, Paris 2005, p. 172.

720 European Commission, DG Competition, State Aid control, Studies and reports, Scoreboard - Data on State aid expenditure, State aid to horizontal objectives as percentage of total aid (1992-2007), http://ec.europa.eu/competition/state_aid/studies_reports/expenditure.html, 29.09.2009.

(186 million euros)[721]. Total state aid (excluding railway transport) amounted to 234 million euros.[722]

The authors of the "Economic Issues 2008" report emphasized that state aid in Slovenia constitutes a potential threat to competition, mostly due to its high level of concentration. In 2006, as part of different types of aid, the top 10 percent of all beneficiaries received:[723]

- 43% of the total aid allocated to vocational training,
- 46% of the aid for energy saving,
- 50% of the aid for employment,
- 62% of R&D aid,
- 69% of the aid for the protection of the natural environment,
- 76% of the regional aid,
- 84% of the aid for SMEs,
- 95% of the aid for agriculture.

Some entities received aid from more than one source, whereas the highest subsidies were granted to large enterprises, which could potentially influence competition in the industry. On the other hand, more than a half of the beneficiaries received too little financial support to change their behavior, which is instrumental for the aid to be effective. Summing up, expenditures and costs incurred by Slovenia as a result of granting state aid were higher than the benefits generated.[724]

721 European Commission, DG Competition, State Aid control, Studies and reports, Scoreboard - Data on State aid expenditure, Subsidies for the railway sector, EU-27 (2000-2007), http://ec.europa.eu/competition/state_aid/studies_reports/expenditure.html, 29.09.2009.

722 European Commission, DG Competition, State Aid control, Studies and reports, Scoreboard - Data on State aid expenditure, Total State aid by Member State in million Euro, http://ec.europa.eu/competition/state_aid/studies_reports/expenditure.html, 29.09.2009.

723 Slovenian Institute of Macroeconomic Analysis and Development, "Economic", op. cit., p. 43.

724 Ibid.

5. CONCLUSION

Summing up the considerations concerning economic efficiency of state aid, it needs to be stressed that this policy instrument should be used very carefully. As confirmed by the studies presented above, state aid has a great potential to correct market failures and enhance efficiency. Still, if used improperly, it can significantly distort competition and contribute to decreased social welfare, instead of fostering its growth. From the economic point of view, granting rescue and restructuring aid and sectoral aid is the least legitimate. Nevertheless, some studies indicate that such measures, if properly allocated, can contribute to higher productivity in the manufacturing industry.[725] Therefore, each state aid scheme should be assessed individually. Horizontal aid is generally considered as efficient, but, as proved by the Norwegian (R&D aid) and Slovenian (training aid) experiences, there is no guarantee it will generate intended outcomes. This leads to the conclusion that efficiency of the overall state aid policy is equally important as a particular state aid measure's potential to correct market failures.

T. Giebe, T. Grebe and E. Wolfstetter[726] formulated recommendations on how to allocate R&D subsidies so as to make them as efficient as possible. Their hints are also valid in the case of other types of state aid. They assessed the rules of awarding subsidies for R&D in Germany[727] and concluded that they are inefficient for two reasons:[728] selection based on a ranking of individual projects and the lack of competition between entities applying for funds. A group of scientists from the Humboldt University of Berlin characterized the current R&D aid granting system indicating that the financial resources are allocated in the following manner in the majority of schemes:[729] 1) applicants submit written project proposals to the programme manager in a given time, 2) they are assessed by experts as regards their scientific and economic merits, 3) based on this assessment a special committee grades particular projects (e.g. A, B and C) and selects them for the programme (from A to C) until the funds available are exhausted, 4) each selected project is awarded a subsidy amounting to a pre-defined proportion of eligible costs. Experts stated that granting support to the best projects, one

725 In this case studies showed a modest increase in multi-factor productivity. For more, see J. Gual, S. Jódar-Rosell, *Vertical*, op. cit., p. 17 et seq.

726 T. Giebe, T. Grebe and E. Wolfstetter, *How to allocate R&D (and other) subsidies: An experimentally tested policy recommendation*, „Research Policy", Vol. 35, 2006, p. 1261-1272.

727 Similar rules are also used in many other countries, such as Great Britain or US.

728 T. Giebe, T. Grebe and E. Wolfstetter, *How to allocate*, op. cit., p. 1261.

729 Ibid., p. 1261-1262.

by one, until the funds are exhausted, is not a good policy. Instead they proposed that the administrators:[730]

- choose projects based on a ranking of all potential allocations possible under the budget at disposal. The current system does not take into account that financing a high-ranking project can eliminate the implementation of a number of smaller ones, which individually may be ranked lower than the large one, but in sum total, they could lead to a better allocation of funds;

- encourage the applicants to disclose their real financial needs and use this information. The best way would be to introduce tendering procedures (open or closed), that is mechanisms making it possible for the applicants to compete for funds by means of submitting bids. This would lead to the economization of each subsidy's size.

The new selection system would not favour large projects (associated with high quality and high cost) and would allow the implementation of smaller ones, which could indeed compete with the larger ones. From the point of view of benefits for the entire economy or specific sectors or industries, subsidising a few smaller undertakings is sometimes better than financing one big player. The manner of distributing funds would depend on preferences defined in economic policy. However, they should be established earlier, e.g. by the lawmakers or a specially appointed national institute for the development of economy and technology, which would be fully independent from the aid granting process and the administrating institutions.[731]

On the other hand, M. Mosselman and Y. Prince highlighted that for the efficient as well as effective state aid policy one in principal needs:[732]

- to formulate clear and detailed goals to be attained by aid measures. They ought to be measurable, take into account enterprises' outcomes and the impact of the subsidies on total welfare (e.g. profit growth by 20 percent, sales growth by 50 percent, etc). They should be set even before the state aid schemes are launched;

730 T. Giebe, T. Grebe and E. Wolfstetter, *How to allocate*, op. cit., p. 1270.

731 For more, see Ibid., p. 1271.

732 M. Mosselman, Y. Prince, *Review of methods to measure the effectiveness of state aid to SMEs. Final Report to the European Commission*, EIM Business & Policy Research, November 2004, p. 23-25.

- the efficiency assessment should take into account the causality between a particular state aid scheme and measured economic benefits, or the lack of it (deadweight factors), as well as the positive and negative side effects of subsidizing experienced both by the beneficiaries and those which were not granted aid, e.g. additionality (i.e. boosting private investment), crowding-out of private investment, knowledge spillover, etc.

In the end, it is worth emphasizing that despite the fact that aid efficiency is undoubtedly a highly significant criterion, the ultimate objective should be to assess whether a measure has contributed to increased competitiveness of the enterprises and the economy sectors or industries which received it. The competitiveness should be measured by an increase in sales capacity, reflected in the share in the domestic and international markets. If supported enterprises and domestic industries improve their position in international trade, then we can be certain that the aid was used in the best possible way from the economic point of view. This, however, does not allow to answer the question as to whether other non-economic objectives of aid, such as income redistribution, protection of the natural environment, etc., have been achieved.

Soultana Paschalidou[733]

RECOVERY OF UNLAWFUL AND INCOMPATIBLE STATE AID – AGAINST ALL ODDS?

1. INTRODUCTION AND HISTORICAL DEVELOPMENT OF THE POWER TO RECOVER

European Union (hereafter "EU") rules on the supervision of State aid[734] provide that Member States are not allowed to implement aid until it has been authorised by the European Commission (hereafter "the Commission") and the "standstill"[735] obligation has been respected. Aid which is granted by a Member State before the approval of the Commission is automatically considered as "unlawful". If it is subsequently found to be incompatible with the common market, the Commission is under an obligation to order recovery from the beneficiaries.

Although the EU rules on State aid were already laid down in the Treaty of Rome, recovery policy developed much later. This can be explained by the fact that in the early years of the European Community the economic situation was favourable and up to the mid 1970s the Commission only received on average 20 notifications per year.[736] The first time the Court of Justice of the European Union (hereafter the "Court") considered the right of the Commission to recover was in its *Kohlegesetz* judgment of 1973, where it stated that *"(…) the Commission is competent, when it has found that aid is incompatible with the Common Market, to decide that the state concerned must abolish or alter it. To be of practical effect, this abolition or modification may include an obligation to require repayment of aid granted in breach of the Treaty (…)."*[737]This judgment confirmed that the Commission had the power to order the recovery of unlawful and incompatible State aid.

However, the economic situation in Europe changed after the mid 1970s and a number of sectors faced structural difficulties. State aid increased significantly

733 The content of this article does not necessarily reflect the official position of the European Commission. Responsibility for the information and views expressed lies entirely with the author. This article was completed in October 2009. Thereafter, only editorial changes were made, to reflect the re-numbering resulting from the Treaty of Lisbon.

734 Articles 107-109 Treaty on the Functioning of the European Union (hereafter "TFEU") (ex 87-89 EC).

735 According to Article 108(3) TFEU (ex 88(3) EC) Member States are not allowed to implement aid before it has been notified to and authorised by the Commission.

736 See Adinda Sinnaeve, Die Rückforderung gemeinschaftsrechtswidriger nationaler Beihilfen, Diss. Tübingen 1996, p. 61.

737 Case 70/72, Commission v. Germany, [1973] ECR 813, para. 13.

and Member States often did not fulfil their notification obligations.[738] As a consequence, the Commission assumed a stricter approach towards the monitoring of State aid. Moreover, it adopted in 1983 a Communication where it declared that it would use all measures at its disposal to ensure that Member States' obligations under Article 108(3) of the Treaty on the Functioning of the European Union (hereafter "TFEU") (ex 88(3) EC) are fulfilled. This includes requiring individual countries to recover aid granted illegally from recipients.[739]

In the second half of the 1980s and in the 1990s, the Commission ordered the recovery of unlawful and incompatible aid more systematically, and in 1999, basic rules on recovery were incorporated into Council Regulation 659/1999 of 22 March 1999[740] ("the Procedural Regulation").

2. PURPOSE AND PRINCIPLES OF RECOVERY

According to the established jurisprudence of the Court, the purpose of recovery is to re-establish the status quo ante; the situation that existed on the market prior to the granting of the aid.[741] By repaying the State aid, the recipient forfeits the advantage that it had enjoyed over its competitors and the situation prior to payment is restored.[742] The Court has emphasized that the recovery of unlawful and incompatible aid is not a penalty against the recipient,[743] but the logical consequence of the finding that it is unlawful.[744] It can therefore not be regarded as disproportionate to the objectives of the Treaty with regards to State aid.[745]

However, in order to effectively restore the situation as it was prior to the payment of the illegal State aid, all of the financial benefits resulting from the aid

738 See Adinda Sinnaeve, cited above in fn. 736, p. 62.

739 OJ C 318, 24.11.1983, p. 3-4.

740 Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty (OJ L 83, 27.03.1999, p. 1).

741 Case C-142/87, Commission v. Belgium ("Tubemeuse"), [1990] ECR I-959, para. 66; Joined cases C-278/92, C-279/92 and C-280/92, Spain v. Commission, [1994] ECR I-4103, para. 75.

742 Case C-348/93, Commission v. Italy, [1995] ECR I-673, para. 27; Case C-350/93, Commission v. Italy, [1995] ECR I-699, para. 22.

743 Case C-75/97, Belgium v. Commission, [1999] ECR I–3671, para. 65.

744 Case C-142/87, "Tubemeuse", cited above in fn. 741, para. 66; Case C-183/91, Commission v. Greece, [1993] ECR I-3131, para. 16; Joined Cases C-328/99 and C-399/00, Italy and SIM 2 Multimedia v. Commission ("Seleco"), [2003] ECR I-4035, para. 66.

745 Case 310/85, Deufil v. Commission, [1987] ECR 901, para. 24; Joined cases C-278/92, C-279/92 and C-280/92, cited above in fn. 741, para. 75; Case C-148/04, Unicredito Italiano, [2005]ECR I-11137, para.113. Case C-419/06, Commission v. Greece, [2008] ECR p. I-27, para. 55.

which adversely affect competition in the common market have to be eliminated. The financial advantages incidental to unlawful and incompatible aid can be excluded by recovering interest on the sums illicitly granted. According to the jurisprudence of the EU Courts, illegal State aid would otherwise amount to an interest-free loan.[746] This principle has been codified by Article 14(2) of the Procedural Regulation. More detailed rules on the method to set the interest rate for recovery and calculate the total sum to be repaid are provided in Chapter V of the Implementing Regulation[747].

Article 14(3) of the Procedural Regulation specifies that *„recovery shall be effected without delay and in accordance with the procedures under the national law of the Member State concerned, provided that they allow the immediate and effective execution of the Commission's decision."* This provision codifies the principle of effectiveness, according to which the relevant provisions of national law must be applied in such a way that the recovery required by EU law is not rendered practically impossible and the interests of the EU are taken fully into consideration[748]. The Court has insisted that in order for a Commission recovery decision to be fully executed, the actions undertaken by a Member State must be immediate and effective. National procedures which prevent the immediate restoration of the previously existing situation and prolong the unfair competitive advantage resulting from unlawful and incompatible aid do not fulfill the conditions laid down in Article 14(3) of the Procedural Regulation and should therefore not be applied[749]. According to the Court, effective recovery means that the efforts made by the national authorities must result in the actual recovery of the sums owed[750]. In order to fulfill its recovery obligation it is not enough for the Member State concerned to limit itself to *„a certain number of procedural and administrative steps"*[751]. Any measure adopted in order to fulfill an obligation to recover illegal aid must be: (i) a suitable instrument for re-establishing the conditions of competition which have been distorted by the grant of that illegal aid; (ii) capable of being identified

746 Case T-459/93, Siemens v. Commission, [1995] ECR II-1675, paras. 97-101.

747 Commission Regulation (EC) No. 794/2004 of 21 Apr. 2004 implementing Council Regulation (EC) No. 659/1999 laying down detailed rules for the application of Art. 93 of the EC Treaty (the "Implementing Regulation"), OJ L 140, 30.04.2004, p. 1, as last amended by Commission Regulation (EC) No 271/2008 of 30 January 2008, OJ L 82, 25.03.2008, p. 1.

748 Case 94/87, Commission v. Germany, [1989] ECR I-175, para. 12; Case C-142/87, "Tubemeuse", cited above in fn. 741, para. 66; Case C-24/95, Alcan Deutschland, [1997] ECR I-1591, para. 24; C-209/00, Commission v. Germany, [2002] ECRI-11695, paras. 32-34.

749 Case C-232/05, Commission v. France ("Scott"), [2006] ECR I-10071, paras. 49-53.

750 Case C-415/03, Commission v. Greece ("Olympic Airways"), [2005] ECR I-3875, para. 35; Case C-369/07, Commission v. Greece, [nyr], paras. 65-73.

751 Case C-415/03, "Olympic Airways", cited above in fn. 750, para. 44.

as such by the Commission and other interested parties; (iii) unconditional; and (iv) immediately applicable[752]. The requirement to recover is, therefore, normally defined as an obligation of result[753].

3. LIMITS TO RECOVERY

The Procedural Regulation lays down two limits to the recovery of unlawful and incompatible State aid. Firstly, under Article 14(1) the Commission is obliged to order the repayment of unlawful and incompatible State aid from the beneficiary as long as a recovery obligation is not contrary to a general principle of EU law. Secondly, Article 15 provides for a limitation period of ten years. In addition, the EU Courts have recognised a third limit, namely the existence of exceptional circumstances which mean that recovery is absolutely impossible. Member States often argue that the Article 14(1) exception applies and no recovery should be imposed, allegedly because it would be in breach of general principles linked to "legitimate expectations"[754] or to "legal certainty"[755].

The EU Courts have, so far, construed the notion of legitimate expectations strictly and have therefore rejected an overwhelming majority of the claims formulated on this ground. They have consistently held that undertakings to whom aid has been granted may not, in principle, entertain a legitimate expectation that the aid is lawful unless it has been granted in compliance with the procedure laid down in Article 108 TFEU (ex 88 (3) EC). A diligent businessman should normally be able to determine whether that procedure has been followed[756]. The Court has further refused to allow a Member State whose authorities have granted aid contrary to the above-mentioned procedural rules to rely on the legitimate expectations of recipients in order to justify a failure to recover the aid. Otherwise, national authorities would be able to rely on their own unlawful conduct in order

752 Case C-209/00, Commission v. Germany ("WestLB"), [2002] ECR I-11695, para. 58.

753 Elisabetta Righini, Godot Is Here: Recovery as an Effective State Aid Remedy, EC State Aid Law/Le droit des aides d'Etat dans la CE. Liber Amicorum Francisco Santaolalla Gadea, (2008), p. 265-288, p. 271.

754 On the principle of the protection of the legitimate expectations, see Case C 5/89, Commission v. Germany, [1990] ECR I-3437, paras. 13-14; Case-C 24/95, cited above in fn. 748, para. 25. For an example where the Court recognized the existence of legitimate expectations on the side of the beneficiary, see Case C-223/85, RSV, [1987] ECR 4617.

755 On the principle of legal certainty, see Case T-115/94, Opel Austria GmbH v. Council, [1997] ECR II-39 paras. 124-133; Case C-372/97, Italy v. Commission, [2004] ECR I-3679, paras. 116-118; Joined Cases C-74/00P and C-75/00P, Falck and Acciaierie di Bolzano v. Commission [2002] ECR I-7869, para. 140. See also Case C-408/04P, Commission v. Salzgitter, [2004] ECR II-1933, para. 166.

756 Case 265/85, Van den Bergh en Jurgens v. Commission, [1987] ECR 1155, para. 44; Case C-5/89, Commission v. Germany, cited above in fn. 754, para. 14; Joined Cases T-239/04 and T-323/04, Italy and Brandt Italia v. Commission, [2007] ECR II-3265, paras. 153-154.

to deprive decisions taken by the Commission of their effectiveness[757].

Appellants also often claim that the principle of legal certainty has been breached following an undue delay in the proceedings on the part of the Commission. This delay would allegedly constitute an implicit assurance that the aid did not fall within Article 107 TFEU (ex 87 EC). However, the Court found in a recent case that a delay by the Commission in exercising its supervisory powers and ordering recovery of the aid does not render that recovery decision unlawful, apart from exceptional cases where the Commission manifestly failed to act and clearly breached its duty of diligence[758]. The standard applied by the EU Courts as regards the principle of legal certainty is therefore a very high one[759].

The second limit to recovery in the Procedural Regulation, Article 15, establishes that the powers of the Commission to recover aid shall be subject to a limitation period of ten years. Any support awarded before this span, shall be deemed to be existing aid. The limitation period begins on the day when the unlawful aid is awarded to the beneficiary, and can be interrupted by any action taken by the Commission (or by a Member State, acting at the request of the Commission), with regard to the unlawful aid. Each break will start the time running anew.

The Court has recognised one additional exception to the obligation to recover, namely the existence of exceptional circumstances that would make it absolutely impossible for the Member State to execute the decision properly[760]. The Court has interpreted the notion of “absolute impossibility” very strictly. It has in particular confirmed that the expiration of a time-limit existing under national law in the interest of legal certainty does not constitute exceptional circumstances that would make the recovery impossible[761]. Member States can also not plead other requirements of national law[762] or the absence of a recovery title under their regimes[763] in order to justify their failure to comply with a recovery decision.

757 Case C-5/89, Commission v. Germany, cited above in fn. 754, para. 17.

758 See Case C-408/04P, Salzgitter, cited above in fn. 755, para. 106, where the aid was granted under the ECSC Treaty.

759 See in this regard also Joined Cases T-30/01 to T-32/01 and T86/02 to T-88/02, Diputación Foral de Álava v. Commission, [nyr], paras. 258-274.

760 Case C-348/93, Commission v. Italy, cited above in fn. 742, para. 16; Case C-261/99, Commission v. France, [2001] ECR I-2537, para. 23; Case C-499/99, “Magefesa”, [2002] ECR I-6031, para. 21; Case C-404/00, Commission v. Spain, [2003] ECR I-6695, para. 45.

761 Case C 24/95, Alcan Deutschland, cited above in fn. 748, paras. 27-38.

762 Case C-52/84, Commission v. Belgium, [1986] ECR-89, para. 9.

763 Case C-303/88, Italy v. Commission, [1991] ECR 1-1433, paras. 58-60.

This also applies to arguments brought forward based on factual difficulties, e.g. financial difficulties of the beneficiary. The Court has held that since the Commission's objective is to abolish the competitive advantage provided by the aid, that aim can also be achieved through the liquidation of the company[764]. When this occurs, a Member State may claim absolute impossibility only if it shows that there are no recoverable assets available[765].

4. RECOVERY AND INSOLVENCY

For a company in financial difficulties, repaying the illegal aid may have serious consequences. The financial situation of the company and the possible risk of insolvency cannot, however, be invoked to escape the recovery obligation. The fact that a company is insolvent and/or subject to bankruptcy proceedings has no effect on the requirement to repay the aid. The Court has stated that, since the ultimate goal of recovery is to end the distortion of competition, liquidation of the beneficiary can be regarded as an acceptable alternative in cases where it will not be possible to recover the full amount of unlawful and incompatible aid[766]. Liquidation will prevent a future distortion of competition by the original aid beneficiary. It will also free the market segment previously held by the firm and make it available to creditors, while giving them the opportunity to acquire the assets and reallocate them more effectively[767]. Nevertheless, it is important to stress that even if the liquidation of a company is an acceptable alternative to full repayment, the Member State is still under the obligation to enforce its recovery claim. Removing the obligation to repay in the event of a company's liquidation would render the rules on State aid meaningless[768].

If the beneficiary of the aid is subject to insolvency proceedings, the first obligation of the Member State, as creditor of the incompatible illegal aid, is to register its claim in the bankruptcy proceedings[769]. Recovery will then proceed according

764 Case C-52/84, Commission v. Belgium, cited above in fn. 762, para. 14.

765 Case C-499/99, "Magefesa", cited above in fn. 760, para. 39.

766 Case C-52/84, Commission v. Belgium, cited above in fn. 762, para. 14.

767 Commission Decision 2000/536/EC of 2 June 1999 concerning State aid granted to Seleco SpA (OJ L 227, 07.09.2000, p. 24, para. 113) as confirmed by Joined Cases C-328/99 and C-399/00, "Seleco", cited above in fn. 744, para. 69.

768 Commission Decision 93/133/EEC of 4 November 1992 concerning aid granted by the Spanish government to the Merco company (OJ L 055, 06.03.1993, p. 54) as confirmed by Case C-42/93, Spain v. Commission ("Merco"), [1994] ECR I-4175.

769 Case C-52/84, Commission v. Belgium, cited above in fn. 762, para. 14; Case C-142/87, "Tubemeuse", cited above in fn. 741, para. 62; Case C-277/00, Germany v. Commission ("SMI"), [2004] ECR I-3925, para. 85; Case C-214/07, Commission v. France, [nyr], para. 56.

to national bankruptcy rules[770] and the recovery debt will be refunded by virtue of the status given to it by the country's legal regime. The relevant provisions of national legislation must, however, be applied in such a way that the recovery required by EU law is not rendered practically impossible and the interests of the EU are taken fully into consideration[771].

Yet, in the application of national insolvency rules, several problems may arise in relation to the registration of the recovery claims. There are cases where the insolvency administrator refuses to register part or the totality of the Member State's claims, or gives the claims a ranking which deprives the Member State of any right in the proceedings and of any prospect of recovery. In these situations, the Member State is expected to oppose any refusal by the insolvency administrator to register the recovery claim or any ranking depriving it of rights in the proceedings on the ground that such a decision would go against the "effet utile" of the Commission decision[772].

National procedures may furthermore allow for a continuation of the activities of the company in financial distress. It is clear that, from a competition point of view, insolvency proceedings that do not result in the immediate reimbursement of the aid or the immediate ending of the activity of the beneficiary, should be regarded as problematic. They do not result in the instantaneous discontinuation of the distortion of competition. The Court has stated that the possibility of a company in difficulties taking measures to rehabilitate the business cannot be ruled out a priori because of requirements relating to recovery of the aid which is incompatible with the common market[773]. It appears, nevertheless, reasonable and necessary to impose a limit on the period of time during which the administrator can allow an insolvent company to continue its activities in the absence of a full reimbursement of the unlawful and incompatible aid.

770 Case C-142/87, "Tubemeuse", cited above in fn. 741, para. 62.

771 Case C 24/95, Alcan Deutschland, cited above in fn. 748, para. 42.

772 Judgment of the Commercial Chamber of the Amberg Court of 23 July 2001 in relation to the aid granted by Germany to Neue Maxhütte- Stahlwerke GmbH (Commission Decision of 18 October 1995, OJ L 53, 2.3.1996, p. 41). In that case, the German court overruled the refusal of the insolvency administrator to register a recovery claim resulting from an illegal and incompatible aid granted in the form of a capital injection, as this would render the execution of the recovery decision impossible. See also the judgment of the Bundesgerichtshof in SKL Motoren- und Systembautechnik GmbH (decision of 9 April 2002, OJ L 314, 18.11.2002, p. 75). In this case the Bundesgerichtshof found that the recovery claim regarding the aid granted in form of a deferred purchase price would have to be regarded as "subordinate", i.e. lower ranking insolvency claim which could not be expected to be met in practice. The Bundesgerichtshof therefore decided not to apply the relevant provision of the German Insolvency Code (§ 39(1) Nr. 5). Cf. Nicolai Ritter in "How to effectively Recover State Aid in Insolvency Proceedings", EStaL 1-2008, p. 28.

773 Joined Cases C-328/99 and C-399/00, "Seleco", cited above in fn. 744, para. 76.

The authorities responsible for the execution of the recovery decision should, therefore, appeal any decision by the insolvency administrator or the insolvency court to allow a continuation of the insolvent beneficiary's activity beyond the time limits set in the recovery decision[774]. Likewise, national courts, when faced with such a request, should not allow for a continuation of an insolvent beneficiary's activity in the absence of full recovery.

For a Member State to achieve an effective execution of the recovery decision in a liquidation situation, it does not suffice to ensure that it receives a fair share of the bankrupt's estate. The Member State should also ensure that the undue advantage created by the aid is not transferred to the acquirer of the assets, as will be described in detail in the next section.

5. THE IDENTIFICATION OF THE BENEFICIARY

When recovering an undue advantage to a beneficiary in an insolvency situation the identification of the undertakings from whom the illegal aid must be regained can be problematic. The unlawful and incompatible aid must be recovered from the undertakings that actually benefited from it[775]. The identification of the beneficiary of unlawful aid can pose problems when the company that originally received the aid has been transformed, sold or liquidated by the time of the implementation of the recovery decision. If it then appears that the aid was relocated to other entities, the Member State may have to extend the recovery obligation to other companies in order to cover all effective beneficiaries and to ensure that the reimbursement requirement is not circumvented.

The transfer of ownership of an undertaking, in whole or in part, can be realized in different ways. The Court has differentiated between so called "share deals" or "asset deals".

In the event of a transfer of the shares, the identification of the beneficiary is not complicated. The Court has held that the sale of shares in a company to a third party does not affect the obligation of the original recipient or its

774 See Notice from the Commission – Towards an effective implementation of Commission decisions ordering Member States to recover unlawful and incompatible State aid, OJ. C 272, 15.11.2007, para. 66.

775 Case C-303/88, Italy v. Commission, cited above in fn. 763, para. 57; Case C-305/89, Italy v. Commission ("Alfa Romeo"), [1991] ECR I-1603, para. 40; Case C-277/00, "SMI", cited above in fn. 769, para. 75; Joined Cases T-111/01 and T-133/01, Saxonia Edelmetalle/Commission, [2005] ECR II-1579, para. 125.

successors to reimburse the aid if it can be established that the buyer paid the prevailing market price[776]. Then, the company, by continuing to pursue the subsidized activity, continues to derive an advantage from the aid, thus perpetuating the distortion of competition. The market price is the highest price which a private investor acting under normal competitive conditions is ready to pay for the entity having received unlawful and incompatible State aid. The aid element is then assessed at the market price and included in the purchase price[777]. As a result, if at the time of the transfer through a share deal it is already known that the company is obliged to repay an illegal aid, this will be reflected in the price of such company, which will be proportionally lower[778].

The Court has established that if assets are acquired by a third undertaking in the context of an open and competitive tender under market conditions at the market price, the element of aid enjoyed by the original recipient is not passed on to undertakings which won tenders[779]. Therefore, in these situations, the aid has to be repaid by its first beneficiary.

However, there are circumstances where the identity of the party against whom the recovery decision should be enforced is more complex. Such is the case when, following a Commission investigation or decision, the assets and liabilities of the firm as an ongoing concern are transferred to another entity controlled by the same persons at below-market prices or by way of procedures that lack transparency so that competitors are prevented from purchasing them[780]. In many instances the relocation does not reflect any other economic rationale than the invalidation of the recovery order[781]. The purpose of such a transaction can be to place the assets out of reach of the Commission decision and to ensure the business continues, albeit in a different guise[782]. For example, transferring all the assets of a company, free of any debt, to a new company, in such a way as to make it impossible under national law to recover the debts of the original beneficiary, creates an obstacle

776 Case C-328/99 and C-399/00, "Seleco", cited above in fn. 744, para. 83; Case C-277/00, "SMI", cited above in fn. 769, para. 80.

777 Case C-390/98, Banks, [2001] ECR I-6117, para. 77; Case C-277/00, "SMI", cited above in fn. 769, para. 80.

778 See Elisabetta Righini, Godot Is Here: Recovery as an Effective State Aid Remedy, cited above in fn. 753, page 278, see also Notice from the Commission, cited above in fn. 774.

779 Case C-390/98, Banks, cited in fn. 777, para. 77; Case C-277/00, "SMI", cited above in fn. 769, para. 80, see also paras. 94-95; Case C-214/07, Commission v. France, cited above in fn. 769, paras. 57-59.

780 Joined Cases C-328/99 and C-399/00, "Seleco", cited above in fn. 744, para. 69.

781 Case T-318/00, Freistaat Thüringen/Commission, [2005] ECR II-4179, para. 340.

782 Joined Cases C-328/99 and C-399/00, "Seleco", cited above in fn. 744, para. 69.

to the effective implementation of a recovery decision[783]. Where the Commission can prove that an entity was created in order to evade the obligation to repay aid, the new company will be required to reimburse the aid granted[784].

As regards recovery where the beneficiary is part of a group, the Court stated in its early jurisprudence[785], that if companies belonging to the same group form a single economic unit, they are considered as a sole undertaking for the purpose of the application of the State aid rules, despite having a legal personality separate from the original recipient. The State aid can, therefore, be recovered both from the parent company and the subsidiaries. If the Commission extends the recovery order to other group members as the original beneficiary, it has to verify whether these undertakings actually benefitted from the unlawful aid. Therefore, an undertaking belonging to a group of associated undertakings with internal mechanisms for the transfer of assets cannot be required to reimburse unlawful and incompatible State aid on the grounds that it belonged to the group, if it is clear that those transfer mechanisms were only used to the detriment of that undertaking and not for its benefit[786].

In sum, the two criteria to be considered in order to identify the beneficiary of the aid when the original recipient is part of a group or has been transformed, sold or liquidated by the time the recovery decision is implemented, are:

- Who has actually benefitted from the aid? and

- Has the undue advantage been transferred to another company? This will usually not be the case if the company, in part or as a whole, is transferred at market price, following an open, transparent and unconditional tender.

If the Commission suspects that these conditions are not fulfilled, it needs to prove that this is the case[787].

783 Case C-415/03, "Olympic Airways", cited above in fn. 750, paras. 33-34

784 Case C-277/00, "SMI", cited above in fn. 769, para. 86.

785 Case 323/82, Intermills v. Commission, [1984] ECR 3809, paras. 11-12.

786 Case T-318/00, Freistaat Thüringen/Commission, cited above in fn. 781, para. 324; Case T-324/00, CDA Datenträger Albrechts GmbH, [2005] ECR II-4309, para. 93.

787 The EU Courts have annulled a number of recovery decisions in which the Commission extended the recovery to third undertakings for lack of motivation. See Joined Cases C-328/99 and C-399/00, "Seleco", cited above in fn. 744; Case T-318/00, *Freistaat Thüringen/Commission*, cited above in fn. 781; Case T-324/00, CDA Datenträger Albrechts GmbH, cited above in fn. 786; Case C-277/00, "SMI", cited above in fn. 769; Case T-192/06, MTU Friedrichshafen v. Commission, [2007] ECR II-2889, paras. 46-52, confirmed by Case C-520/07 P, Commission v. MTU Friedrichshafen [nyr], para. 58.

6. THE PRINCIPLE OF LOYAL COOPERATION BETWEEN MEMBER STATES AND THE COMMISSION

A Member State's obligation to recover is unavoidable, except in the circumstances discussed above. Therefore, the obligation remains valid, even when the Member State encounters unforeseen and unforeseeable difficulties, or becomes aware of consequences overlooked by the Commission. In such case, the Member State should submit any problems for consideration to the Commission[788], together with proposals for suitable amendments to the decision in question. In such situations the Commission and the Member State concerned must respect the principle underlying Article 4(3) Treaty on the European Union (hereafter "TEU") which imposes a duty of genuine cooperation, and must work together in good faith with a view to overcoming difficulties whilst fully observing the provisions of the Treaties, and in particular the provisions on State aid[789].

It is, however, not sufficient for a Member State to merely inform the Commission of the legal and practical difficulties involved in implementing the decision, e.g. the very high number of beneficiaries involved[790] or other insurmountable internal difficulties[791], without taking any step to recover the aid from the undertaking in question, and without proposing to the Commission any alternative arrangements which enable the alleged problems to be overcome[792]. Mere apprehension of such difficulties cannot justify a failure by a Member State to apply EU law correctly[793].

Since the Commission and the Member States' authorities must cooperate to attain the objective of the restoration of competitive conditions in the Internal Market, the former may accept, in justified cases where the legal or technical difficulties have not yet been fully ascertained, a provisional implementation of the decision.

788 Case C-303/88, Italy v. Commission, cited above in fn. 763, para. 58.

789 Case C-303/88, Italy v. Commission, cited above in fn. 763, para. 58; Case C-348/93, Commission v. Italy, cited above in fn. 742, para. 17; Case C-350/93, Commission v Italy, cited above in fn. 742, para. 16; Case C-378/98, Commission v. Belgium, [2001] ECR I-5107, para. 31; C-261/99, Commission v France, [2001] ECR I-2537, para. 24; Case C-499/99, "Magefesa", cited above in fn. 760, para. 24; Case C-415/03, "Olympic Airways", cited above in fn. 750, para. 42.

790 Joined cases C-278/92, C-279/92 and C-280/92, cited above in fn. 741, paras. 14-18.

791 Case 94/87, Commission v. Germany, cited above in fn. 748, para. 10; Case C-6/97, Italy v. Commission, [1999] ECR I-2981, para. 32.

792 Case 94/87, Commission v. Germany cited above in fn. 748, para. 10; C-280/95, Commission v. Italy, [1998] ECR I-259, para. 14.

793 Case C-52/95, Commission v. France, [1995] ECR I-4443, para. 38; Case C-265/95, Commission v. France [1997] ECR I-6959, para. 55; Case C-280/95, Commission v. Italy, cited above in fn. 792, para. 16; Case C-404/97, Commission v. Portugal [2000] ECR I-04897, para. 52.

It is conditionally accepted if the full amount of unlawful and incompatible aid, including recovery interests, is paid into a blocked account. Thus, the company no longer benefits from the unlawful and incompatible advantage and the distortion of competition is removed until the final resolution of the difficulties.

It seems clear, therefore, that the EU Court will deal strictly with Member States claiming to encounter difficulties with implementation of a Commission decision, particularly where they have not cooperated with the Commission to resolve or mitigate those difficulties. The Court recently even condemned a Member State for failure to comply with a Commission recovery decision and for breach of the loyal cooperation obligation under Article 4(3) TFEU [794].

7. CONCLUSION

As outlined above, there are a number of both legal and practical obstacles impeding the effective implementation of a recovery decision by Member States. Nevertheless, in recent years the total number of pending cases, i.e. recovery decisions adopted by the Commission that are still awaiting full execution, has continually decreased. On 30 June 2009[795], there were 56 pending cases compared to 60 at the end of 2006 and 94 at the end of 2004. The amount of illegal and incompatible aid recovered has increased from 2.3 billion euros in December 2004 to 9.4 billion euros on 30 June 2009 (i.e. 90.9 percent of the total amount to be reimbursed). The percentage of illegal and incompatible aid still to be repaid has fallen accordingly (from 75 percent at the end of 2004 to 9.1 percent on 30 June 2009).

Where the Member State concerned does not comply with a recovery decision, the Commission may refer the case directly to the Court in accordance with Article 108(2) TFEU. If the judgment of the Court is not respected, the Commission may pursue the matter in accordance with Article 228(2). By 30 June 2009, 27 pending cases had been referred to the EU Courts under Article 108(2) TFEU (ex 88(2) EC) or Article 260(2) TFEU (ex 228(2) EC). This shows that in spite of the encouraging and improving repayment figures outlined above, the Commission continues to take the recovery of unlawful and incompatible aid very seriously and that it remains determined to push the implementation of its decisions, against all odds.

794 C-441/06, Commission v. France ("France Télécom"), [2007] ECR I-8887, para. 51.

795 The statistics provided in this article refer to decisions within the remit of DG Competition. The figures are updated twice a year and can be found under http://ec.europa.eu/competition/state_aid/studies_reports/recovery.html.

Mikołaj Stasiak

SELECTED ISSUES RELATING TO STATE AID IN THE TRANSPORT SECTOR

1. INTRODUCTION

Granting State aid in the transport sector is subject to many specific regulations which do not apply to other sectors. It can be justified by the fact that although the sector has undergone a range of transformations over the years, with liberalisation and technical advancement being the most important ones, there still remains the need for implementing national and EU policies concerning transport and ensuring that services will be generally available, provided at appropriate quality, safe, developing respecting the natural environment and well-coordinated. The specific approach of the Community lawmakers to the rules of admissibility of State aid in the transport sector manifests itself in the Treaty establishing the European Community ("EC Treaty") itself. According to Article 73, aid which meets the needs of transport coordination or is reimbursement for discharging certain obligations inherent in the concept of public service is compatible with the common market. At the same time, the provision of this article is *lex specialis* to Article 86(2) of the EC Treaty (judgment in the Altmark case),[796] which is also the basis for admissibility of aid in the transport sector.

The objective of these considerations is to indicate the fundamental provisions of the law which are specific for the transport sector differing from the general rules following from Article 87 of the EC Treaty and which are particularly applied when granting support, also due to their significance for shaping the transport policy[797].

2. ROAD TRANSPORT

Granting aid in this sector, just as in the entire land transport sector, is governed by Article 73 of the EC Treaty. According to the judgment in the case Altmark as well as Combus[798], in the event of State aid, its provisions were implemented only

796 Altmark Trans GmbH i Regierungspräsidium Magdeburg v. Nahverkehrsgesellschaft Altmark GmbH, [2003] ECR I-7747.

797 This article does not include issues relating to granting support for maritime and intermodal transport as well as for support for infrastructure.

798 Danske Busvognmoend, [2004] ECR II-917.

through Regulation No 1191/69[799] and Regulation No 1107/70[800]. This precluded the possibility to directly apply Article 73 as a basis for admissibility, particularly for aid whose compliance with the common market could not be determined on the grounds of these two regulations.

Within the scope of Regulation 1191/69, a number of doubts occurred. They were mainly addressed by the Court of First Instance in the Combus judgment. They were focused on the notion of public service obligations and public service contracts as well as on the provision of Article 14 of the Regulation No 1191/69[801]. At the same time, due to the passing of time and liberalisation of the market of land transport services, Regulation No 1107/70 has lost its significance.

On 3 December 2009 both these regulations were superseded by Regulation No 1370/07[802], which relates exclusively to public services concerning passenger transport by rail and by road. Article 1 of this regulation determines the manner of how "*competent authorities may act in the field of public passenger transport to guarantee the provision of services of general interest which are among other things more numerous, safer, of a higher quality or provided at lower cost than those that market forces alone would have allowed*"[803]. Due to the fact that the services provided are of public character, a compensation may be granted on the basis of a contract.

Article 2(i) of the Regulation stipulates that a public service contract means "*one or more legally binding acts confirming the agreement between a competent authority and a public service operator to entrust to that public service operator the management and operation of public passenger transport services subject to public service obligations; depending on the law of the Member State, the contract may also consist of a decision adopted by the competent authority: taking the form of an individual legislative or regulatory act, or containing conditions under which the competent authority itself provides the services or entrusts the provision of such services to an internal operator*".

799 Regulation (EEC) No 1191/69 of the Council of 26 June 1969 on action by Member States concerning the obligations inherent in the concept of a public service in transport by rail, road and inland waterway, OJ EU L 156 of 28.6.1969 as amended.

800 Regulation (EEC) No 1107/70 of the Council of 4 June 1970 on the granting of aids for transport by rail, road and inland waterway, OJ EU L 130 of 15.6.1970 as amended.

801 Exercising the obligation to provide services was understood as exercising the obligation imposed by the conduct with features of a decision. For public service contracts – providing a service resulted from a contractual liability. According to provisions of Regulation No 1191/69, this distinction caused a number of consequences of a material and legal nature (no foundation for admissibility of aid stemming from a contractual liability) as well as of a procedural character (no obligation to notify the Commission about aid on the basis of the conduct with features of a decision).

802 Regulation (EC) No 1370/2007 of the European Parliament and of the Council of 23 October 2007 on public passenger transport services by rail and by road and repealing Council Regulations (EEC) Nos 1191/69 and 1107/70.

803 Article 9 of Regulation No 1370/07 is applicable also to coordinating passenger land transport.

At the same time, this Regulation provides that a public service contract will:

- clearly define the public service obligations, including the geographical areas concerned;

- establish in advance, in an objective and transparent manner, and preventing overcompensation:
– the parameters to calculate the compensation,
– the nature and extent of any exclusive rights granted;

- determine the arrangements for the allocation of costs connected with provision of services. These costs may include in particular the costs of staff, energy, infrastructure charges, maintenance and repair of public transport vehicles, rolling stock and installations necessary for operating the passenger transport services, fixed costs and a suitable return on capital;

- determine the arrangements for the allocation of revenue from the sale of tickets which may be kept by the public service operator, repaid to the competent authority or shared between the two;

- be binding, in principle, for a period not exceeding 10 years.

The Regulation determines that public service contracts for passenger transport services by bus or tram must be awarded in accordance with procedures provided in Directive 2004/17/EC[804] and Directive 2004/18/EC[805]. The above requirement is not applied if such contracts take the form of concessions – in such case the provisions of the discussed Regulation apply. It should be emphasised in this context that application of national laws implementing the abovementioned directives does not mean, despite public procurement procedures being applied, that State aid is automatically ruled out, since this does not have to be connected with fulfilling all four conditions of the Altmark judgment[806].

804 Directive 2004/17/EC of the European Parliament and of the Council of 31 March 2004 coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors, OJ EU L 134 of 30.4.2004, p. 1.

805 Directive of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts, OJ EU L 134 of 30.4.2004, p. 114.

806 According to the Court, the compensation cannot be considered as State aid if all the following conditions are fulfilled at the same time:
the recipient undertaking must actually have public service obligations to discharge;
the parameters on the basis of which the compensation is calculated must be established in advance in an objective and transparent manner, to avoid it conferring an economic advantage which may favour the recipient undertaking over competing undertakings;

In situations when the provisions of the directives do not apply, an authority contracting a third party which is not an internal operator, awards the contract on the basis of a competitive tendering procedure. The procedure should be open to all operators, fair and observe the principles of transparency and non-discrimination. Following the submission of tenders and any preselection, the procedure may involve negotiations in accordance with these principles in order to determine how best to meet specific or complex requirements.

According to the Regulation, an internal operator is a legally distinct entity over which the competent local authority, or in the case of a group of authorities at least one competent local authority, exercises control similar to that exercised over its own departments. When identifying the competent authority, the following should be taken into consideration: the degree of representation on administrative, management or supervisory bodies, specifications relating thereto in the articles of association, ownership, effective influence and control over strategic and individual management decisions. However, 100% ownership of an internal operator by the competent public authority is not a mandatory requirement for exercising control similar to that exercised over its own departments.

The Regulation provides also in what circumstances it is not necessary to carry out a tender procedure when the service is committed to a third party which is not an internal operator.

The Regulation requires that for the purpose of calculating the compensation the contract:

- determines in a clear manner the public service obligations which the public service operator is to discharge and the geographical areas concerned;

- establishes in an objective and transparent manner the parameters on the basis of which the compensation is calculated and the extent of exclusive rights granted in order to prevent overcompensation;

the compensation cannot exceed what is necessary to cover all or part of the costs incurred in the discharge of public service obligations, taking into account the relevant receipts and a reasonable profit for discharging those obligations;
the undertaking which is to discharge public service obligations should be chosen pursuant to a public procurement procedure which would allow for the selection of the tenderer capable of providing those services at the least cost to the Community. If the tender procedure was not carried out, the amount of compensation must be determined on the basis of an analysis of the costs which a typical undertaking, well run and adequately provided with means of transport would have incurred in discharging those obligations.

- specifies the arrangements for the allocation of costs connected with providing the services.

In the event that a public service contract is directly awarded to an internal operator or when a competent local authority decides to provide services itself, the parameters for calculating the compensation should be specified in such a way that no compensation payment exceed the amount required to cover the net financial effect on costs incurred and revenues generated in discharging the public service obligations, taking account of revenue relating thereto kept by the public service operator and a reasonable profit. The manner of calculating the compensation in such cases is determined in detail in the Annex to the Regulation.

Article 9 of the Regulation provides that compensations for public services provision paid in accordance with this Regulation are compatible with the common market. They are not subject to the notification requirement laid down in Article 88 (3) of the EC Treaty, which, however, does not mean that the compensation for public service provision is not State aid.

3. RAIL TRANSPORT

Since 2000 the Community policy has been gradually heading towards creating conditions for the development of competition on the markets of rail transport services. In 2003, the market of rail freights was opened for competition as regards the Trans European Rail Freight Network (TERFN), three years later – with respect to international rail transport, in 2007 – rail cabotage and in 2010 – international passenger transport by rail.

At the same time, new legal provisions were introduced, making it necessary to:

- provide accounting and organisational separation between railway companies and enterprises managing railway infrastructure,

- introduce independent management in railway companies in accordance with the provisions applying to commercial companies.

Underlying the liberalisation of the sector was the conviction that it is necessary to grant State aid to railway undertakings. Consequently, the European Commission developed Community Guidelines on state aid for railway undertakings[807]. These guidelines apply also to the operation of urban, suburban or regional services.

As it has been mentioned before, no aid which did not comply with the conditions of admissibility provided in Regulation No 1191/69 and Regulation No 1107/70 could be treated as compliant directly on the basis of Article 73 of the EC Treaty. However, after Regulation No 137/07 entered into force, this article may be applied directly in relation to aid not covered by Regulation No 1380/07, which is the case, in particular, of aid for the needs of coordinating rail transport.

The Guidelines cover the application of Article 73 and 87 of the EC Treaty concerning State aid in the sector of rail transport as regards financing railway infrastructure, purchase and replacement of the rolling stock, cancellation of debts, restructuring and coordinating of transport.

3.1 RAILWAY INFRASTRUCTURE

The Commission would point out that the above listed Guidelines apply only to railway undertakings. Therefore, the Guidelines introduced no detailed solutions for providing aid to undertakings dealing with infrastructure. The Commission emphasises, however, that in principle support granted to infrastructure is not State aid under the condition that it provides equal and non-discriminatory access to infrastructure for all its users.

3.2 PURCHASE OF ROLLING STOCK

The European Commission confirms in the Guidelines the need to finance the purchase of new rolling stock in Member States. It maintains the position that such aid may be assessed on the basis of the general principles of the EC Treaty (aid for restructuring, small and medium-sized enterprises, environmental protection, compensation for public service provision) and on the basis of Article 73 of the EC Treaty (aid for coordinating transport).

At the same time the Guidelines introduce specific rules concerning regional aid. They allow to treat the costs of purchasing rolling stock in the sector of passenger railway transport and the costs of purchasing light trains, underground and trams as eligible for regional aid, which is a departure from the rules included in

807 OJ EU C 184 of 22.7.2008, p. 13.

the Guidelines on national regional aid for 2007-2013[808]. In reference to such aid, the Guidelines introduce also a number of additional conditions of admissibility in order to ensure that the new rolling stock complies with relevant standards concerning safety, environmental protection and interoperability.

Regional aid for the purchase of rolling stock, both in the form of initial investments and replacement of rolling stock, may be awarded only under the condition that the rolling stock is used on routes operating in a region covered by Article 87(3)(a) of the EC Treaty, an outermost region or a sparsely populated region. It is also required that the rolling stock be used in urban, suburban or regional passenger transport in a specific region, or on a specific route serving several regions, for a time not shorter than 10 years.

3.3 CANCELLATION OF DEBTS

Directive of the Council No 91/440/EEC of 29 July 1991 on the development of the Community's railways[809] stipulates that the Member States shall introduce appropriate mechanisms which would help reduce indebtedness of public railway undertakings to a level which would not impede sound financial management, and improve their financial situation. In order to achieve this objective, granting State aid according to Articles 73, 87 and 88 of the EC Treaty was planned.

The European Commission points out in the Guidelines on state aid for railway undertakings that irrespective of applying in Member States the appropriate mechanisms referred to in Directive 91/440/EEC, the level of indebtedness of many railway operators is still a mater of concern. This refers particularly to states which became a member of the EU after 1 May 2004.

The Commission emphasises that the admissibility of cancellation of debts considered to be State aid (i.e. fulfilling the conditions set forth in Article 87(1) of the EC Treaty) should be, in principle, evaluated on the basis of provisions concerning rescue aid and aid for restructuring based on Article 73 of the EC Treaty (providing that cancellation of debts relates exclusively to transport coordination and compensations for providing public services) and Regulation No 1192/69[810] (providing that debts relate to the normalisation of accounts).

808 OJ EU C 54 of 4.3.2006, p. 13.

809 OJ EU L 237 of 24.8.1991, p. 25 as amended.

810 Regulation (EEC) No 1192/69 of the Council of 26 June 1969 on common rules for the normalisation of the accounts of railway undertakings, OJ EU L 156 of 28.6.1969, p. 6, as amended.

The Commission assumes that old debts, incurred before Directive 2001/12/EC entered into force opening up the sector for competition, may be cancelled. The consequent State aid will be considered as compatible with the common market on the basis of Article 87(3)(c) of the EC Treaty, even without financial restructuring. For such aid to be compatible with the common market, it should be used only to offset clearly determined and individualised debts incurred before 1 May 2004 (and in relation to so-called old EU Member States – before 15 March 2001). The debts have to refer directly to the activity of railway transport or the management of railway infrastructure, its construction or use. These debts may not be incurred for implementing investment not directly relating to transport or infrastructure.

The cancellation of debts may apply to undertakings whose over-indebtedness impedes their proper financial management and when due to the anticipated development of competition on the market it cannot be expected that their financial situation improves. The aid may not, however, exceed the amount required to cancel debts, taking into consideration probable development of competition. Under no circumstances the aid may, in short time, place the beneficiary in a situation more favourable than that of an average well-managed undertaking with the same activity profile. The cancellation of debts must not give a beneficiary a competitive advantage which would prevent the development of effective competition on the market.

Cancellation of debts fulfilling all the above conditions may be considered as compatible with the common market.

3.4 AID FOR RESTRUCTURING

Aid for restructuring the railway transport sector is, in principle, granted based on Community Guidelines on State aid for rescuing and restructuring firms in difficulty[811]. The Guidelines on state aid for railway undertakings introduce, however, some departures in relation to freight transport. In particular, these departures take into consideration the fact that in many Member States freight transport and passenger transport have not been separated yet or this has occurred quite recently (Chapter 5 of the Guidelines).

811 OJ EU C 244 of 1.10.2004, p. 2.

3.5 AID FOR COORDINATION OF TRANSPORT

Aid for coordination of freight railway transport may be deemed compatible only on the basis of Article 73 of the EC Treaty. Community Guidelines on state aid for railway undertakings indicate the conditions taken into consideration by the Commission when assessing the admissibility of such aid, taking also into account the fact that the aid's objective is to guide the development of the transport sector in common interest. The Guidelines allow to grant aid for the use of railway infrastructure, limitation of external costs, interoperability and R&D. What is more, in reference to aid for coordinating passenger transport by rail, Article 9 of Regulation 1370/07 is applied.

4. AIR TRANSPORT

Opening up of the Community air transport market occurred at the end of the 1990s. Since then, a distinct development of the sector of airports has been observed; we have also see the appearance of cheap air carriers.

Community guidelines on financing of airports and start-up aid to airlines departing from regional airports[812] specify conditions of the admissibility of granting State aid in particular in the context of the Aéroports de Paris case [813].

The European Commission would point out that the basis to granting aid for airports and of start-up aid to airlines may be Articles 86 (2) or Article 87 (3)(a), (b) or (c) of the EC Treaty. Due to their particular significance for the development of the air transport market in Poland, this paper focuses in the fundamental issues concerning the aid for airports, omitting matters relating to start-up aid to airlines.

4.1 AIRPORTS

One of the conditions of obtaining State aid is running economic activity. In the Aéroports de Paris case, the Court stated that the activity carried out by airports is, in principle, economic activity, however, their operations may include also issues falling within the powers of the state, which are not economic activity and therefore are not covered by the provisions on State aid. Airports can also provide

812 OJ EU C 312 of 9.12.2005, p. 1.

813 Judgment of 12 December 2000 in case Aéroports de Paris v. Commission of the European Communities, [2000] ECR II-3929.

public services. Compensation for this, based on the conditions indicated in the Altmark judgment, will also not be State aid due to the lack of selective economic advantage.

Moreover, lack of State aid as regards some categories of airports may result from the fact that the aid granted to them does not influence competition or trade between Member States. It may also result from the fact that the state's activity can be considered as typical for a private investor operating in free market economy.

Analysing the above cases when State aid may be excluded, the Commission specifies in the Guidelines situations where aid will be considered as compatible with the common market.

Leaving aside cases when the state operates in a manner which is typical for a private investor, aid for constructing infrastructure or transferring infrastructure will be State aid. In such events, the Commission uses Article 86(2) or Article 87(3)(a), (b) or (c) of the EC Treaty as the basis for the aid's compatibility and verifies mainly the following issues: whether the construction and use of infrastructure correspond to precise objectives connected with the general economic interest, whether the infrastructure is necessary from the point of view of the objective it is supposed to serve, whether it offers satisfactory perspective of using in the medium term (concerns mainly the existing infrastructure), whether the access to it is open, equal and non-discriminatory for all potential users and what its impact on the development of trade is.

In relation to aid for the use of infrastructure, the Commission's position is that such aid can be considered as compatible with the common market only on the basis of Article 86(2)[814] of the EC Treaty, which means that it must be necessary for providing public services and cannot influence trade in a manner contradictory to the common market. Otherwise, it is treated as operating aid which may be admissible to a very limited extent on the basis of Article 87(3)(a) and (c) of the EC Treaty.

814 In relation to these issues, the Commission Decision of 28 November 2005 on the application of Article 86(2) of the EC Treaty to State aid in the form of public service compensation granted to certain undertakings entrusted with the operation of services of general economic interest (OJ EU L of 29.11.2005 No 312, p. 67) applies. As regards airports to which the above decision cannot be applied, the Commission, in its assessment, takes into consideration points 65-67 of the Community Guidelines referring to financing airports.

5. CONCLUSION

Irrespective of the specific regulations concerning road, rail and air transport, one should also notice several significant changes which have occurred in relation to the transport sector in the context of *de minimis* and regional aid.

Commission Regulation (EC) No 1998/2006 of 15 December 2006 on the application of Articles 87 and 88 of the Treaty to *de minimis* aid[815], as stipulated in its Article 1(1)(g), is not applicable to aid for purchasing vehicles intended for road transport granted to undertakings performing road freight transport for hire or reward. *De minimis* aid can be, however, granted for the purchase of passenger road transport vehicles.

Based on this Regulation, it is assumed that the total amount of *de minimis* aid for one undertaking operating within the sector of road transport cannot exceed 100 thousand euros throughout the period of three years.

In relation to regional aid for investment, it should be noted that Commission Regulation (EC) No 800/2008 declaring certain categories of aid compatible with the common market in application of Articles 87 and 88 of the Treaty[816] (General Block Exemption Regulation) precludes the possibility to treat means of transport and transport equipment as eligible costs.

What is more, Guidelines on national regional aid for 2007-2013 envisage detailed provisions relating to the admissibility of State aid in relation to some sectors. They can differ entirely from the Guidelines' provisions. One of such sectors is the transport sector. Point 50 of the Guidelines (footnote 48) states that expenses for purchasing transport equipment (movable assets) in the transport sector are not eligible for aid for initial investments. As it has already been pointed out, the Guidelines on state aid for railway undertakings introduce a departure from this rule in relation to passenger rail transport. These Guidelines also state that such departure may also be applied in relation to the stock used within public road transport, provided it is in accordance with the latest Community standards relating to new vehicles (point 34 footnote 1).

815 OJ EU L 379 of 28.12.2006, p. 5.
816 OJ EU L 214 of 9.8.2008, p. 3.

The development of the Community law with respect to State aid in the transport sector which has occurred throughout the last several years was caused mainly by the liberalisation of the sector and its gradual opening up for competition. The process of transformation has not, however, been completed yet. New provisions on granting support in relation to infrastructural projects as well as intermodal and multimodal transport might still be adopted in the near future.

Chapter IV

COMPETITION POLICY CHALLENGES

Henryka Bochniarz

COMPETITION AS A FOUNDATION OF MARKET ECONOMY

1. INTRODUCTION

Market economy was established in Poland twenty years ago under the conditions marked by great uncertainty, and neither with a legal system tailored to its requirements, nor capital, experience or knowledge of the ways of acting in the new market situation. Large state-owned enterprises prevailed at the time, controlling fixed assets, markets, equity and customers. The market structure was monopolistic. Only small areas of the economy were open to competition. Today, twenty years later, the legal system is more adjusted to market economy. Companies still have too little capital, but they are well-endowed with experience and knowledge. In most cases, the majority of market decisions are made by customers instead of manufacturers or suppliers. The market structure has also changed completely. Only in a few areas one can find activities characteristic for monopolies, abuses of companies' dominance, or price fixing agreements and other collusions. This results from a very dynamic development of entrepreneurship in Poland, as well as from the activity of the Antimonopoly Office (since 1996, the Office of Competition and Consumer Protection), established at the very beginning of the transformation in order to *counteract anti-competitive agreements and abuses of market dominance, as well as controlling mergers between enterprises*.[817] And if subsequent governments and parliaments based their decisions concerning the economy on efficiency rather than political criteria, there would be even less of such anti-competitive practices today.

Before the transformation, at the end of 1980s, 600 thousand private craft workshops were operating in Poland, employing 1.5 million people.[818] However, those enterprises did not form a basis for the development of market economy in Poland. After 1989, only 300 thousand of them survived, i.e. less than 10% of all businesses registered today.[819] Market economy has developed on the basis of newly registered enterprises. At the end of 1993, there were already 1.95 million

817 www.uokik.gov.pl.

818 www.zrp.pl.

819 *Zmiany strukturalne grup podmiotów gospodarki narodowej w 2008 roku*, Central Statistical Office (GUS), 20.02.2009.

of them, and at the end of 2008, 3.63 million.[820] Over 99.8% of them are small and medium-sized enterprises, over 96% of which are micro-enterprises, i.e. employing up to nine employees. It is difficult to imagine broad-scale monopolistic practices in an economy with a business sector of such a structure. Although such practices occur, Polish economy may nowadays be considered competitive. This results from privatisation and Poles' inclination to entrepreneurship. "Entrepreneurship" should be understood here as businesses competing for better market positions in order to generate profit and increase their economic value[821], but also to improve social welfare. Adam Smith already stated that humans in general tend to focus on their own profit instead of supporting public interests. However, with their own interest in mind, humans often support public interests in a more efficient way than when they actually intend to serve them.[822] This is what happened in the Polish economy, since between 1989 and 2009, owing to competition, among other factors, the Gross Domestic Product increased by over 70%.[823]

Nowadays, in the majority of sectors of the Polish economy, the competitive market structure prevails: market shares of individual companies are relatively small, their impact on prices or other conditions on the basis of which products are sold is comparable to that effected by other entities. However, this does not mean that anti-competitive practices do not occur. Data provided by the Polish competition authority show that in 2008, the authority completed 104 competition proceedings, 84 of which related to abuses of dominance.[824] In 32 cases, the Office concluded that the investigated practices were illegal and ordered them to be ceased. Assuming that the authority investigates abuses of dominance effected by large companies, the 32 cases identified in 2008 account for 1% of all large enterprises operating in Poland.

This is confirmed by a study concerning large enterprises, drawn up in 2009 by the Polish Confederation of Private Employers Lewiatan and Deloitte.[825] Companies employing more than 250 employees (there are over 3.2 thousand of

820 Number of companies entered in REGON register. The number of active companies is lower by 50 percent.

821 J. Bossak, *Międzynarodowa konkurencyjność gospodarki kraju i przedsiębiorstwa. Zagadnienia teoretyczne i metodologiczne*, (in:) *Konkurencyjność gospodarki Polski w dobie integracji z Unią Europejską i globalizacji*, ed. J. Kruszewski, SGH.

822 A. Smith, *Badania nad naturą i przyczynami bogactwa narodów*, PWE 2008.

823 GDP growth in 2009 – estimate.

824 http://www.uokik.gov.pl/pl/o_urzedzie/informacje_ogolne/sprawozdania_z_dzialalnosci_urze/.

825 *Monitoring kondycji sektora dużych przedsiębiorstw*, PKPP Lewiatan and Deloitte study, 2009 (nationwide random sample of 251 active large enterprises; surveys by CBOS).

such companies in Poland[826]), when asked about factors considered to carry the highest risk in their regular, non-critical operations, ranked the risk associated with increased competition on the market as the third most important factor. They estimated the risk at 2.24 points on a scale of five (with the possible contraction of the economy being most important – at 2.58 point). The fifth most important risk factor indicated was unfair competition (1.97 points). Therefore, large enterprises consider the market on which they operate as competitive, with the tendency for even stronger competition in the future. However, they fear that part of such competition may result from activities of other businesses that fall outside legal standards. In the group of small and medium-sized enterprises (SME), 26.9% of companies fear increased number of competitors on the market[827], while in the opinion of over 18% of them, competition in their sector is decreasing. However, large companies are not a threat for small and medium-sized enterprises. Almost 1/3 of SMEs consider cooperation with large companies as a factor facilitating growth and improving their economic condition. Only 6% of them perceive it as a threat.

Thus, the Polish economy is still developing its competitive structure. If assessed by means of structural methods, which assume the existence of a positive dependence between market share and company performance, the level of competitiveness in the Polish economy is high. Small and medium-sized enterprises, with small market shares, tend to have a better work and remuneration performance than large companies.[828] However, if we applied new methods of measuring competitiveness (non-structural methods[829]), based not on market shares or the assessment of market consolidation, but rather on the assessment of barriers to entry and exit, or on the assessment of potential competition, which may be an efficient market regulator, we might discover that the level of competition is still not high. This stems from legal regulations relating to the economy, including those governing business activity.

2. COMPETITION AND REGULATIONS

In terms of business environment, Poland was rated the 72th among 183 countries analysed by the World Bank in 2009[830] (compared to 68th in 2007). In terms of starting

826 *Działalność przedsiębiorstw niefinansowych w 2007 roku*, GUS 2009.

827 *Monitoring kondycji sektora MSP*, PKPP Lewiatan study, 2008 (nationwide random sample of 1100 private enterprises; surveys by CBOS).

828 Own calculations based on: *Działalność przedsiębiorstw niefinansowych w 2007 roku*, Central Statistical Office (GUS) 2009.

829 G. Iwata, *Measurement of conjectural variations in oligopoly*, Econometrica, 42/1974.

830 *Doing Business 2010*, World Bank, September 2009.

a business, Poland is rated the 117th, the 75th in terms of enforcing contracts, and the 164th in terms of dealing with construction permits.

How is it possible, considering the fact that Article 20 of the Constitution of the Republic of Poland stipulates that "*a social market economy, based on the freedom of economic activity, private ownership, and solidarity, dialogue and cooperation between social partners, shall be the basis of the economic system of the Republic of Poland*"? Unfortunately, the Constitutions allows to limit the freedom of business activity, however, "*only by means of statute and only for important public reasons*" (Article 22). This possibility is consequently used by the lawmakers: not long time ago there were 75 areas in the Polish economy where 236 types of authorisations were needed for running business activity, 30 areas where 85 types of clearances were needed to introduce products and services on the market, 140 areas where 48 types of clearances were needed for devices and installations to be admitted for use, 7 areas where 13 types of limitations of production and trading existed, 10 areas where 43 types of licenses were needed to run business, and 38 areas where 135 types of licenses were required to purse a profession. The situation has not much improved since then. The scale of regulation of business activity is too large. And this is not all: in the course of legislative works on the Act of 2 July 2004 on Freedom of Economic Activity, which governs *the starting, running and terminating business activity in the territory of the Republic of Poland* (Article 1), thus limiting economic freedom, over 800 acts of law have been revised. This shows the scale of regulation of business activity in Poland. 60% of acts adopted by the lower chamber of the Polish Parliament, or *Sejm*, are amendments. Since the beginning of the transformation, acts relating to taxation have been amended more than 100 times. The European Commission estimates that the costs resulting from defective regulations in Poland account for 4% of GDP (optimistic variant) or 5% of GDP (pessimistic variant). This is further increased by the costs of lost potential due to the need to participate in various administrative formalities by the management of small and medium-sized enterprises: every day SME directors lose 1.5 hours of their working time due to such formalities.

It is difficult to develop a competitive market under such conditions. Regulation of business activity not only limits consumer access to products and services, but also triggers tendency of businesses to operate on the grey market. This kind of competition restrictions fall beyond the scope of the Polish competition authority's responsibilities. This may be considered unfortunate, since we should see a comprehensive reform of regulated business activity prepared and adopted by *Sejm* as soon as possible.

Moreover, it is necessary to introduce systemic solutions limiting the room for developing defective legislation which requires frequent amendments. Retaining the current legislative system limits businesses' ability to adjust to new regulations, and thus the law becomes dead.

3. COMPETITION AND FACTORS BUILDING A BUSINESS'S COMPETITIVE MARKET POSITION

According to the above mentioned survey investigating small and medium-sized enterprises[831], over 50% of them builds their competitive position on prices. This rate is lower among large enterprises, constituting 37% as regards companies operating on the Polish market and almost 1/3 of companies operating on foreign markets.[832] Yet, the importance of quality of products and services is growing as 26.8% of SMEs consider this factor as the most important for building competitive position on the market. In the group of large companies, the number of enterprises putting emphasis on the quality of products and services is lower and constitutes 23.9% of companies competing on the Polish market and 20.1% of companies operating on foreign markets.

What does it imply for the competition on the market? Focusing business activity on cost cuts, which in most cases is exactly what "price competition" stands for, result in enterprises striving to reduce unit costs. Those companies are thus more inclined to seek potential economies of scale. They also aim at economies of scope (concentrating the production of many products in a single company). Both of these trends may affect market competition.

The shift in factors on which Polish enterprises build their competitive positions in the future, i.e. moving from costs towards quality, will make it possible to limit those trends. This process has already begun. It may be accelerated if companies gain access to EU funds, which are mainly allocated to innovative projects and projects improving the quality of human capital, as well as the increase of competition, which will certainly occur as soon as the world's economies come out of the crisis. Part of the companies surveyed support that, claiming that it is competition that would increase their inclination to innovation.[833]

831 *Monitoring kondycji sektora MSP*, PKPP Lewiatan study, 2008 (nationwide random sample of 1100 private enterprises; surveys by CBOS).

832 *Monitoring kondycji sektora dużych przedsiębiorstw*, PKPP Lewiatan and Deloitte study, 2009 (nationwide random sample of 251 active large enterprises; surveys by CBOS).

833 *Monitoring kondycji sektora dużych przedsiębiorstw*, PKPP Lewiatan and Deloitte study, 2009 (nationwide random sample of 251 active large enterprises; surveys by CBOS); *Monitoring kondycji sektora MSP*, PKPP Lewiatan study, 2008 (nationwide random sample of 1100 private enterprises; surveys by CBOS).

4. COMPETITION AND BEST PRACTICES

Milton Friedman claimed that *there is one and only one social responsibility of business – to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game.*[834] These rules are numerous: the law, but also established practices, traditions or informal codes of conduct. Their task is to reduce uncertainty, limit risk and thus decrease transaction costs in the economy. The problem appears when the law, informal codes of conduct or established practices, instead of supporting business activity, limit its development. Theoretically, the law may be quite quickly amended. However, changing informal limitations is much more difficult and requires much more time. The solution applied by developed economies, including the Polish economy, is to develop the best practices. All companies listed on the Warsaw Stock Exchange (WSE) have the obligation to take a stand with respect to the best practices prepared by the WSE. These best practices are not binding for the companies, however. They either have to comply by them or explain their non-compliance. This seems an important measure, which may complement other measures supporting market competition. To date, only a few out of over 1.8 million of businesses actively operating on the Polish market have their own codes of best practices or have adopted codes prepared by other entities, including such institutions as PCPE Lewiatan.

In 2006, the Confederation has prepared and adopted the Ethical Code Of Employers Members of the Polish Confederation of Private Employers Lewiatan: a declaration of values in business. Each member company, as well as each company applying for Lewiatan membership, must confirm its approval of the rules specified in the Ethical Code, which reads:

1. As entrepreneurs, we acknowledge that our primary responsibility is to:

    - provide clients and consumers with products (goods and services) of adequate quality,

    - do so on a long-term basis,

    - ensure appropriate relations with a company chief stakeholders,

    - act in compliance with the law and ethical standards.

834 M. Friedman, *The Social Responsibility of Business Is to Increase Its Profits*, NYTM, 1970.

2. Our objective is to ensure that our enterprises enjoy confidence of all the stakeholders, e.g. customers, consumers, employees, managers, shareholders, suppliers, recipients, competitors and the general public.

3. While taking our decisions, we analyse carefully and take into consideration opinions of individuals and groups functioning in the immediate environment of our companies.

4. We shape the organizational culture of our companies in such a way as to make the employers feel responsible for their employees and the employees –responsible for the assignments they are entrusted with.

5. We ensure that our employees are not subject to any kind of discrimination, their dignity is respected, their work is appropriately and timely remunerated and their working conditions are safe and healthy.

6. We try to ensure that our companies are managed efficiently at all levels and in compliance with ethical standards so as to serve as an example of best practice.

7. Our production, service and trade activities as well as our financial operations are performed transparently and we are prepared to bear the consequences of our errors.

8. We are solid partners in production of goods and multiplication of values; our capability of responding creatively to changes in the social environment is proved by fair competence and profits we achieve.

9. In pursuit of general welfare, including the natural environment, we undertake vital social initiatives and provide sponsorship adequate to our possibilities.

10. Our reliability is proved by the consistence of what we say and what we do.

Point 8 of the Code directly refers to fair competition; other points refer to it indirectly.

Along with best wishes for the Office of Competition and Consumer Protection on its 20th anniversary, PCPE Lewiatan would like to propose that the institutions join forces promoting the idea of economic competition by disseminating the best practices. Let us show all companies in Poland that having and complying by the best practices is worthwhile and beneficial. This way, the activity of enterprises becomes more transparent for all stakeholders, which does not only reduce their operating costs, but also increase trust in business, thus improving market competition. Since trust in the Polish context, including business relations, is scarce, let us together try and make it universally available.

In order for competition to become a real and sustainable foundation of the Polish market economy, the Competition Authority's activities, however important and efficient, must be supported by measures taken in other areas as well. We need a reform of regulated business activity and the legislative process, limiting red tape and related costs. We need the development of enterprises that would trigger increasing importance of non-price factors in building competitive position on the market, and the implementation of the best practices by companies. These crucial factors will complement the activities of the Office of Competition and Consumer Protection thus turning the objective of strengthening competition on the Polish market from the task of a single institution into a priority of many entities, enterprises included.

Gergely Csorba, Virág Balogh and Balázs Pálvölgyi

COMPETITION POLICY CHALLENGES IN THE RETAIL SECTOR: SOME HUNGARIAN EXPERIENCES[835]

1. INTRODUCTION

In recent decades, the retail sector has increasingly become a focus of attention for policymakers and consumers alike, especially in emerging markets. The entry and subsequent expansion of international supermarket chains resulted, on the one hand, in a significantly greater variety of products being available to consumers, coupled with a decreasing real price level – developments which most probably increased consumer welfare. On the other hand, the aggressive advertising strategies employed by the supermarkets led to many complaints on the part of individuals. Additionally, local suppliers (especially of agricultural products) lost a considerable part of their bargaining power to the retail chains, and it is controversial how the resulting decrease in wholesale prices affects welfare in the short and the long run. In some countries, as in Hungary, the ensuing lobbying activities of various groups of producers led to the government attempting to intervene in the retail market, leading to heated debates and disagreements.

This paper examines the challenges faced by competition policy in regard to the retail sector. The relevant practices will be addressed taking into account firstly, whether they are compatible with competition law, and secondly, whether they contribute to consumers' welfare (as distinct from total welfare, which would include producers' surplus). The analysis will be biased towards the problems the Hungarian Competition Authority (Gazdasági Versenyhivatal, hereafter "GVH") faced; however, these experiences may be relevant for other jurisdictions, especially in Central and Eastern Europe.

Following a brief overview of the Hungarian sector, three main areas are presented where competition policy and competition authorities could have an impact:

835 This paper is partly based on the lecture of the first author at the 2009 International Competition Law Forum organized by the Office of Competition and Consumer Protection, Poland. We thank Aliz McLean for useful comments. The views expressed are those of the authors only, and should not be interpreted as the opinion of the Hungarian Competition Authority (GVH).

1. Directly protecting competition (and thus indirectly consumers) from the harmful effects of concentration, using the traditional tools of antitrust, specifically: preventing restrictive agreements, abuses of dominance and anti-competitive mergers.

2. Directly protecting consumers (and thus indirectly competition) from the harmful effects of information distortion, using tools of consumer protection:[836] especially important practices to look at here are price depiction and bait advertising.

3. Directly protecting competition (and thus indirectly consumers) from the potentially harmful effects of legislation through competition advocacy, as opposed to safeguarding (domestic) competitors.

In our experience, traditional antitrust tools offer fewer opportunities for competition authorities to handle the possible problems arising in the retail sector, because of the structural features of this market: usually, there are large supermarket chains competing fiercely, so there is no firm in dominant position and less room for restrictive agreements. However, the competitive process can be significantly affected by the retail chains' advertising methods and the government's industry policy, and this is the area where competition authorities can have more influence through active consumer protection and advocacy.

2. MARKET STRUCTURE OF THE HUNGARIAN RETAIL SECTOR

In the past fifteen years, the Hungarian retail sector (similarly to the case of many other countries in the region) experienced considerable growth, fuelled by large-scale entries and the following market consolidation.

International supermarket chains have been active in the Hungarian market since the end of the 1990s, and have expanded considerably in the recent decade. Tesco quickly became the largest player, and is still developing fast by building smaller outlets (under the brand Tesco Express) in smaller locations, while already being present in most areas with hypermarkets. The previously fragmented domestic retailers lost considerable market shares to the supermarkets, consequently

836 We realize that not all competition authorities have a legal obligation and jurisdiction to examine consumer protection cases.

a large number of them merged, creating three national conglomerates, each with a market share of approximately 10-15 percent. Following this consolidation, there was still some room for entry on the part of the low-pricing discount chains: Lidl successfully entered and subsequently expanded in 2006, similarly to Aldi in 2008. The public market shares of the main Hungarian retail firms are shown in Table 1 below.

Table 1 Major retail firms in Hungary and estimated market shares in 2007 by AC Nielsen

Undertaking	Nationality	Estimated market share
Tesco Global	British	17.3%
CBA	Hungarian	16.4%
CO-OP Hungary	Hungarian	13.7%
Reál Hungária	Hungarian	10.3%
SPAR	Austrian	8.1%
Auchan	French	6.6%
Penny Market	German	4.5%
Lidl	German	3.8%
Magyar Hipermarket / Cora	French	3.7%
Plus	German	3.3%
Other smalls	Hungarian	12.1%
Total		**100%**

As a result of the series of entries, retail turnover almost doubled from 2000 to 2007 (reaching a level of around 12.7 billion euros), a process accompanied (and partly driven) by a significant decrease in prices.

3. ANTITRUST ACTIVITIES IN THE RETAIL SECTOR

The main objective of all competition authorities is to prevent harmful effects of various concentrations of market power. The three main areas of antitrust shall be covered in the following order: restrictive agreements,[837] abuses of dominance,[838] and merger control.

There exists an issue concerning the retail sector that is often presented as a primary source of sector-specific problems: the buyer power of large retail chains.

837 Article 81 of the EC Treaty and Article 11 of the Hungarian Competition Act (Act LVII of 1996).

838 Article 82 of the EC Treaty and Article 21 of the Hungarian Competition Act.

The long-run theory of harm is assumed to be the following: low wholesale prices enforced by the supermarkets create barriers to entry and expansion, and prevent investments at the upstream (producer) level, therefore causing exits from the market, which in turn could lead to a drop in the quality of goods, resulting in consumer harm. It is, however, very hard to find evidence supporting these negative effects of buyer power,[839] while the beneficial effects of low retail prices (due to the lower wholesale prices) are clear. Therefore, in our view, the starting point when considering buyer power in the retail sector from an antitrust point of view should be that it is, at least, neutral with regard to consumer welfare, unless proven otherwise.

3.1 RESTRICTIVE AGREEMENTS

Horizontal price-fixing seems infrequent between retail chains – indeed, the GVH has not conducted any cartel investigations concerning supermarkets.[840] A possible explanation stems from the structure of the industry: a large number of differentiated products are offered, competition is not based solely on price, market power is usually not symmetrically distributed – these factors make collusion harder to sustain, monitor and enforce.

A self-organized cartel does not seem probable on the producer level either, due to the market being very fragmented. Trade associations could present an opportunity to get around this problem, and make it possible to organize (or at least recommend) some kind of price-fixing or market sharing. However, no such activity has been observed by the GVH in the past five years,[841] and therefore no cartel investigations were conducted against the producers either.

Producers could potentially greatly increase their efficiency, or possibly counterbalance the buyer power of retailers through some manner of (non hard-core) horizontal cooperation, for example the common use of infrastructure like marketing, storage, or logistics. This type of horizontal cooperation would

839 On this theory and empirical evidence, see Chapter 9 of the very detailed UK Competition Commission [2008] groceries report: The supply of groceries in the UK market investigation.

840 Although rarely allegations of price-fixing emerge (dawn raids in Belgium and Iceland in 2007), we are not aware of an across-the-board cartel among retail chains. There have been a few examples however, where suppliers of specific products and competing retailers were involved in a cartel activity: the UK milk cartel that ended with a settlement in 2007, and the French perfume cartel in 2006).

841 The last GVH case in 2005 involved the price fixing and market sharing of Egg Producers' Association (case number Vj-199/2005). Interestingly, the Ministry of Agriculture was notified about the activities of the "price committees", but did not notice that it violates competition law.

most probably be pro-competitive, especially if the combined market share of the participants were below 10 percent, in which case the agreement would be exempted.[842] However, even this kind of benign cooperation is hard to find in Hungary, mainly due to internal conflicts among producers.

In a similar spirit, smaller retailers could also cooperate in a way that is not anti-competitive, by forming so-called buyer groups. In this case, positive effects may be even more likely to emerge, leading to a decrease in prices of consumer goods.[843] The GVH has not investigated any horizontal agreements between buyers in the past five years.[844]

As a consequence of producers' small market power coupled with retailers' large buyer power, there are few, if any, vertical agreements initiated by the producers (such as retail price maintenance or exclusivity clauses), which in many markets are the concerted practices most frequently investigated by competition authorities. Vertical agreements introduced by the supermarkets will be discussed in the next section.

3.2 ABUSES OF DOMINANCE

The typical market structure in the retail sector is oligopoly with a large number (usually around 5 to 12) of major chains competing vigorously with relatively low barriers to expansion. The market circumstances make it very difficult for any company to behave to an appreciable extent independently of its competitors and its consumers, that is to establish dominant position. This configuration applies to the Hungarian retail sector as well (the largest firm's market share being below 20 percent), and therefore the GVH did not conduct any investigations into cases of abuse of dominance in the traditional antitrust sense.

However, the GVH is in the special position of also acting as the agency to enforce a specific article of the Trade Act,[845] which contains a definition for "abuse of significant market power" that is different from the well-known antitrust use.

842 See the Commission's Horizontal Guidelines (2001, O.J C3/02).

843 The pro- and anti-competitive issues concerning buyer groups are discussed in detail in the OFT [2007] discussion paper: The competitive effects of buyer groups.

844 The last cases in 2003-2004 (Metro/Spar/Praktiker Vj-176/2003 and Delta Unio Vj-30/2004) were cleared under the de minimis rule as the joint shares of products procured were below 10 percent of the relevant market.

845 Article 7 of the Act CLXIV of 2005 on Trade.

A supplier is said to have significant market power (SMP) based solely on its revenue and not on its market position – specifically, its consolidated net revenues should be in excess of 100 billion Hungarian forints (around 400 million euros). The listed abuses of SMP are in fact very similar in spirit to potential abuses of (buyer-sided) dominance in the antitrust sense, or to simple vertical agreements enforced by the retail firms. These abuses are the following:

- Direct exploitation: "unjustified amendment of contractual conditions; undue risk pooling contract conditions; applying various charges for services not otherwise requested by the supplier as a precondition for being admitted to the trader's list";

- Discrimination: "undue discrimination against a supplier" (these are also very similar to selective dealerships agreements);

- Below-cost pricing: "applying a sale price for products which are not owned by the trader below the price invoiced as contracted";

- Explicit refusal: "undue restriction of access of a supplier to marketing channels; asserting a threat for canceling the contract".

Although no effect-based logic is needed explicitly in investigating these claims, the GVH has attempted to apply rule-of-reason, since, as previously discussed, buyer power can have significant pro-competitive effects. It would be, however, beneficial to protect wholesalers against ex post exploitative abuses (like renegotiating contracts after delivery, or not adhering to the previously agreed returning policy) and create a predictable environment, otherwise it might indeed render producers' business too risky, or even unprofitable, leading to a potential consumer harm in the long run.

Seven cases have been investigated from 2006 in detail, each concerning exploitative and discriminative contracting practices; six of these resulted in the company committing to change its policies on fees and selection of suppliers in accordance with the Trade Act.[846]

846 In case Vj-92/2006, Tesco substantially modified its policies relating to the stocking of its shelves: while before, 40-50 companies had contracts with one or more suppliers, under the new regime, Tesco only allowed six chosen merchandiser companies to offer services to the suppliers, unnecessarily limiting their choice. The case was closed after the behavioral remedies offered: Tesco agreed to hold an open tender yearly to determine the list of companies the suppliers could chose from, and to supply these companies with the tools/appliances they need without charging the expenses to Tesco's suppliers.

3.3 MERGER CONTROL

The retail mergers typically investigated by national competition authorities involve domestic chains. Given the market structure presented in Section 2, the transactions of relatively less significant supermarkets are unlikely to raise competition problems in small countries like Hungary, because of the strong presence of international chains – indeed, all of these transactions were cleared in Phase I by the GVH.[847]

The more problematic are mergers involving international retail chains, as these chains are the driving forces behind competition in the sector, and a post-transaction price increase could materialize if the merging parties were each other's closest competitors. These are typically mergers that would be notified to the European Commission, given the revenue and widespread presence in various EU countries.

There is an inherent characteristic of the Merger Regulation (ECMR), however, that renders it difficult for the Commission to effectively challenge transactions significantly impeding effective competition on local level, since such small markets cannot constitute a "substantial part of the common market", as required by the law.[848] Since competition in the retail sector is typically localized, it thus becomes possible that a merger, though cleared by the Commission, adversely affects some small markets, and thus might have been challenged by a national competition authority.

Such a case occurred recently when Tesco acquired Carrefour in the Czech Republic and Slovakia.[849] The transaction concerning stores in the former country was reviewed by the Commission, that found the possibility of a significant lessening of competition in two local areas with around 200 thousand inhabitants. However, since the parts of the Czech Republic did not represent a substantial part of the

Four parallel cases were run against six supermarket chains (Vj-91/2008, Vj-92/2008, Vj-93/2008, Vj-94/2008), in which problems arose regarding extra fees stipulated in contracts with suppliers, which were very obscure and could have been freely interpreted after delivery (concerning for example the returning of goods). The GVH thought these contracts place too large proportion of the risk onto the suppliers, and accepted a detailed remedy packages: the most problematic points were removed from the contracts, and a more balanced distribution of risk was created between the contracting parties.

847 In the last two merger cases (Vj-41/2009 and Vj-64/2009) there existed some territorial overlaps between the merging parties' catchment areas, but there were enough larger competitors present in those areas to likely prevent any price-raising initiative.

848 See Article 2 of Council Regulation (EC) No 139/2004.

849 Comp.M.3905 Tesco/Carrefour (Czech Republic and Slovakia).

Internal Market, the merger was subsequently cleared.[850] Conversely, the Slovak Antimonopoly Office requested to review the Slovak part of the transaction itself, and blocked it.

Concluding, obviously not all retail mergers should be investigated by the affected countries' national competition authorities, however, these agencies should, in each case, carefully consider whether the transaction might have anti-competitive effects in some, but not all local markets – if there is such a clue, then they are in a better position to address the anticipated problems.[851]

4. CONSUMER PROTECTION IN THE RETAIL SECTOR

It is conventional to assume in today's antitrust and consumer protection policy that competition is the best way to protect consumers: when the competitive process is effective, consumer choice is optimal and consumer detriment is minimized. On the other hand, optimal consumer choice is a cornerstone of effective competition, so distortions on the demand side of markets can be as harmful to the competitive process as distortions on the supply side.[852] Therefore, a competition agency with a market-based consumer protection approach can do a lot in ensuring that consumers make optimal decisions, and that markets serve them efficiently.

If a consumer makes a sub-optimal choice, it can be detrimental to him/her in the following ways:

1. Direct consumer detriment is sustained in the short term and does not have an effect on competition (e.g. the consumer pays more than he/she intended).

2. Consumer detriment in the long term (or structural consumer detriment)

850 Point 32 of the decision: "Thus the population of these two local areas represents less than 0.05% of the total EU population. As regards the total volume of retail sales of daily consumer goods realised in these two local markets, they would represent less than 0.05% of the retail sales of daily consumer goods within the common market. Therefore, the local markets of Plzeň and Hradec Králové cannot be considered as a substantial part of the common market."

851 When supermarket chain Spar (with a national market share of [5-15%]) bought the Hungarian branch of Plus (with a national market share of [2-5%]), the GVH, after careful consideration, did not request the merger, as the combined market share of the parties was always below 20% not only nationally, but in all overlapping markets as well (the figured are based on the public version of the Commission's decision in COMP.M.5134 Spar/Plus Hungary).

852 See OECD [2006], Roundtable on demand-side economics of consumer protection: Summary Report, DSTI/CP(2006)3/FINAL.

affects consumers through the distortion of the competitive process if they consistently make sub-optimal choices.

3. Moreover, in the long term, confidence in the market is essential to ensure that the competitive process functions in the best possible way. Consumers should not need to question the truthfulness of statements in advertising, otherwise their search costs might rise dramatically and they might even exit the market, which would lead to further long-run detriment.

4.1 COMMERCIAL PRACTICES AND CONSUMER BEHAVIOR IN RETAIL MARKETS

Usually retailers apply specific commercial practices in the form of leaflets that are sent out to consumers living in the vicinity of specific stores, which underlines the strong geographic dimension of competition in this market. The promotional materials come out every sale period, and every material advertises multiple products on sale for a limited period of time (usually one or two weeks). There are hardly any integrated communication campaigns in the retail market, even TV commercials are rarely used. Although there are some retailers focusing on quality instead of prices, due to the fact that the majority of Hungarian consumers are strongly price-sensitive, the main focus of retail firms' communication strategies is still on low prices.

In most cases, the legal problems on this market are connected either to bait advertising, or false depiction of prices or savings.[853] The US Federal Trade Commission, recognizing the severity of the issue, has introduced a guide concerning bait advertising,[854] while the UK Office of Fair Trading very recently announced that it would open a market investigation into deceptive pricing, including reference pricing and bait advertising.[855]

It may be presumed that consumers, who once went to a given retailer, will not go to another store (which could be at a distance of many miles) if they do not find the product they were hoping to buy. This is the strongest assumption that

853 We will not discuss the "bait-and-switch" strategy, which is a commercial practice very similar to bait advertising. Bait-and-switch means that companies deliberately under-stock a specific kind of good hoping that the consumer will switch to a more expensive good when faced with the unavailability of the one supposedly on sale. See Lazear [1994]: Bait-and-switch, Working Paper in Economics, E-94-1, The Hoover Institution.

854 FTC (1977), Guides against bait advertising, 16 CFR PART 238.

855 See the OFT's press release, http://www.oft.gov.uk/news/press/2009/126-09.

underlines the GVH's cases and thinking on how competition can be affected by these commercial practices. The consumer will purchase some goods even if there might be a better deal for him/her somewhere else, and therefore multiproduct retailers gain even in cases when the advertised good is out of stock – as is the mechanism of bait advertising.

Often, the shortage of stock encountered while investigating bait advertising is not the retailer's goal – being rational market players, retailers want to sell all products. However, due to the high number of goods they sell and the complexity of the logistics needed, failures occur. In recent years, and partly because of an GVH intervention, there has been visible development in the sector as to the shortage of stock and the quality of logistics – resulting ideally in a smaller number of sub-optimal consumer choices and more effective competition.

Although direct consumer detriment might be insignificant in these cases, especially as in the Fast Moving Consumer Goods (FMCG) segment, where these abuses typically happen, the value of transactions usually does not exceed a specific amount, the overall indirect/structural detriment might still be large because of the large number of transactions in the whole sector. Since there is little direct consumer detriment and the price – being a search characteristic – is easily learned, an argument might be made here not to intervene in this segment.[856] However, some problems seem to persist – at least on the Hungarian market – calling to mind the implications of Akerlof's "market for lemons."[857] As consumers do not know which market player can be trusted as to validity of prices and sufficient stocks (shortage of stock being a key element when assessing bait advertising), there is little incentive for firms to improve their quality of advertising and little incentives for consumers to learn.

In reaction to the above-mentioned persistent problems in the sector, the GVH has opened 23 cases in the retail market from the beginning of 2007 and has levied fines totaling approximately 1.5 million euros.

In the GVH's practice, bait advertising is considered to be unlawful, if:

- advertised good is not available at stores during the entire sales period, or

856 Nelson [1970]: Information and consumer behavior, Journal of Political Economy 78, p. 311-329.

857 Akerlof [1984]: The market for "lemons": Quality, uncertainty and the market mechanism, Quarterly Journal of Economics, pp. 488-500.

- advertised item is not available at stores only at the beginning of the sales period, even if it is offered later (taking into consideration that consumers are often inclined to attempt purchases at the beginning of the sales period due to sales only being in effect "until stocks last"), or

- starting stock of the advertised good is unrealistically low at the beginning of the sales period and hence runs out relatively early. The GVH has established a requirement for a substantive stock to be available during the first three days of the sales period.[858]

When consumers are to pay a higher than advertised price, it definitely leads to direct and also indirect consumer harm. Therefore, the GVH has stated that it is deceptive to offer goods for a price different to that depicted in the commercial practice. Furthermore, it is also deceptive to quote a reference price that has never been charged – in this case, the amount of the price cut (the "sale", often expressed in percentage terms) in the advertisement is false, and is thus misleading to consumers.[859]

4.2 THE UNFAIR COMMERCIAL PRACTICES DIRECTIVE AND THE WAY AHEAD

The described practice of the GVH was established under national unfairness law. Hungary, however, has recently implemented the Unfair Commercial Practices Directive, [860] which came into effect in September 2008.[861] Recognizing the importance and possible harmful effects of bait advertising, the European Union included this commercial practice in its so-called blacklist,[862] while price deception is handled under misleading advertising (Article 6). Since then, advertisements that involve shortage of stock or price deception must be appraised on this basis. There are several ongoing cases under the new regime, but it seems now that the earlier practice of the GVH might be maintained.

It is obvious that it is difficult to build a coherent strategy for solving these

858 See case number Vj-173/2007 concerning Tesco's bait advertisement of several products.

859 See case number Vj-133/2008 concerning Penny Market's price deception of several products.

860 Directive 2005/29/EC of the European Parliament and of the Council of 11 May 2005 concerning unfair business-to-consumer commercial practices in the internal market.

861 Act XDIV of 2008 on unfair commercial practices.

862 Point 5. of annex 1 of the UCPD.

problems while serving consumers and competition at the same time – due to the vast logistical systems used, it is foreseeable that retail companies will always make mistakes. It is for the future to decide if there needs to be an intervention in the case of each failure, however small it might be, or whether resources should be focused on the truly detrimental bait advertising and price deception cases. It is still an open question how these goals might be achieved under the new directive, since the GVH's relevant experience is still quite narrow.

There is no question, however, that the retail sector will always remain in the focus of consumer protection agencies, the GVH included. It remains to be seen how these problems should be solved: (1) by business outreach covering finding a solution to lessen the logistics problems, without direct GVH intervention, (2) by raising consumer awareness, so the market will be able to resolve its problems through consumer behavior, or (3) by opening new cases, or perhaps some kind of a "healthy mixture" of the three should be sought.

5. COMPETITION ADVOCACY IN THE RETAIL SECTOR

State regulations have a strong impact on competition in any industry, including retail trade. The influence may be predominantly positive: for example, well-founded contract law may promote competition through increased transparency and by making the market environment more predictable. Regulations may, however, have serious negative effects, for instance, by establishing entry barriers, such as restrictions on the establishment of new outlets (or restrictions on floor size). Competition may also be damaged if competitors' ability, or incentives, to compete are constrained, i.e. through the outright prohibition of below-cost pricing (especially if the cost benchmark is wrongly defined).

Retail regulation is particularly sensitive to anti-competitive lobbying for three reasons. First, the efficiency of the trade sector has an impact on the whole economy. As an intermediary, trade has a large influence on both consumer choice and sales opportunities of producers. Retailers act as gate-keepers, and so determine to a large extent which supplier will be in the position to access final consumers. This process is not without conflicts. Second, the current trend of consolidation renders smaller retailers less competitive, and shifts bargaining power from suppliers to large retailers. Third, the trade sector is a considerable employer itself. In Hungary, around 300 thousand employees, about 12 percent of all employees, work in trade, and this share is similar in other countries as well.

As a result, anti-competitive regulatory proposals can gather strong support from most interested parties. Suppliers and smaller retailers are keen to support set of laws that soften price competition, while larger chains are also ready to accept restrictions that do not harm their profit. These problems are not specific to Hungary: competition authorities all around the world deal with similar issues in the retail sector.[863]

Sometimes, the restriction of competition may be warranted, as policymakers need to consider various social objectives, such as environmental protection, public health, or social equality. Often, however, the constraint is not justified by other benefits and might be a result of ignorance, or regulatory capture. Moreover, as consumers are usually weaker in representing their own interests than industry groups, competition authorities have a special duty to draw attention to the consumer welfare resulting from the competitive process. Hence competition advocacy, where the antitrust authority promotes a competitive environment through its relationship with other governmental entities (especially, through commenting on draft legislative proposals), constitutes a major instrument of competition policy.

5.1 RETAIL REGULATION AND COMPETITION POLICY IN HUNGARY

Concerns involving the impact of growing consolidation in the retail trade and a push for potentially anti-competitive regulation, notably for a ban on resale below cost (RBC), have been present in Hungary since the late 1990s. In 2000, the GVH published an in-depth analysis of the competitive conditions in retailing, where the authority acknowledged a trend of market concentration and reviewed international initiatives to deal with the buyer power of supermarkets. Specifically, this document stated its concerns on RBC regulations, regarding them false remedies.[864]

Despite continuous advocacy, the GVH could not prevent the adoption of special trade rules on agricultural products in 2003. According to the so-called Agricultural Regime, the retail price of agricultural and food industry products falling under the scope of the Act cannot be lower than the invoiced purchase price determined in the contract. Also, the time allowed for payments cannot exceed 30 days from the receipt of the goods. While some efficiency arguments can be raised

863 See for example the above-mentined grocery report of the UK Competition Commission, or the similar study of The Competition Authority (of Ireland) [2008]: Grocery Market Report.

864 GVH [2000]: Large Scale Retail Trade and Competition, Competition Office Bulletin, No. 3.

for the second rule, as it creates more transparency while not disproportionately restricting business practices, the first rule obviously reduces retailers' incentives to engage in sales promotions. This anti-competitive effect was however slightly reduced, as resale below the invoice price was eventually allowed in certain cases, such as in the case of vending products of reduced value, damaged packaging, or after their date of expiry.

The fact that the first restrictive regulations concerned agricultural products is not entirely surprising. The industry, being highly politicized due to its obvious importance for everyday life, has received special treatment even in the European Union, with the Common Agriculture Policy (CAP) legally restricting competition between producers through price regulations and quotas.[865] Nevertheless, even CAP regulations have recently been moving in a more pro-competitive direction.

In 2005, regulatory proposals aiming to restrict commercial practices applied by supermarkets beyond agricultural products were raised. In an attempt to provide higher quality background information to the lawmakers, the GVH organized a workshop where OECD experts presented how RBC regulations reduced welfare. Submissions to the OECD Roundtable also revealed that while RBC rules were difficult to enforce, they were likely to result in consumers paying higher prices, while their claimed benefits might be already provided by other laws. Thus, RBC was generally supported neither from an economic nor an empirical point of view.[866]

These arguments had some effect, and a general extension of resale below cost regulations was taken off the agenda. However, RBC was forbidden for goods where the supplier remained the owner, and various other regulations were included in the Trade Act, as discussed before in Section 3.2. The Trade Act follows international best practice in the sense that it promotes industrial self regulation, similarly to the UK Supermarket Code. The prohibition of many conducts listed may also be underpinned by efficiency arguments.

Nevertheless, the Trade Act also has significant shortcomings. First, it protects not only small and medium-sized enterprises (SMEs), but also big suppliers in

865 A detailed analysis can be found in Debroux [2008]: Politique agricole et droit & politique de la concurrence: une moisson à risque. Les raisons d'une cohabitation orageuse. (in:) Concurrences, No. 4, 2008, and in Debroux [2009]: Agriculture and competition law: a stormy relationship. (in:) Farm Law 2009 January.

866 OECD [2005]: Resale Below Cost Laws and Regulations. OECD Best Practice Roundtables. DAF/COMP(2005)43.

concentrated industries, thus preventing retailers from mitigating (through their buyer power) the seller power of big suppliers. Second, although larger chains are required to mutually adopt an ethical code, the nature of the rules was not established. Hence, the formal implementation of an Ethical Code had to be accepted by the GVH. Indeed this proved to be the case in 2006, when the retailers submitted a draft code to the GVH, and the authority voiced its concerns regarding both its content and its usability. They underlined that the Code contained only vague descriptions and detailed rules were lacking for the most widespread problems. Furthermore, the ethical committee to decide in disputes was not required to have representatives of all parties involved. The GVH tried its best to get the most out of the situation: it gave only a temporary permission for the application of the soft law, for about a year, until 31 December 2007. This allowed to accumulate experience on the working of the Code, and the GVH maintained the option to intervene. However, there was no significant enforcement in this period, and neither retailers nor suppliers advocated a change in the Code; hence, the authority prolonged its permission till 2010.

The restrictive regulations of the Agricultural Regime and the Trade Act are not unparalleled, but according to a survey of 17 European countries, most jurisdictions do not apply similar rules.[867] According to this study, RBC clauses are present in only six countries, and regulations constraining buyer power have been found in only eight.

After the initial uncertainty, enforcement related to the Trade Act increased, as more and more suppliers started to file complaints to the GVH. Building on this experience, and trying to tackle new regulatory initiatives willing to restrict competition further, during the summer of 2009 the GVH prepared a detailed study of the supplier-retailer relationships in agriculture.[868] In this study, the authority argued for the improvement of the transparency and predictability of contractual terms, which would be important to prevent the ripping-off of suppliers. The GVH also promoted the correction of the already mentioned shortcomings regarding the Ethical Code and advocated better rules in the Trade Act prescribing the requirements of soft law.

867 Pfister, Etienne [2008]: Regulation of the supplier-retailer commercial relationships: An overview of 17 European countries regimes. (in:) Concurrences, No. 3-2008.

868 See GVH press release of 29 September 2009: The GVH suggests enforceable ethical rules to the agricultural sector, available at http://www.gvh.hu/gvh/alpha?do=2&st=2&pg=133&m5_doc=6077.

Due to the quickly changing structure of the industry and the ever-present activities of various industry groups, there will always be room for retail regulation, and therefore competition advocacy. It is now more generally accepted that regulatory proposals be fact-based, empirically sound and make explicit the various outcomes of possible solutions.[869] Ensuring predictability while maintaining strong competition will certainly be an important challenge for all public policy makers.

869 The OECD Competition Assessment Toolkit offers methods to estimate the competitive effects of various policies. The most up-to-date version with related brochures is always available at the OECD website.

Anna Fornalczyk

THE BEGINNINGS OF COMPETITION POLICY IN POLAND

1. WHAT WAS THE STRATEGY OF COMPETITION LAW IMPLEMENTATION?

In December 1989 a package of 10 acts was adopted by *Sejm*, the lower chamber of Polish parliament, and entered into force on 1 January 1990. It was the beginning of political system changes in Poland consisting in the shift from central planning to market economy. It required the development of competition in order to force enterprises to be more efficient, the market to be better supplied and the increase of prices to be slowed down. The package mentioned above was supplemented by the Act of 24 February 1990 on counteracting monopolistic practices, which entered into force on 13 April 1990 (Antimonopoly Act)[870]. It was a beginning of the Antimonopoly Office's (AO) activity. AO was seated in Warsaw and it was the first competition authority in the whole post-communist countries. In 1990–1991 seven branches of the office were established: in Gdańsk, Lublin, Łódź, Katowice, Kraków, Poznań and Wrocław, which were to support the central office's activity in local markets[871].

Monopolistic structure of the economy, inherited from the central planning system, was perceived by the reformers as an important obstacle in the process of transformation. In this context, it was of utmost importance to create the right conditions for the emergence of competitive markets and to counteract monopolistic practices. It was also important to overcome stereotypes and change behavioral patterns of the managerial staff in enterprises and public administration, shaped in the past by the central planning system. The order in which the priorities of the Office of those days were listed is not random. This was how the Office's chief officers defined its strategy at the time.

Apart from organizing the AO, in the first year of its activity, it was essential to determine the method of implementation of its statutory tasks. The priority was to create the right conditions for developing competitive markets in Poland

870 Dz.U. of 1990 No 14, item 88 as amended.

871 Regulation of the President of the Antimonopoly Office of 28 September 1990 on the establishment of divisions of the Antimonopoly Office and establishment of their seats, territorial competence and jurisdiction (Monitor Polski No 36, item 294).

by influencing the organizational structure of the economy (monitoring of ownership transformations of enterprises, control of mergers and acquisitions (concentration transactions), divisions of enterprises). The structural approach to the implementation of competition law was based on the premise that eradicating or minimizing the causes of monopolistic practices (demonopolization of the economy) would be more efficient than focusing on imposing sanctions for anti-competitive practices of enterprises resulting from their dominant position in the market (regulatory approach).

2. HOW WAS DEMONOPOLIZATION PERFORMED BY THE OFFICE?

The Antimonopoly Act gave the Office important powers in terms of preventive control of ownership transformations of state-owned enterprises, control of mergers and acquisitions and division or liquidation of enterprises which have a dominant position in the market and „restrict competition or the conditions fostering it" (Article 12 (1))[872]. In Chapter 3 of the Antimonopoly Act, entitled „Influencing the development of organizational structures of economic operators" no thresholds were established for controlling transformations and concentration transactions, which meant that all transactions were controlled by the Office. The structural approach to the implementation of competition law, adopted in the early 1990s, assumed that with competition developing and dominance disappearing, the extent of administrative intervention in the behavior of enterprises which are dominant in relevant markets should decrease.

2.1 RESTRUCTURING OF THE ECONOMY

Since its inception, the Office took part in the restructuring and privatisation processes of state-owned enterprises and whole sectors of the economy. This occurred in a twofold manner: through statutory preventive control of ownership transformations of state-owned enterprises and the participation of the Office's representatives in the activities of government teams preparing sectoral restructuring and privatisation programmes (the sectors concerned include: the coal mining, petrochemical, steel, heavy chemistry, electricity supply, heating, armament, car, and sugar industries). The Office was actively involved in the implementation of the Mass Privatisation Programme commenced in 1991.

872 The latter right was used only in specific cases which resulted from the implementation of government demonopolisation programmes concerning selected branches of the economy (e.g.: division of enterprises of the wheat and milling industry as an activity fostering demonopolisation of the agricultural environment).

The Inter-Ministerial Team for Demonopolization and Privatization of the Agricultural Manufacturing Sector, managed by the Secretary of State in the Ministry of Ownership Transformations, was responsible for most of the demonopolization activities at that time. The Office had its representative there. The activity of this team impacted on the decisions of the President of the AO issued in 1991–1992 and concerning the forestry and agri-food processing industries. In 1992, 86 decisions of the President of the AO concerned those sectors[873].

The task of the Office's representatives in the activity of the teams dealing with restructuring and privatisation was to prevent the envisaged solutions from leading to excessive restricting of competition, as well as to prevent the return to the old organisation of enterprises typical for the centrally-planned economy.

For instance in February 1990, a new act entered into force shutting down central and regional unions of co-operatives. The act gave the AO power to prohibit the establishment of agricultural co-operatives, which were the exact replicas of Przedsiębiorstwo Spółdzielcze "Samopomoc Chłopska" (Cooperative Enterprise "Farmer Self-help"), which was being wound up at that time.

It was absolutely clear that constraints of competition generally led to shifting costs of the transformation onto the consumers through price increases. It happened that the increases were part of the programme or were tolerated by the government institutions as part of the strategy adopted by enterprises. In addition, bans related to the transformation or establishment of enterprises linked to agriculture or orders related to their division (in 1991–1992 this concerned the forestry industry, State Cereal Warehouses and Granaries and seed wholesalers) were aimed at encouraging the growth of SMEs in rural areas.

Another instance of the Office's representatives' participation in demonopolization of the economy was their involvement in the restructuring of the electricity supply sector and the prevention of the development of vertically integrated production and distribution structures restricting the development of competition in the electricity market. One of the first actions taken by the President of the AO was submitting an objection to the Court of Registration in August 1990, based on Article 11(5) of the Antimonopoly Act: on 2 August, the Minister of Industry established Polskie Sieci Elektroenergetyczne (PSE – Transmission System Operator), a joint-

873 Report on the activity of the Antimonopoly Office in 1992, Warszawa 1993.

stock company, failing to notify the fact in accordance with the relevant statutory procedure applicable in such situations and ensuring preventive control of setting up new and merging existing enterprises.

The objection regarding the enterprise's registration was not only of formal but also of substantive nature, as PSE would be responsible not only for the transmission of electricity but also for the wholesale trade of electricity[874]. According to the Office's opinion, crucial from the point of view of creating conditions for the development of competition in the electricity market were the provisions of PSE's statute concerning the Third Party Access (TPA) rule in transmission and regulation of the wholesale trade of electricity. The agreement that was reached on this issue with the Minister of Industry lead the President of the AO to cancel the objections with respect to the establishment of the new enterprise, which was subsequently registered on 28 September 1990. The above mentioned experience of the Office made it a natural candidate to take part in the works on the Energy Law concerning regulating access to transmission networks and setting electricity and gas tariffs.

Another instance of structural activities of the AO was the preparation of effective argumentation against the establishment of the Polish Coal Mining Company in the early 1990s, in which profitable mines were to be merged with non-profitable ones. The Office was against the idea of merging mines in that way also when a few years later a proposal to establish coal companies and the Coal Holding in Katowice was put forward. These were established anyway, as it was hoped that merging profitable and non-profitable mines would benefit the latter[875]. It turned out that the AO's proposal to establish a restructuring company was a good idea but such a company was set up by the Minister of Economy only in late 1990s. The Office had no legal grounds to issue a negative decision concerning the creation

874 On 1 July 2004, the national distribution of electricity was separated from its transmission. PSE Operator S.A., a joint-stock company wholly owned by the State Treasury was established and became the operator of the transmission system in Poland.

875 In 1992, the AO submitted to the Economic Committee of the Council of Ministers an assessment of risks related to the implementation of the governmental competition development programme for 1991-1993 which stated that: "It is all about including structurally inefficient mines (generating losses) in the holdings that are being created. Keeping mines of this kind as a part of larger structures will mean that internal subsidizing mechanisms known from the past will emerge again. These will not only weaken pro-efficiency motivations of those mines but will also weaken the mechanism of eliminating inefficient mines from the market. (…) due to the centralistic character of the holding, each of them will aim at maintaining the status quo. However, the fact that following an administrative decision inefficient mines were also included in the holding, will be used by the managements of particular holdings as an argument justifying why the rules of the economic game should be less strict and why the internal and external competition should exert less pressure", Antimonopoly Office, unpublished manuscript, Warszawa 1992.

of coal companies and the Coal Holding in Katowice as these activities were not likely to lead to excessive consolidation of the coal market. Efficiency arguments proved not to be convincing enough.

2.2 NATIONAL INVESTMENT FUNDS

Another example of the Office's structural activities was the National Investment Funds (NIF) scheme, developed in collaboration with the AO in 1992–1993. The Office's role was to formulate antitrust provisions to be included in the Act on NIFs to prevent concentrations of the funds' management. When assigning enterprises to particular NIFs in 1994, it was assumed that one fund may only consist of enterprises whose share in a relevant market does not exceed 30 percent. It was also agreed that assigning enterprises to NIFs would not be based on individual applications being submitted to the AO as a part of the statutory merger control. However, the Office had reserved the right to exclude enterprises assigned to a given NIF to prevent excessive concentration of enterprises of the same sector within one fund. The AO used this right in 1994 while monitoring the process of assigning companies owned by the State Treasury to particular NIFs. It was assumed that NIFs were to restructure enterprises designated for privatization, rather than to copy the structures typical for the centrally planned economy.

The cooperation of the Office with the Ministry of Ownership Transformations with respect to the establishment of NIFs consisted in the preparation of lists of state-owned enterprises and companies participating in the Mass Privatization Program. While verifying the lists of enterprises assigned to particular NIFs, the Office evaluated the impact of their concentrations in a given NIF on restricting competition in a given relevant market and prepared the so-called "exclusion list" which enumerated enterprises and companies which should not have their controlling stock of shares in the same NIF. This was done in order to avoid a situation in which the funds have a sectoral character and cause excessive concentrations in relevant markets.

2.3 OWNERSHIP TRANSFORMATIONS

Controlling the transformation of state-owned enterprises into one-person State Treasury commercial code companies (it was the first step in a process of privatisation), companies owned by employees or *gminas* (communes), the Office frequently put forward that certain conditions had to be met before it approved the transformation. One of the basic criteria for giving (or not giving) a transformation the green light was its potential impact on the state and development of competition in a given relevant market.

For instance, the Office played a very active role in the process of communalisation of the State Treasury property, which was an important element of the local government reform commenced in 1990. As part of that process, the AO issued conditional approvals for ownership transformations concerning, for example, the communalisation of enterprises in charge of residential and industrial waste disposal. The condition concerned developing competition by divesting of a dumping site[876]. An analysis of the Offices past decisions showed that the newly-created, private enterprises which were the competitors of the existing monopolist were forced to pay more for using dumping sites than those who used the services provided by waste disposal companies owned by *gminas*. This had a considerable impact on the prices of the services provided, making the new enterprises non-competitive. Through structural decisions of this kind, the Office tried to prevent creating favourable conditions for monopolistic practices and artificially increases of the prices for utility services. In 1992 alone, the President of the Office issued 141 decisions and notifications concerning transformations in the utility sector.[877]

Creating the legal possibility for establishing utility enterprises in the form of commercial code companies was aimed at rationalization of their activity and opening up the market related to these services to competition. The consequent demonopolization of the utility services market became inconvenient for many local government authorities and now there seems to be a tendency to

876 An example of a decision prohibiting the transformation when no separate space has been allotted for a dumping site is the decision concerning a motion from the City Council in Łódź. The decision states that due to the dominant position of MPO Łódź, maintaining the current organisational structure "...would allow the company to influence the prices of waste disposal services in the market" and that ..."an organisational merger of those two types of activity is an opportunity for funding waste disposal from the income generated by dumping sites and by means of a transfer of own costs onto the competitors. This enables an artificial increase of profitability of own waste disposal services and a decrease of prices of waste disposal in the market to such an extent that competition is eliminated due to unprofitability"(Decision Lodz.UA/DŁ/413-2/93/869/AK). Similar prohibition criteria are present in the decision UA-DK-412/25/92. Activities aimed at closing the market (price differentiation which discriminated the competitors of the municipal enterprise), referred to in the above mentioned motivation of the decision, were prohibited in the following decisions of the Office: DO-I-500/58/1200/91/HS, DP-500/193/230/ES. Activity of municipal enterprises and *gminas* which restricts competition in the waste collection and disposal sector is still common practice, as can be evidenced by the decisions of the President of UOKIK of 2009 RWR 30/2009, RWR 5/2009). In both cases the competitors of municipal enterprises were forced to pay more for dumping of waste than municipal enterprises. This makes the strategy adopted in early 1990s (separating the dumping site from the structure of municipal enterprises dealing with waste collection) perfectly justified.

877 Raport of the Antimonopoly Office..., op. cit.

withdraw from this idea. It is now being replaced by the concept of "regulated competition", or closing the market for competition in order to protect utility companies, treated by local government authorities as an area of their exclusive economic and political influence. In most cases, utility companies have the status of commercial code companies. However, the way in which provision of services is commissioned to them and the way in which the remuneration they are supposed to receive is established give them the character enterprises owned by the local government.

Summing up the activity the Office related to exercising its powers laid down in Articles 11 and 12 of the Antimonopoly Act, in 1990–1993 the President of the Office issued a total of 2 443 structural decisions and notifications on the absence of reservations towards envisaged organisational and ownership changes[878]. 4 percent of the decisions (102 cases) concerned conditional approval for transformation, 1 percent (28 cases) concerned bans on transformation and almost 1 percent (21 cases) concerned division of enterprises. The above data shows that 88 percent of the Office's activity consisted in monitoring structural changes and issuing notifications on absence of reservations to envisaged transformations or setting up of new enterprises. Merger and acquisition control was a negligible part of the Office's activity as, for instance, in 1992, decisions of this kind accounted only for 2 percent of the total number of decisions and notifications.

2.4 LIBERALISATION OF IMPORTS

The Office's involvement in liberalisation of imports stemmed from its strategy of demonopolizing the economy. Owing to liberalization, better quality products (compared to national products) appeared on the Polish market. We also saw the emergence of new products, previously unknown to the Polish consumer (complementary imports). For instance, in early 1990s much controversy and political discussions were spurred by imports of mineral water and dairy products (yoghurts, cream cheese, fruit and milk mousses). Demand for these products created by complementary import encouraged domestic entrepreneurs to produce these products and today Polish consumers may choose from a wide range of domestic mineral waters and tasty high quality dairy products.

878 Raport of the Antimonopoly Office..., op. cit.

Activities performed in order to liberalize imports were an important instrument for demonopolization of the economy and were one of the priorities of the AO since its inception. The Office's representatives participated in the works of the Inter-ministerial Committee for Updating and Modifying Import Tariffs and in the works of units developing the rules and criteria for the introduction of import quotas and import concessions. The role of the AO's representatives consisted in reviewing projects related to modification of tariffs in order to assess their value with regard to the development of competition in the Polish market.

While performing the reviews, the Office presented arguments against excessive protection of the Polish market against competitive imports, in particular in relation to these product markets which were characterized by a high level of monopolization. The arguments in question were the result of the monitoring activities performed by the AO with a view to establish the existing level of competition in monopolized markets (in 1993, entities holding a market share exceeding 80 percent were found in 177 relevant markets).

2.5 COMPETITION POLICY PROGRAMS

It should be noted that the more pro-competitive Polish economic policy was becoming, the pro-competition and pro-efficiency argumentation of the Office was gaining more momentum. Every two years, the Office prepared and submitted competition development programs to the Council of Ministers. The first one was adopted by the government in May 1991. This program and the ones that followed contained tasks for the government institutions along with deadlines for their fulfillment. The Office would then submit reports on the implementation of the programs to the Council of Ministers. Even if not all tasks were carried out, the programs had an important impact in terms of influencing the public opinion and educating the public administration.

The demonopolization of the economy carried out by the AO was an important element in the process of reforms of the economy. Organizational and ownership transformations were carried out by relevant ministers and *voivodes* (governors of provinces) who cooperated with the AO. Only in 1990, 188 enterprises were divided and 784 enterprises were established on the basis of the formers' assets[879].

879 A. Cylwik, *Ekspertyza dla Rady Strategii Społeczno-Gospodarczej przy R.M. nt. „Organizacyjnej i finansowej koncentracji gospodarki w obliczu prywatyzacji"*, Biuletyn Urzędu Antymonopolowego, Warszawa 1996, Year III, No. 9-10.

As a result of these activities and actions taken by entrepreneurs, in 1989–1994, the structure of the economy changed radically.

In 1989, the number of private commercial code companies stood at 15 252, whereas there were 813 145 economic operators without legal personality. In 1994, these data stood at over 70 thousand and 1 924 230,[880] respectively.

3. HOW EFFECTIVE WERE THE PREVENTIVE MEASURES UNDERTAKEN TO COMBAT MONOPOLISTIC PRACTICES?

Poland was the first country in Central and Eastern Europe to have introduced competition law. What is more, it also established a central administration authority in charge of the implementation of this law. It was expected at the time that the AO would be in charge of price control. One needs to bear in mind that in 1989 inflation stood at 700 percent and in 1990 it would increase by several percent monthly. However, it was not the AO's strategy to transform itself into an office in charge of price control, even though many countries undergoing political transformation and drafting its competition regulations were interested in assigning this function to their competition authorities.

Giving the AO a broader scope of responsibilities than mere price control made sense in the light of the experiences of countries which had not had a 40-year-long break in the functioning of market economy. Since its inception, the AO was learning its lessons from cooperation with experts from the OECD, the US Federal Trade Commission and the US Department of Justice. After the end of the negotiations on the Association Agreement between the Polish government and the European Commission in 1991, the AO started to cooperate with the European Commission's Directorate-General for Competition, as well as with the competition authorities from EU Member States.

In 1990–1993, the President of the AO issued 139 decisions against monopolistic practices. [881] When evaluating the effectiveness of the AO's activity, it is particularly worth to note four decisions (out of many others) aimed against abuses of a dominant position by companies and against cartel agreements.

880 A. Cylwik, *Ekspertyza dla Rady Strategii Społeczno-Gospodarczej przy R.M. nt. „Organizacyjnej i finansowej koncentracji gospodarki w obliczu prywatyzacji"*, Biuletyn Urzędu Antymonopolowego, Warszawa 1996, Year III, No. 9-10.

881 Report on the activity of the Antimonopoly Office in 1992, Warszawa 1993; Information on the activity of the Antimonopoly Office in 1993, Warszawa 1994.

The first of those four decisions, issued in October 1990 concerned monopolistic prices policy of FSO, a car manufacturer, in Warsaw[882]. The second one dates back to 1993 and concerned the practices imposed by Telekomunikacja Polska S.A. (TP S.A. – telecommunications operator). Although both of these decisions concerned pricing practices (Article 4(1)(1) of the Antimonopoly Act), it has to be admitted that the AO still continued to avoid price control. Even though the reason why the proceedings were instituted in the first place was anticompetitive price policy of the companies, decisions of this kind were accompanied by the AO's activities aimed at systemic changes preventing practices of this kind in the future.

3.1 COUNTERACTING THE ABUSE OF A DOMINANT POSITION

The first of the above decisions concerned the activitiy of FSO, which was at that time the only manufacturer and the dominant seller of medium volume engine cars. In January–June 1990, FSO had the dominant position in the national market of medium volume engine cars. The enterprise's market share was 70 percent without taking into account individual imports of cars because purchases of this kind were made outside of the Polish market. The antitrust investigation conducted by the Office revealed that FSO imposed monopolistic practices consisting in: "... restricting, despite its capacity, of the production of cars of such makes as FSO 1500 and Polonez, which was aimed at increasing their prices". In the second quarter of 1990, FSO increased the price of FSO 1500 three times, by 25 percent in total, while the price of Polonez increased twice – by 24 percent in total. The Office failed to find any economic rationale for these price increases and interpreted this as the abuse of a dominant position by FSO.

The decision issued by the AO ordering FSO to lower the prices of its cars was accompanied by a motion submitted to the Council of Ministers for a suspension of tariffs for this type of cars. The Council of Ministers decided that customs duty should be lowered by 70 percent and in 1991 the imports of medium volume engine cars was three times higher than the national production, which created competition on the market. Due to constant development of competition, there was no need to interfere in the medium volume engine car market any further.

882 Decision of the President UADO-I-644/37/90/HS, Biuletyn Urzędu Antymonopolowego, Trial issue. September, 1993, p. 46-47.

The more pro-competitive government and parliamentary economic policies become, the greater the effectiveness of the implementation of competition law. This was very adequately put in the justification of the decision issued by the Supreme Court considering a final appeal lodged by the Minister of Justice in the FSO case[883]. Upholding the judgment of the Antimonopoly Court which rejected the decision of the AO, the Supreme Court stated that there are inconsistencies in the actions taken by the central administration bodies. On the one hand, the national manufacturer was protected by the government by customs duty and, on the other hand, the government authority prohibits the enterprise from taking actions which follow logically from protection of this kind. This approach was used in decisions taken by the Office in other cases (e.g.: FIAT AUTO – Poland[884], a price fixing agreement between producers of fertilizers [885]) and was also used as justification for giving up proceedings against enterprises protected by administrative barriers against national and foreign competition.

The requirement of the coherence of actions taken by governmental agencies to encourage competition while increasing the competitiveness of the economy did not always translate into a more pro-competitive macroeconomic policy. Such a consensus was frequently difficult to achieve in practice, especially in the process of economic transformation. For instance, negative external effects of employment restructuring (increase of unemployment) or environmental protection (increase of production costs) hampered the process of change for economic, social and political reasons.

The second mentioned decision concerned an economically unjustified differentiation of telecommunication tariffs in local, long-distance and international markets. The differentiation of tariffs consisted in a substantial decrease of tariffs in local markets and an increase in international markets. At the time, first local networks operators obtained licenses to operate and by decreasing its local tariff, Telekomunikacja Polska S.A. (TP) tried to close relevant markets for potential competitors. The prices were extremely low, or "predatory", and they were aimed at restricting competition.

883 Judgment of the Supreme Court III CRN 120/91, Biuletyn Urzędu Antymonopolowego, Trial issue. September, 1993, p. 46-47.

884 Decision of the President of the Antimonopoly Office DO-II-50-S/5/94/57/HS, Judgement of the Voivodeship Court – Antimonopoly Court XVII Amr 9/95, Biuletyn Urzędu Antymonopolowego, Warszawa, Year II, 1995, No. 6, p. 42-55.

885 Decision of the President of the Antimonopoly Office DO-II-50/S/2/94/DG, Biuletyn Urzędu Antymonopolowego, Warszawa, Year I, 1994 No. 3, p. 26-31.

The legal monopoly that TP enjoyed in the long-distance and international calls market allowed the company to use cross-subsidies, which itself constitutes an anticompetitive practice usually connected with predatory pricing. The investigation and the decision were brought about negative publicity for the AO. It was necessary to explain TP's clients why the AO was against reducing local tariffs (!). A lot of work was done in order to clarify this issue.

The relevant markets concerned by the above mentioned decisions differed and still substantially differ in terms of competition and the market behavior of companies resulted from the level of competition in relevant markets. In the medium volume engine car market, competition has been existed for many years with all the beneficial (from the clients' point of view) consequences following from these processes. In contrast to the car market, the telecommunications market has seen the emergence of adequate conditions for the development of competition only recently. This is due to firm actions taken by the sector regulator (the Office of Electronic Communications), new fixed-line telephone operators entering the market, and as well as competition on the part of mobile phone operators.

3.2 PREVENTION OF CARTELS

In the early days of AO's activity (1990–1993), 55 administrative investigations were conducted against anticompetitive agreements, which accounted for 13 percent of the total number of investigations concerning monopolistic practices[886]. Only in 6 cases, the investigations concerned charges related to pricing agreements (Article 4(2)(1) of the Antimonopoly Act). In 1991 the President of the AO issued a decision following from such an investigation and concerning a price fixing agreement by sugar producers[887]. A decision on a price fixing agreement concerning prices of nitric and phosphoric fertilizers issued in 1994, is also worthy of note[888].

The investigation concerning price fixing collusion in the sugar sector was launched as a result of information submitted by a confectionary producer, who was informed by his sugar supplier about a national price fixing agreement concluded by directors of sugar producers and concerning the basic price of sugar. Enclosed with the letter was an excerpt from the minutes of a meeting in which the pricing agreement was a mentioned.

886 Report of the Antimonopoly Office 1990-1993, Warszawa, January 1994, p. 28-30.

887 Decision of the President of the Antimonopoly Office DO-I-500/26/91/JC.

888 Decision of the President of the Antimonopoly Office DO-I-50/S/2/94/DG.

In the course of the investigation concerning all Polish sugar producers (70), the Office did not receive any documents which would prove the fact that a pricing agreement had been concluded. All sugar producers under investigation claimed that no such agreement had ever been concluded. On the basis of an analysis of sugar prices in 1991, the Office established that a single price of sugar was set only in the event of a production surplus and situations where the production costs incurred by sugar producers varied. Pricing arrangements were usually conducted in the course of meetings of the Sugar Industry Council. The Office found that 32 sugar producers participated in the scheme, banned it and then imposed fines in order to discourage others.

Sugar factories lodged an appeal against the AO's decision, which was, however, upheld by the Antimonopoly Court. The grounds for the judgment are of unprecedented character in Polish case law, as the Court said that given the absence of "direct evidence", the price fixing agreement may be proved "in an indirect manner, if any similarities in the actions taken by the economic entities or their associations are impossible to explain – taking account of all the premises – without assuming that they made a prior agreement concerning their behaviour in the market" [889].

The second of the above mentioned decisions is a result of an investigation conducted on the basis of motions submitted by a deputy *voivode* (a province's deputy governor), the president of NSZZ "Solidarność" and the Minister of Agriculture and Food Industry. The motions in question were submitted against producers of nitric and phosphoric fertilizers and motivated by uniform price increases of their products following a publication of a decision of the Council of Ministers on aid to farmers for the purchase of fertilizers.

The Office initiated an explanatory investigation concerning 15 national producers of fertilizers, following which it identified a group of producers whose prices and dates when these were introduced were similar. As a result of this investigation, the Office initiated the antitrust proceedings against four producers of fertilizers, one of which was the price leader. Copying the leader was brought up by the producers as a justification for similarities in their pricing policies. Upon detailed analysis of the time and scope of the price changes, the Office found that this could not have been the case of price leadership, as the time intervals between similar changes introduced by the enterprises were too small.

889 Judgement of the Antimonopoly Court of 1 March 1993, XVII Amr 37/92.

The Office found that in 1993 there was no clear indirect evidence for price fixing, but in 1994 three enterprises in particular clearly fixed prices. In the justification to its subsequent decision imposing fines on the participants of the agreement, the role of the Polish Chamber of Chemical Industry, the Minister of Industry and Commerce and the Minister of Finance and the Minister of Agriculture and Food Industry in organizing certain meetings was discussed. During these meetings the situation of producers of fertilizers was debated and suggestions as to how to improve their situation were made. Although it was never proved that representatives of government administration approved price fixing agreements, the Office used the results of the investigation to advocate liberalization of fertilizer imports, which were to foster competition in this market. In addition, on the basis of the facts gathered in the course of the investigation, in the future, the Office consistently refused to conduct similar proceedings if the market behaviour of enterprises resulted from an inspiration or protective measures of government administration. The above mentioned judgement of the Supreme Court concerning FSO was used as a justification for adopting this kind of approach. It drew attention to the necessity of maintaining coherence of actions of the general government.

4. WHAT WAS THE AO'S ROLE IN DEVELOPING A PRO-COMPETITION SYSTEM OF ECONOMIC LAW IN POLAND?

Since its inception, the Office has had an important role in the development of economic law. Two general principles were part of the AO's strategy: in the Antimonopoly Act there would be no mention of sectoral or ownership exemptions; and competition rules would be laid down in different acts of law where its creation and development might be threatened. Consequently, provisions aimed at protecting competition were introduced in different acts of law (legislative acts, implementing regulations), for example those concerning: NIFs, securities, telecommunications services or the energy sector.

Competition rules were introduced to the new economic system by means of three methods: drafting new legislative acts and implementing acts, drafting provisions fostering competition in legislative acts and implementing acts concerning different areas of the economy and reviewing legislative acts and implementing acts drafted by central government authorities.

The AO initiated the Act on counteracting unfair competition, which was prepared by prominent Polish experts and entered into force in 1993. The Office also prepared further amendments to the Act on counteracting monopolistic practices, as it wanted the act to be applied more efficiently. One of the important areas of the Office's activity was reviewing draft legislation and implementing acts prepared by the government. In the first year, as arranged between the relevant ministries, the Office would only receive acts containing direct references to competition. However, it soon turned out that provisions which at first glance seemed to have little to do with promotion or development of competition, may still be of relevance in this context.

An instance of this may be the amendment to the Act on the rules of authorizing food products for trade (1992). The first draft act stated that in each case, food products were to undergo tests before they were accepted for the market. However, the draft significantly discriminated against entities willing to market new imported products. If the results of the tests were negative, then the potential distributor was to cover their cost, while if the results were positive, the tests were financed by the government. However, for imported products, in both cases the tests were to be conducted at the expense of the entity which commissioned the tests. The Office considered this discriminatory and the provision was later removed from the amendment to the act.

5. CONCLUSION

From the perspective of the last 20 years and taking into account the nature of the practices that the Office of Competition and Consumer Protection (UOKiK) has to deal with, and the administrative pressure that it needs to face, it should be noted that in the early days of the AO's existence, the same problems emerged when it comes to sectoral scope of application of the Antimonopoly Act; not to mention the relatively unfavorable perception of the Office as an institution interfering not only in anticompetitive business activity but also in the activity of government. Both today and in the early days of the Office's existence from the ideological point of view, it was generally accepted that competition should be protected. However, none of the dominant companies or cartel participants wanted to accept applying competition rules to their own actions.

When trying to evaluate the sectoral scope of the AO's activity, it may be stated that all fields of the economy in which UOKiK's intervention is visible now were also the areas in which the AO tried to counteract monopoly practices. The sectoral structure of decision-making in the Office changed in the sense that competition developed in relevant markets and administrative interference is no longer necessary. Instances of markets of this kind include: medium volume and small volume engine car industry, meat products and toiletry. Combating monopolistic practices is still relevant in the following markets: utility services (in which competition is restricted by local governments), telecommunications, rail transport and wholesale trade of construction materials.

The AO had more powers than UOKiK in terms of influencing structure of the economy, which was helpful in eliminating structural causes of monopolistic practices. In the early years of transformation of the Polish economy, in many cases, activities of the AO were coherent to those undertaken by the government and enterprises themselves. However, when the AO stood by its pro-competition arguments alone, conservative approaches prevailed, restricting the development of competitive markets. The AO was involved in the negotiations on the Association Treaty and harmonization of the Polish competition law to the European standards, convinced that the accession of Poland to the European Union was going to entail enlargement of markets and foster competition benefiting Polish consumers and the entire economy.

David J. Gerber

GLOBALIZATION, EUROPEANIZATION AND COMPETITION LAW: LOCATING EUROPE, LOCATING POLAND

1. INTRODUCTION

Globalization has encouraged and supported the development of competition law in much of the world, especially on the global level, but the path of global competition law development faces uncertainties and conflicts. It has underscored a fundamental tension in global economic development. On the one hand, competition can produce major economic benefits everywhere, but, on the other hand, its benefits are distributed unevenly, and it can also cause harm. A global competition law regime can protect this productive process and enhance its benefits, but if it is inappropriately conceived or ineffectively implemented, it can also increase its potential for harm.

The current legal regime for global competition evolved under the very specific circumstances of the twentieth century, and it may not be adequate to meet some of the challenges of globalization in the twenty-first century. Since the beginnings of competition law more than a century ago, international jurisdictional principles that were developed to prevent wars in Europe have been used as the basis for treating transnational competition issues. With the renewal of globalization after the fall of the Soviet Union, the limitations of this jurisdiction-based regime have become increasingly apparent. Many new competition laws have been enacted, and enforcement efforts in most competition law regimes have been significantly increased. This has positive benefits for the protection of competition. Yet it also creates conflicts, tensions, uncertainties and costs, and the jurisdictional framework has limited capacity to deal with these problems.

Efforts have been made to create a more effective model for transnational competition. There has been progress, but the changes so far have failed to address fundamental shortcomings of the existing jurisdictional regime. As we shall see, there may be good reasons to pursue additional strategies. In particular, it is likely to be necessary to forge new legal relationships among states and international institutions that are designed to harness the potential of globalization's new political configurations and new technologies.

In this brief essay, I outline some of the forces of globalization as they impact global competition law development. I identify key themes, potentials and obstacles.[890] I then locate Europe and Poland within this set of forces.

2. GLOBALIZATION AND COMPETITION LAW DEVELOPMENT: NATIONAL LAWS AND GLOBAL MARKETS

The "turn to the market" that followed the fall of the Soviet Union has dramatically increased and intensified global competition. Economic globalization has combined with technological and communications advances to reduce or eliminate obstacles to transnational economic competition. Competition has become broader, deeper and more complex than anything previously experienced. It now involves more business decision makers making a broader range of decisions among more alternatives, and with potentially greater and more multifaceted effects on more societies. In short, it operates within a more complex and interrelated transnational economic system.

The new prominence of global competition has focused attention on competition law at both the international and national levels. If competition is important, then a law that can protect it is also important. On the national level, the number of states with competition laws has increased from some forty to over one hundred. In most of these regimes, the budgets for application and enforcement have also increased significantly during the past fifteen years, and the penalties for violating competition laws have often been considerably strengthened.

These rapid developments have occurred primarily among the new Member States of the European Union and in developing and recently-developed countries of Latin America, Asia and Africa. In the EU, new members were required as a condition of membership to adopt competition laws for the first time, or to reform their existing statutes to conform to the EU standards. In other parts of the world, competition law was of limited importance until the 1990s, but most states have now adopted competition laws and begun to develop enforcement institutions. In some cases these developments have been spurred by the need to meet the requirements of international lending institutions, but they have also been driven by a growing perception that a market economy requires a competition law regime

890 I develop these issues in far more detail in David J. Gerber, Global Competition: Law, Markets and Globalization (forthcoming, Oxford U. Press, March, 2010).

to protect it against distortions by dominant firms or through agreements among companies.

The increased attention to global competition has many benefits, but the increased intensity of global competition combines with increases in the number of competition laws and their enhanced enforcement to create some negative consequences. First, globalization can reduce the capacity of the current jurisdictionally-based competition law regime to detect and deter anticompetitive conduct on global markets. For example, it can make detection and the acquisition of evidence more difficult, because it increases the breadth and complexity of decisions on such markets as well as the ease with which information can be transmitted and evidence can be moved and concealed. Second, it tends to reduce a state's incentives to take enforcement action, not only because of the potentially high cost of such actions, but also because the effects within that jurisdiction of anticompetitive conduct relating to only a component in the value chain of a product that is produced in many countries may be limited. Moreover, the effects of anticompetitive conduct may extend to numerous other countries, leaving no single state with incentives to combat the conduct on its own (the so-called "free rider" effect). Third, in this context of intensive globalization, the greater number of competition laws and increases in enforcement can increase the potential for conflicts among jurisdictions, their likely intensity, the costs and difficulty of resolving them. There are more competition agencies, more trans-border transactions and more complex interrelationships within global markets.

The capacity of the jurisidictional system is limited, however, because it is *inherently national in scope and dynamics*. Its institutions are not neutral arbiters whose role is to take into account or reconcile divergent interests among states or to resolve conflicts resulting from them. Those institutions are responsive primarily or exclusively to domestic constituencies. In addition, the cost, delays and uncertainties associated with national litigation make them poorly suited to solve global jurisdictional conflicts. These and related problems have led to growing awareness of the limitations of the jurisdiction-based regime.

3. THE EVOLVING GLOBAL COMPETITION REGIME

Globalization and national and regional responses to globalization have raised profound questions about the current legal regime for global competition. The conflicts, uncertainties and costs of the current have made competition law for global markets a prominent and controversial issue. We look briefly at the evolution of that framework in order to reveal its dynamics and its influence.

3.1 THE JURISDICTIONAL REGIME FOR GLOBAL COMPETITION LAW

Efforts to develop competition law on the international level began to appear in the 1920s, and they came not from the US, but from Europe. They were based on the model that had been taking shape in Europe since the 1890s.[891] By the late 1920s there was widespread international concern about the effects of private restraints on global competition, and there was broad support for multinational efforts to combat these harms. The motivating idea was that the international community had to protect the process of global competition from constraints and abuses, because individual states could not effectively perform that function. Soon, however, depression and war submerged this initiative and suspended efforts to develop a multinational response to the problem.

In the wake of the Second World War, the project was revived when it was included in the proposals for an International Trade Organization (ITO) that were included in the Havana Charter. This ambitious project was part of the postwar efforts to create a more effective legal framework for the global economy that produced, among others, the International Monetary Fund and the World Bank. An agreement that would have created a global competition law regime was agreed by virtually all trading states, but the onset of the Cold War destroyed hopes for global economic development and led the US to withdraw support for the ITO. As a result, the agreement was not ratified. This led to more than four decades in which the idea of global competition was barely thinkable, and the image of multilateral cooperation in the competition law area was in almost total eclipse.

When the Cold War division of the world made a global competition law regime impossible, the only available legal mechanism for treating harm to worldwide competition was the basic jurisdictional framework that had been developed in the preceding centuries to avoid trans-border clashes between European monarchs. As gradually expanded in the second half of the twentieth century, this jurisdictional regime basically allows any state to apply its laws where it has a

891 I trace the development of competition law in Europe during the twentieth century in David J. Gerber, Law and Competition in Twentieth Century Europe: Protecting Prometheus (Oxford U. Press, 1998, pbk, 2001).

sufficient connection to the conduct involved, either because the conduct occurred within its territory, or because one or more of those engaging in the conduct is a national of the state, or – and this was the new element – where the conduct has sufficient effects within the state's territory. This framework allowed the US as the dominant economic and political power in the non-Communist world to take responsibility for dealing with threats to transnational competition, because for decades it was the only state that both wanted to enforce its competition law outside its own territory and also had the political and economic leverage to do this effectively.

Despite the enormous changes in the economic and political landscapes over the last two decades, this basic situation still exists today. A few governments, most notably the European Union, have joined the US in applying their statutes to conduct outside their territorial boundaries, but most lack both the political and economic leverage to do so. In effect, the jurisdictional regime for global competition *relies on national laws to provide competition rules for global markets*, but few states are in a position to use that jurisdictional authority. The result is that the US (and, to a lesser extent, the EU) provide the standards for global markets.

3.2 RESPONDING TO THE LIMITATIONS OF THE JURISDICTIONAL REGIME: COMMUNICATION AND ASSISTANCE

When a new wave of globalization began in the 1990s, the limitations of this regime for the protection of global competition became increasingly obvious. In the early 1990s, European Union leaders responded by pushing to include competition rules in the then newly-formed World Trade Organization. In essence, they revived the idea of a multilateral solution that had been submerged at the beginning of the Cold War. The US did not support the effort, however, and many developing countries opposed it. By 2003, the WTO had dropped the proposal.

With the abandonment of the WTO project, responses to globalization and the deficiencies of the jurisdictional regime focused on spreading competition law ideas among countries that had had little or no experience in this branch of law. Leading competition law regimes such as the US, the EU and Japan paid increasing attention to bilateral arrangements with such states. Often under the rubric of "technical assistance", these programs have sought to spread "donor" countries ideas and experiences. This communication and assistance strategy has also been pursued by international organizations. Institutions such as the ICN

(International Competition Network), the OECD (Organization for Economic Cooperation and Development) and UNCTAD (United Nations Conference on Trade and Development) have devised programs to disseminate information about competition law, to assist developing competition law regimes, and to develop communication networks among competition officials. These networks are intended to foster communication and relationships that will allow information to flow effectively within them and thereby increase the efficiency of competition law enforcement on a global basis. Many hope that such networks will enable the jurisdictional regime to function more effectively. These efforts have led to increasing contacts among officials, scholars and lawyers, especially between the United States and Europe.

3.3 CONVERGENCE AS STRATEGY

Discussion of more long-term responses to global competition law issues have so far centered on one or the other of two strategies – convergence or multilateral agreement. Networking and technical assistance efforts are often associated – usually vaguely – with the expectation that such efforts will lead to convergence among competition law systems around the world. In essence, "convergence" refers to the idea that competition law regimes will become increasingly similar over time. In particular, the ICN specifically seeks convergence around "best practices" in a variety of competition law domains, and it has done valuable work in this context. Many expect this process to lead to greater and more predictable enforcement of generally agreed rules. This is expected to significantly improve the capacity of the jurisdictional regime to deter anti-competitive conduct. Many assume further that convergence will move all competition law systems toward the US antitrust law model and the economics-based approach that it represents.

For now, convergence appears to be the central strategy for long-term responses to globalization, in large part because there is little apparent basis for agreement on a multilateral basis. Thus we look briefly at basic issues related to that strategy. In particular, we explore some of the assumptions about convergence as a long-term response to global economic integration.

Convergence as a strategy remains a somewhat elusive idea. There has been little systematic analysis of its basic components. It often appears as only a rather vague notion of increasing similarity. In order to talk meaningfully about convergence, however, there must be some means of identifying and conceptualizing differences among systems, and there must also be some means of measuring reductions in the differences or distances among regimes. This critical element of analysis is, however, seldom examined. Moreover, convergence implies movement toward a central point. Although many in the US and Europe assume that this central point is an economics-based system such as the one found in US antitrust law, the issue is rarely discussed openly, and many outside the US are not so sure that this should be the result of convergence. There is also little clarity about *what exactly is converging.* Discussions of convergence typically imply that convergence refers to the "operative rules" (or normative standards) of competition law and thus to outcomes reached in applying the law. Yet in competition law, the gap between operative rules and formal rules is often immense, and the discussions themselves usually refer only to the latter – e.g. what statutes say. Finally, there is often little explanation of what the mechanism of convergence might be – what factors can be expected to lead to similar outcomes. There is thus much work to be done in clarifying convergence ideas.

In evaluating convergence as a strategy, it is necessary to take into account the national experiences and perspectives that shape the interests, incentives and perspectives of those who will make the relevant decisions. The officials and leaders of states will make decisions related to convergence, and thus their incentives and perceptions will determine the extent to which convergence will occur as well as its timing and its forms. We look very briefly at these national experiences as they relate to efforts to respond to globalization.

US antitrust law has been at the center of the competition law world since the end of World War II, and it continues to play the central role in global competition law development. Countries everywhere have looked to the US in shaping their own decisions in the field, and US experience is the lens through which US officials, scholars and practitioners have viewed competition law in other countries and on the global level. This pre-eminent role of US antitrust law is based largely on the specific political and economic contexts of the second half of the twentieth century and on the dominant roles that the US economy and political system have played in them, but it is also related to the depth of US experience with competition issues and the richness of the case law and scholarly literature in the area. Ironically, however, US antitrust experience is highly unique and shares few similarities with other regimes. From the first US antitrust statute until the mid-1970s, the Federal courts developed the law through traditional case law methodology. Policy issues such as economic development and the international aspects of competition law seldom played roles. By the 1960s antitrust had, however, come to be perceived as a burden on the US economy, and during the 1970s a law and economics "revolution" began among legal scholars and in the courts that would within little more than a decade change the system to one in which economic methodology has become the central basis for antitrust norms. This has focused attention on cartels and reduced enforcement in most other areas. This trajectory has little in common with competition law development elsewhere.

The US antitrust system itself also differs in many fundamental ways from most other competition law regimes. It is, for example, an almost entirely court-driven model. The legislature has seldom played a significant role. Moreover, US antitrust is distinguished from virtually all other competition law regimes by the central role it gives to neo-classical economics and the prominence of private enforcement of the antitrust laws.

Competition law in Europe has had a very different trajectory that can give it an important role in global competition law. It began to develop around the turn of the twentieth century, but the cataclysms that inflicted Europe during the next half-century prevented significant development. After the Second World War, earlier ideas were revisited and new elements were added to create a distinctly European competition law "model." Initially centered in Germany, this model evolved rapidly both at the national level and in the context of European integration. It featured a central role for administrative decision-making, and at the substantive level it emphasized the need to combat the use of private economic power to restrict competition.

Over the last decade, some elements of this European model have moved toward the current US view of competition law. The changes have been primarily in substantive law, although in some areas European competition law remains very different from US law. In particular, the treatment of dominant enterprises in Europe differs significantly from US law. Procedurally, the European focus on administrative enforcement remains little changed, although the forces of globalization and Europeanization have focused greater attention on developing private enforcement in the future. As we note below, Europe has played important role in the development of competition law on the global level, and its role in the future will depend on decisions to be made over the next few years.

The newer players in the global competition arena will be central to the evolution of competition law on the global level, because the success of any global competition law strategy will depend on their support. Yet their needs and the factors that influence their capacity and willingness to develop competition law are often overlooked in the US and in Western Europe. Competition law experience in these countries is thin, and confidence in competition and in competition law is often weak. Virtually all such regimes have been significantly influenced by US and European experience and/or pressures. Moreover, in many cases, these countries have introduced competition law in response to pressures from Western institutions, in particular in order to meet the requirements for acquiring loans and other support from international financial institutions and Western governments.

Except for the newer Member States of the European Union, which have become part of the European system, competition law officials, scholars and political leaders in countries with newer competition legislation often ask whether they should follow these Western models and, if so, to what extent and with which adaptations. For them, the key issues are often how to create and maintain effective institutional mechanisms for protecting competition and for enhancing their own economic development. Given that such institutional structures are already in place in the US and the EU, and that economic development tends to play a less central role in competition law there, the newer players are often asking very different questions than those posed in the US and Europe, and from very different perspectives on competition, on law, and on globalization.

This brief review of the differences in experience and institutional perspectives suggests that convergence may be a more complicated and difficult process than some imagine. Moreover, even if significant convergence is achieved, this cannot by itself overcome the fundamental limitations and weaknesses of the jurisdictional regime. Wherever there are differences between systems, there will be potential for conflict, uncertainty, and increased costs for international business, and the jurisdictional regime provides few incentives for states to cooperate to reduce these effects and limited capacity to promote domestic support for competition law development.

3.4 THE POTENTIAL FOR MULTILATERAL COORDINATION

The other long-term strategy for responding to globalization and the limitations of the jurisdictional regime is some form of multilateral agreement. This would be a return to the earlier insight that effective protection of competition on global markets calls for coordinated international effort. Discussion of multilateral agreement in recent years has generally referred to either of two forms of agreement. One is inclusion of competition law within the current framework of the WTO; the other is some form of international antitrust "code". Both have significant limitations, and neither has found significant support.

One pressing task is, therefore, to develop forms of multilateral coordination that correspond more effectively to the pressures of globalization. Many factors enter into fashioning such a strategy, and I look at them more carefully elsewhere.[892] For our purposes here, however, it is important to note only that there is now a basis for developing such a strategy. Extensive experience in the US and Europe and growing recognition elsewhere of the potential contributions of competition law to economic development provide strong incentives for multilateral cooperation and a basis for confidence that an effective global competition law regime can be constructed.

A key to developing an effective multilateral strategy is likely to be its capacity to structure the relationships between national and international institutions and groups in ways that harness the interests of national institutions to support more effective global competition. It must, therefore, be adapted to the specific needs of worldwide development. Relying on pre-existing forms or subjecting global competition law to pre-existing institutional procedures is not likely to be effective. Time and flexibility are likely to be critically important in fashioning a successful strategy, because if used effectively, they can allow the obligations of states and the relationships among countries to be adapted to the process of global economic development. These features make possible a gradual alignment of national economic and political interests that is unlikely to occur without commitment to a common set of goals. An effective strategy will call for active support from all types of participants in the global economy.

4. LOCATING EUROPE: THE COMBINED IMPACT OF GLOBALIZATION AND EUROPEANIZATION

This essay is part of a volume celebrating the twentieth anniversary of the Polish Competition Authority, and thus it is important to locate Europe and, even more

892 See Gerber, supra, note 1.

specifically, Poland within this globalization scenario. In Europe, globalization and Europeanization have intertwined in complex ways that we are only beginning to understand. We look at the impact of globalization on European competition law, and the potential roles of Europe in future global competition law development. Globalization has led to changes in both the procedural and substantive aspects of European competition law. I will refer to them, respectively, as procedural and substantive modernization. They are closely related.

The combined processes of globalization and Europeanization that began in the 1990s shook the confidence of European competition officials and others in the competition law arrangements that had evolved in Europe. Awareness that the European integration process would soon encompass many new countries, most of which had long been part of the Soviet system, urged changes in the procedures of EU law. In particular, it called for reducing the central role of the European Commission in enforcing European competition rules. This combined with a perceived need to make competition law more efficient and to reduce regulatory burdens on EU businesses and make them more competitive on global markets.

These factors led to the procedural "modernization" of European competition law. In it, primary enforcement responsibilities for competition law were shifted from Brussels to the Member States. At the same time, however, the new arrangement required for the first time that national authorities apply EU competition law to most transactions that were not purely local. The practical effect of this step was to increase the role of European law and to reduce the role of national competition laws. A European competition law network made up of national competition authorities and the Commission was created that has allowed Brussels to coordinate these enforcement efforts throughout the EU. These "modernizations" have significantly increased the role of Member State governments in enforcement, but they have considerably reduced the independent importance of national regimes and thus the potential impact of each country on formulating and influencing competition policy.

This process of procedural modernization also encouraged the reform of EU substantive law. Here globalization forces were also central. In the late 1990s, a new set of top European competition law officials, many of whom were economists, began to move the substantive principles of EU competition law toward a more economics-based approach (often referred to as the "more economic approach") along the lines of US antitrust law. One justification for this move was to reduce regulatory burdens on European business and thereby improve their global competitiveness. In addition, US economic successes in the 1990s appeared to justify emulating US approaches to economic policy, including competition law policy. Beginning with the analysis of vertical agreements and expanding to mergers and horizontal agreements, this more economics-based form of competition law analysis significantly altered many of the basic principles of substantive law. The only major area in which it has not become prevailing is the treatment of dominant firms. Globalization's effect on competition law in Europe – both procedural and substantive – has thus been profound.

At the same time, Europe's role on the global level has become less clear. Prior to the modernizations, many countries around the world, especially in Asia, viewed European competition law as an alternative to the US model. During the 1990s, there was a significant contest for the influence of their respective competition laws between the US and the EU in areas such as Latin America. Moreover, countries such as Korea and China have based their own systems to a significant extent on the original European model. As the substantive component of that model has lost some of its separate identity, Europe's role in relation to global competition law development has become less distinct. The future role of Europe in this respect thus remains to be newly defined, and EU decisions in this respect will be of major global importance.

Regardless of the *future* development of European policy, its *past* – the evolution of European competition law during the second half of the twentieth century – can be of great importance for many states seeking to develop their competition laws in the twenty-first century. European national systems have evolved under circumstances that have often been similar to those faced in many countries that seek to develop competition law in the twenty-first century. Their experience is therefore particularly valuable in identifying the issues and obstacles that these states encounter and in providing options and insights for overcoming these barriers. Another reason for its importance is that for decades European national competition laws have developed within the context of European integration, and this national-transnational experience highlights key issues in the development of competition law for global markets. One impetus for my book *Law and Competition in Twentieth Century Europe* (OUP, 1998, 2001) was the realization that the dimensions and patterns of European national competition law experience had not been widely recognized and that they were often shrouded in myths and misunderstandings. As a result, their potential value to decision makers everywhere was not being realized. Although there have been successes in raising awareness of this experience, European experience remains undervalued in much thinking about global competition law development.

5. LOCATING POLAND: AN UNHEARD VOICE?

In one sense, of course, Poland's place in the story is so closely tied to that of Europe generally that it has limited independent importance. This perspective expresses a European vision and the rhetoric of European integration, but it may also tend to underestimate the potential value of individual Member States in this context, particularly the new ones. The priorities and needs of these countries deserve attention in developing European competition law.

The potential importance of Poland's commitment to shaping European responses to globalization can be seen on two levels. One is formal and institutional and involves the Polish participation in European institutions. As recent events have shown, the politics of individual states remains important and sometimes even determinative in some areas of integration. Moreover, the potential roles of Polish officials in the European Commission deserve to be highlighted. The other level is less obvious, but no less important. The history of competition law everywhere shows that participation and political involvement are critical factors in promoting the development and effectiveness of this branch of law. Political leaders, officials, scholars and non-governmental organizations are likely to support competition law development only to the extent that they see value in it, participate in competition law decisions and have a voice in the direction of competition policy.

In my view, therefore, Poland can play very important roles in the development of European and competition law and global competition law development in general. From some perspectives, Europeanization and globalization appear to submerge the voices of individual states, and the needs of European integration require an emphasis on factors that unite rather than divide Europe. Within the UE, there must be coordination and cooperation, and in the competition law area, great progress has been made in achieving harmonization. Yet the voices of individual European states remain critical to the success of both competition law and European integration. Both the political institutions of the countries and individual politicians, officials and scholars reflect and identify economic and social needs in ways that need to be taken into account in the process of policy formulation as well as in the process of enforcement. Poland has been forced for centuries to muffle its voice. It has often suffered from the lack of any significant voice in the decisions that affect Polish people and institutions. The size and economic development of Poland, as well as its scientific and technological potential emphasize the potential value of listening to that voice.

6. CONCLUSION: PATHS FORWARD

Globalization has directed the attention of decision makers in many parts of the world to improving the legal protections against anti-competitive conduct. It has increased awareness of the potential value of economic competition and of the importance of providing an effective legal framework for it. In particular, there is growing awareness that trans-border competition in particular can generate economic growth and the jobs, income and public and private resources that are crucial everywhere, but that are desperately needed by so many. The need to provide an effective legal framework for global competition has also become increasingly obvious, and the financial crisis of 2008 has further emphasized its importance.

Increasing recognition of the deficiencies in the current jurisdictional system has led to valuable efforts to respond to them. Groups such as the International Competition Network, the OECD and UNCTAD have been laying the foundations for development of a more effective legal framework for global competition, but fundamental changes in this direction have yet to be made. In my view, this provides a valuable window of opportunity for scholars, competition officials and political leaders from all EU Member States to provide insight into the forces that will influence the effectiveness of competition law arrangements on the global level. As of now, our knowledge of competition law experience in many parts of the world is thin and awareness of the range of policy options and the likely consequences of choosing those options may be too narrow and too poorly understood. This greatly enhances the risk of making decisions solely or primarily on the basis of short-term political and economic power considerations. Above all, it is critically important that the voices of countries with differing backgrounds and needs be included in the discussion, and in this context I expect the work of Polish officials and scholars to be of major importance.

Stanisław Gronowski

COMPETITION JUDICIARY IN POLAND

1. INTRODUCTION

There is no international agreement which would generally standardise Polish obligations in terms of national judicial system and provisions regarding court proceedings. Minimum requirements in this respect are indicated in Article 6(1) of the Convention for the Protection of Human Rights and Fundamental Freedoms[893], which states that courts shall be established by law, be fair, independent and impartial as well as that it shall guarantee the cognisance of a case in a reasonable period of time.

Accession to the European Union did not impose formal obligations on Poland regarding the judiciary, because these are not included in the Community law. However, in order to implement Community law, the Court of Justice of the European Union in its case law created foundations for the concept of procedural autonomy of EU Member States[894]. In light of the judgement of the Court of Justice of the European Union of 16 December 1976 Ref 33/76, it is up to the internal legal system to regulate the jurisdiction and procedural rules in order to ensure that individuals' rights resulting from directly enforceable law are protected. Procedural autonomy is of conditional nature, it comes into play when there is no appropriate Community legislation. However, it does not have the status of a general principle of Community law. It is rather a legal concept (acknowledged standard, doctrine) derived from Article 10 of the EC Treaty. It is of open nature, because it is constantly redefined in order to ensure efficient application of Community law[895].

The judiciary is an element of the system of public authorities. Article 7 of the Polish Constitution provides that public authorities operate on the basis and within the limits laid down by law, while Article 2 provides that the Republic of Poland is a democratic state ruled by law and implementing the principles of social justice.

893 Dz.U. of 1993 No 61, item 284 as amended.

894 See: Z. Kmieciak, *Zasada autonomii proceduralnej państw członkowskich UE i jej konsekwencje dla procesu orzekania przez sądy administracyjne i organy administracji publicznej*, „Zeszyty Naukowe Sądownictwa Administracyjnego", year V, No 2(23)/2009, p. 9.

895 See: A. Wróbel, *Autonomia proceduralna państw członkowskich. Zasada efektywności i zasada efektywnej ochrony sądowej w prawie Unii Europejskiej*, „Ruch Prawniczy, Ekonomiczny i Socjologiczny" 2005, No 1, p. 35.

While there is no doubt regarding the obligation of courts to apply law, it might be debatable whether and to what extent a court can justify its decision pleading social justice referred to in Article 2. The term "social justice" is a formal term used in legal language[896], "justice" is not. However, it does not mean and there is no reason for citizens to take a court's decision as unjust due to the above. The lawmakers, at least in a state under the rule of law, strive for the law applicable by courts to be correspond to the principles of justice.[897] Some positive examples can be seen in the legislation on competition and consumer protection. Thus, with the help of Aristotle, who distinguished between commutative and distributive justice, Article 9(2)(1) of the Polish Act on competition and consumer protection of 2007 adopts the principle of commutative justice, which states that a product should be purchased for a price not lower than the cost of its making. Similarly, the postulate of distributive justice, which states that every person participating in the production of a given product should receive part of the income generated by the product, proportionally to his or her contribution, is included in Article 8(1)(2) of the Act.

The connection between law and justice can event be seen in the Latin etymology of these two words, with *justitia* (justice) deriving from *jus* (law). However, with regard to Article 2 of the Polish Constitution, it would be far-reaching to consider "social justice" as a legal principle, and especially a basis for granting a specific right to an individual. "Principles of social justice" or "principles of social coexistence", even if they are defined as specific rules of conduct, do not become, strictly speaking, applicable legal principles, but indicate the direction for using legislative powers.[898] In the doctrine of constitutional law, the "principle of social justice" is denied legislative value unlike other principles included in Chapter I of the Polish Constitution and considered constitutional norms. These principles are also not recognised as a general clause, because they do no refer to any specified system of assessment.[899] For the above-mentioned reasons, the implementation of the "principle of social justice" is not the task of courts, including the Court of Competition and Consumer Protection, but the task of authorities which shape the legislative processes, including the Constitutional Tribunal.

896 See: Z. Ziembiński, *Sprawiedliwość społeczna jako pojęcie prawne*, Warszawa 1996, pp. 7-9.

897 The *aequitas sequitur legem* rule.

898 Cf. Z. Ziembiński, op. cit, p. 52.

899 Cf. J. Karp, *Sprawiedliwość społeczna. Szkice ze współczesnej teorii konstytucjonalizmu i praktyki polskiego prawa ustrojowego*, Kraków 2004, p. 166.

2. CONSTITUTIONAL RULES CONCERNING THE JUDICIARY

In the Polish law, the role and place of the judiciary results from the constitutional principles of the Republic of Poland, which are based on the separation and balance between the legislative, executive and judiciary. Pursuant to Article 10 of the Polish Constitution, judicia power is exercised by courts and tribunals. The most important constitutional principles defining the nature of judicial power are:

- judicial independence (Article 178(1) of the Polish Constitution),
- subjecting judicial power solely to law (Article 178(1) of the Polish Constitution) and not political criteria of purposefulness or efficiency which are the basis for the operation of other authorities,
- entrusting the judiciary with the power to decide on cases and disputes arising in the process of applying or adopting law,
- basing operations of the judiciary on formalized procedures which strongly emphasise the *inter partes* rule[900].

The Polish Constitution guarantees that the Polish judiciary fulfils standards applicable to the judiciary in a state ruled by law. For example, Article 45(1) of the Constitution provides that everyone has the right to a fair and public hearing of his case, without undue delay, before a competent, independent and impartial court. Further provisions elaborate on this general wording. For example, Article 77(2) prohibits refusal of court proceedings in pursuit of claims alleging infringement of freedoms or rights.; Article 78 ensures parties the right to challenge judgements and decisions issued by courts of first instance; Article 173 emphasizes the independence of courts and tribunals from other authorities; Article 176 indicates that court proceedings have at least two stages and the system and jurisdiction of courts as well as court procedures are defined by statues; Article 177 stipulates that courts have exclusive right to exercise judicial power; and Article 178(1) contains the principle of judicial discretion[901]. All these constitutional requirements are met by Polish courts, including those hearing competition and consumer protection cases.

900 L. Garlicki, *Polskie prawo konstytucyjne*, *Zarys wykładu*, Warszawa 2001, p. 351.

901 T. Woś, H. Knysiak-Molczyk, M. Romańska, *Postępowanie sądowo-administracyjne*, Warszawa 2004, p. 17.

The monopoly of courts to exercise judicial power does not at all result in the obligation to hear all cases in which individuals participate, starting at the earliest stage of the dispute. The state's monopoly to exercise judicial power does not exclude the possibility for other bodies, also non-state ones, created for deciding in legal disputes, to act, if regular statues provide for such possibility[902]. However, this mode of proceeding should be based on the assumption that if a decision issued by a non- judicial body is challenged in a court of law, the court's task is to continue with a case initiated in administrative proceedings and not exercise control over the operations of public administration as set forth in Article 184 of the Constitution[903]. Such situation occurs in the case of proceedings before the President of the Office of Competition and Consumer Protection (UOKiK)[904], whose decision may be appealed against to the Court of Competition and Consumer Protection, which examines the case in substantial terms. Yet, the possibility to challenge a decision issued by a non-judicial body before an appropriate court is necessary and is thus guaranteed under the Polish law[905].

In light of Article 175(1) of the Polish Constitution, apart from the Supreme Court there are common courts of law and two types of special courts – administrative courts and military courts. The catalogue of court types cited in the Constitution is closed. Pursuant to Article 177 of the Constitution, common courts of law have jurisdiction in all cases except those statutorily reserved for other courts. Here, the position of common courts of law should be emphasised. Article 177 of the Constitution gives them general jurisdiction resulting. Thus, if it is impossible to determine which court should hear a case, it is presumed that it is the common court of law[906].

Pursuant to Article 184 of the Constitution, the Supreme Administrative Court and other administrative courts exercise control over the public administration's activities, as defined in the Act. This control also includes evaluating the conformity of local governments' resolutions and local public administration bodies' legal acts with statues. Pursuant to Article 177 read in concurrence with Article 184,

902 T. Ereciński, K. Weitz, *Efektywność ochrony prawnej udzielanej przez sądy w Polsce*, PS 2005/10/3.

903 R. Hauser, *Przekształcenie modelu polskiego sądownictwa administracyjnego*, "Forum Iuridicum" 2002, No 1, p. 97.

904 Consideration to statutory guarantees of independence of the President of UOKiK justifies recognition of this authority as "organisationally independent judicial authority" (cf. M. Szydło i Ł. Błaszczak, *Sprawa antymonopolowa jako przykład sprawy administracyjnej oraz sprawy gospodarczej*, PS 2005/7-8/118).

905 In relation to cases within the scope of competition and consumer protection this issue was regulated in provisions of Article 479^{28-35} of the Code of Civil Procedure.

906 J. Boć (in:) *Konstytucje Rzeczypospolitej oraz komentarz do Konstytucji RP z 1997 roku*, ed. J. Boć, Wrocław 1998, p. 277.

the constitutional presumption of common courts' jurisdiction in all cases except those statutorily reserved for other courts means that the Constitution itself reserves exercising control over the public administration's activities to administrative courts, and thus, excludes the jurisdiction of common courts of law in this respect[907]. The system of two instances of administrative judiciary is, as of 1 January 2004, laid down in the Act of 25 July 2002 – Law on the Structure of Administrative Courts[908], and proceedings before these courts are regulated by the Act of 30 August 2002 – Law on proceedings before Administrative Courts[909].

Judicial power is exercised by both common courts of law and administrative courts (Article 175 of the Polish Constitution). However, in light of the Constitution, there are differences regarding the scope of powers exercised by each type of courts, which influences the character of the control they exercise. Administrative courts exercise their powers by controlling the public administration activities and decisions in terms of their conformity with the law, unless legislative acts provide otherwise. Having found the challenged activity or decision inconsistent with the law, the court either overrules the decision or states its invalidity. The role of the administrative court ends here and the case returns to the public administration bodies, which act to reconsider the case or, if the decision was sustained – implement it[910]. The scope of common courts' jurisdiction goes beyond that – a common court decides on the case in substantive terms, i.e. regarding its very essence.

3. COMPETITION JUDICIARY IN HISTORIC TERMS

In the interwar period, despite the existence of administrative judiciary in Poland, the control over antitrust practices was given to the Cartel Court established by the Supreme Court. This was stipulated in the Act of 28 March 1933 on Cartels[911]. The Minister of Industry and Trade, whose powers included preventing cartels, was at first the public prosecutor before the Cartel Court. Then the minister obtained full powers to decide not only in the scope of imposing fines for violating the notification provisions, which he already had, but also in the scope of terminating cartel agreements or overruling appropriate resolutions. Proceedings before the Cartel Court were initiated on a motion from a party to the administrative

907 R. Hauser, op. cit. pp. 97-98.

908 Dz.U. No 153, item 1269 as amended.

909 Dz.U. No 153, item 1270 as amended.

910 J. Borkowski, *Ustawy o dwuinstancyjnym sądownictwie administracyjnym*, part I, „Monitor Prawniczy" 2003, No 7.

911 Dz.U. No 31, item 270, amendment of Dz.U. of 1935 N 86, item 529.

proceedings and an addressee of the decision of the Minister of Industry and Trade. The Cartel Court was composed of five members: three judges of the Supreme Court, one of which was its president, and two members, one selected from among candidates suggested by the Minister of Justice and the other out of those recommended by the Chamber of Industry and Trade in Warsaw. Decisions of the Cartel Court were final.

After the Second World War, under the Act of 28 January 1987 on monopolistic practices in the national economy[912], antitrust cases were at first heard by the Supreme Administrative Court (NSA). Decisions of the antitrust authority, i.e. the Minister of Finance, could be appealed under general principles to NSA in the case of their inconsistency with the law (Article 27(2)). The Supreme Administrative Court reviewed decisions of the antitrust authority in terms of their legality. Court and administrative proceedings had only one stage back then, with the possibility of extraordinary review before the Supreme Court through authorized bodies.

New quality in terms of the procedure of judicial review of decisions of the antitrust authority was introduced by the Act of 24 February 1990 on monopolistic practices and protection of consumer interests[913]. This Act created the Antimonopoly Court, operating by the Voivodeship (or Provincial) Court in Warsaw, i.e. within the system of common courts of law. Later it was renamed the Court of Competition and Consumer Protection (SOKiK) and the name is used to this day. Its activities are regulated by the Act on competition and consumer protection of 16 February 2007. When adjudicating an appeal against a decision of the antitrust authority, SOKiK has the same jurisdiction as the antitrust authority itself, because the court takes over the case for further consideration.

Handing over appeals against decisions of the antitrust authority to the special antitrust court operating within the system of common courts of law was connected with the court assuming the power to consider these cases in substantive terms. At that time it was quite an experiment. In those days (as well as at present) it was unusual for a common court of law to adjudicate on rights and duties of enterprises and other entities in cases arising from administrative law and which were previously decided by a public administration body. Indeed, SOKiK's judgements may potentially shape relations based on administrative law.

912 Dz.U. No 3, item 18 as amended.

913 Consolidated text. Dz.U. of 1999 No 52, item 547 as amended.

Proceedings before SOKiK follow procedures applicable to commercial cases. At first, the court was only a one-instance court, which was questioned in literature as inconsistent with the constitutional principle of two-instance court proceedings[914]. Finally, as a result of the decision of the Constitutional Tribunal of 12 June 2002[915], the second instance was introduced in 2004, which is the Court of Appeal in Warsaw.

Another issue related to SOKiK's structure, is the scope of its cognition, particularly, whether the court should consider the case from the beginning or are its tasks only of supervisory nature due to the case having been first investigated in administrative proceedings by the competition authority. There are examples in the practice of the court where it arrogated the above mentioned powers, limiting to a significant degree the scope of its cognition to controlling the legality of the decision made in administrative proceedings[916]. However, the jurisprudence of the Supreme Court, quite rightly, rejects the above position. According to the Supreme Court, as a court of first instance, SOKiK should adjudicate the case with regard to its substance starting from the very beginning[917]. The jurisprudence of the Court of Appeal in Warsaw adopts the same stance. Nevertheless, there should be no obstacles for SOKiK using the evidence collected in the competition authority's investigations in order to make its own determinations according to the requirements defined in Article 328(2) of the Code of Civil Procedure. However, and this should be emphasised, the nature of the proceedings before SOKiK significantly differs from proceedings before administrative courts, which issue judgements considering appeals from administrative authorities' decisions on the basis of the case file (Article 133(1) of the Law on proceedings before administrative courts) without conducting its own evidence proceedings.

4. PERSPECTIVES OF ANTITRUST JURISDICTION

In the context of the great reform of administrative judiciary in Poland, implemented on 1 January 2004, a question may arise whether it would be justified to hand over the judicial review of decisions of the competition authority

914 S. Gronowski, *Ustawa antymonopolowa*, *Komentarz*, Warszawa 1999, p. 294.

915 Ref P. 13/01, Dz.U. of 2002 No 84, item 764.

916 In the decision of the antitrust court of 8 May 2002, Ref XVII Ama 90/01, overruling the decision appealed against, SOKiK plead procedurally faulty act of the President of UOKiK resulting in stating invalidity of the decision under Article 156 (1) (2) of the CAP. Thus, SOKiK indirectly applied a control instrument of the administrative court envisaged in Article 145 (1)(2) of the Law on proceedings before administrative courts.

917 Cf. Judgement of the Supreme Court of 24 October 2002, ref. no. I CKN 1465/00, "LEX", No 75278.

and sector regulators, now reviewed by SOKiK, to administrative courts. Such proposals appear in the literature[918]. The shift, it seems, would closer correspond to the constitutional model in terms of separating the jurisdiction of common courts of law and administrative courts.[919] SOKiK now hears appeals against decisions of a public administration body (competition authority) while the control of such activity falls in principle within the jurisdiction of administrative courts. However, it should be taken into account that according to the Polish Constitution there are no obstacles for common courts of law to consider cases which were previously decided by a public administration body, as Article 184 states that the control over public administration activities is exercised by the Supreme Administrative Court and other administrative courts within the scope defined in statues.

The previous Act on competition and consumer protection lacked reasons for handing over such cases to administrative courts. Competition protection cases handled by the competition authority were not exactly conducted in the public interest, which to some degree could be an argument in favour of reviewing them by an administrative court. Although Article 1(1) of the previous competition act defined its objective as the protection of the public interest against market monopolisation, it was indicated that interests of enterprises and consumers will also be protected. Moreover, enterprises and consumer organisations were given the right to bring up cases concerning competition-restricting practices and could be party to such proceedings. Consequently, the number of such cases exceeded the number of those initiated ex officio and as a result the competition authority frequently decided disputes of economic nature between enterprises arising in connection with abuses of market power.

From the point of view of the interests of enterprises whose disputes are heard by the competition authority, it would be more favourable if decisions in these cases were reviewed by a court with procedural instruments appropriate to evaluate the cases in terms of their substance. SOKiK has been such a court. Administrative courts are not normatively prepared to exercise such a far-reaching control as in principle they examine cases in terms of their legality and thus are not equipped with proper procedural instruments for verifying administrative decisions in terms of their substance.

918 W. Broniewicz, *Czy potrzebny jest nowy kodeks postępowania cywilnego*, “Państwo i Prawo” 2004/4/11.

919 Cf. S. Gronowski, *Sądownictwo z zakresu ochrony konkurencji w Polsce (wybrane problemy)* (in:) *Prawo konkurencji - stan obecny oraz przewidywane kierunki zmian*, ed. C. Banasiński, Warszawa 2006, p. 17.

The new Act on competition and consumer protection of 2007 (Article 49(1)) deprived enterprises and their associations as well as consumer organisations of the right to bring up cases considering competition-restricting practices, infringements of consumer collective interests and pertaining to the imposition of fines before the competition authority. Such proceedings may be initiated only ex officio. Thus, proceedings before the competition authority are to a great degree of an inquisition nature. The antitrust authority acts to protect enterprises and consumers in the public interest to a significantly greater degree than it was the case under the previous act. The authority is no longer involved in deciding disputes of economic nature between enterprises.

The Act of 2007 provides more grounds for considering the potential handing over of judicial review of the competition authority's decisions concerning competition and consumer protection to administrative courts, due to the fact that now the competition authority's administrative proceedings can only be initiated ex officio, i.e. in the public interest. Nevertheless, the need for changing the model of judicial review over the decisions of the competition authority does not seem so evident. Competition-restricting practices occur most frequently in the area of civil-law agreements. Traditionally, the control over such agreement falls within the competence of common courts of law. Undoubtedly as it seems, common courts of law have greater experience and possibilities for considering such cases of civil-law nature than administrative courts, whose powers in principle consist in examining the legality of administrative decisions and not deciding on their substance. Moreover, the nature of SOKiK as a court which considers cases as to their substance, can also be significant from the point of view of the functioning of Poland in the EU structures. Member States in general use the model of administrative review of competition cases, which is, nevertheless, based on their substantial consideration.

Undoubtedly, a potential change of the current model of judicial review of decisions of the competition authority would be connected not only with the change of the role of the court in exercising its jurisdiction, but would also impose new procedural obligation on parties. For example, currently a decision of the competition authority issued in the first and – what is important – the only instance can be appealed against to SOKiK. Whereas the administrative court procedure, according to the general principle of two-instance administrative proceedings (Article 15 and Article 127(3) of the Code of Administrative Proceedings), requires exhausting all means of appeal before filing a complaint to the administrative court[920]. As a result, from the perspective of enterprises, the potential handing over of the discussed cases to administrative courts does not guarantee speeding up of the proceedings. Moreover, it can be assumed that due to the fact that administrative courts do not conduct their own evidence proceedings, all shortcomings in terms of evidence which occur at the stage of administrative proceedings would likely cause the appealed decision to be overruled, which in turn can even prolong the case. At the same time, SOKiK to issue its judgement has the obligation to make all essential determinations in the case, gathering evidence if it is necessary. The Court of Appeal has a similar obligation (see Article 382 of the Code of Civil Procedure). There are no analogous regulations applying to proceedings before administrative courts and there seems to be no need for their potential introduction, especially if this should only serve taking over competition cases for consideration.

5. OTHER COURTS

Common courts of law, especially SOKiK, have been considering competition cases for 20 years. During this time they have managed to accumulate great judicial experience, organize expert judges (also in the Court of Appeal in Warsaw and in the Supreme Court) and formulate case law as regards many issues. If these cases were taken away from common courts and handed over to administrative ones a great deal of work would be wasted to a great degree. There is no guarantee that administrative courts, at least with their current jurisdiction, would ensure better judicial review of decisions of the competition authority than the common courts.

Counteracting competition restricting practices in administrative procedure before the competition authority does not exhaust all possibilities for protecting rights of persons affected by these practices in civil proceedings before an appropriate court. It pertains especially to the situation where the claimant justifies his claims with the unlawfulness of a agreement or an act manifesting the abuse of a dominant position. In the event that the effects of competition restricting practices applied by an enterprise affect another enterprise, the civil action brought by the harmed firm to court would be an economic case within the wording of Article 479^1(1) of the Code of Civil Procedure.

920 Cf. Article 52 of the Law on proceedings before administrative courts.

In a situation where the effects of competition restricting practices affect a consumer, i.e. a natural person acting outside the scope of his or her business or professional activity, than the consumer's action will be heard by the civil department of the appropriate civil court.

If a consumer was harmed (or may be harmed) by a competition restricting practice as a result of entering into an business-to-consumer agreement which includes unlawful clauses (Article 385^{1-3} of the Code of Civil Procedure), the consumer's interests may be protected under regulations concerning recognising standard form contracts as unlawful before the appropriate court, which in this case is SOKiK (Article 479^{36} of the Code of Civil Procedure).

In connection with the possibility for private entities harmed by competition restricting practices to seek redress in civil proceedings (before a commercial court), another problem arises. Are only bodies operating under the Act on competition and consumer protection (competition authority and SOKiK) are authorised to decide if a given conduct is a competition restricting practice, binding other bodies, including courts, by the decision, or may civil courts (commercial courts) also make decisions of this kind when considering relevant civil actions. According to the judgement of the Supreme Court of 22 February 1994, Ref I CRN 238/93[921], the civil court may initially determine whether the conduct which is the factual basis for the claim is a competition restricting practice for the purpose of considering the case,. This position was criticised in literature. A different opinion was expressed in the resolution of the Supreme Court of 27 October 1995, Ref III CZP 135/95[922]. The court claimed that finding an agreement void due to violation of the Act on competition and consumer protection may be a prerequisite for deciding a civil case, yet bodies mentioned in the Act must first recognise the conduct as anti-competitive. Subsequent decisions of the Supreme Court follow that line[923]. However, this position, as it seems, will have to change in light of the 2007 Act on competition and consumer protection. The current legislation does not give enterprises, their associations or consumer organisations the right to bring cases

921 "Państwo i Prawo", 1995, No 7, with gloss by T. Ławicki.

922 "Orzecznictwo Sądów Polskich" 1996, No 6, item 112, with gloss by S. Gronowski.

923 In the judgement of the Supreme Court of 7 November 1997, Ref II CKN 424/97, OSNCP 1998, No 5, item 77, the decision of the Antimonopoly Office was plead, in the light of which the manifestation of monopolistic practice was the imposition on a customer of a free of charge handing over of power devices mentioned in Article 49 of the Civil Code, to financial circumstances of the entrepreneur from the power sector, which renders such an agreement invalid (Article 8 (2) of the Act on monopolistic practices and protection of consumer interests). As a result, the Supreme Court decided that the recipient of energy can claim reimbursement of incurred costs under provisions on unjust enrichment.

concerning competition restricting practices, infringements of collective consumer interests and the imposition of fines to the competition authority, because now such investigations can only be initiated ex officio (Article 49(1) of the Act). Thus, enterprises and consumers harmed by competition restricting practices can now seek redress only before civil courts. In this situation, without incurring the risk of violating Article 77(2) of the Polish Constitution, which states that a statue cannot deny anyone the right to seek redress in court if his or her rights or freedoms were violated, the civil court (commercial court) will no longer be able to evade determining independently whether the conduct which is the factual basis of the claim indeed violates the Act on competition and consumer protection. Moreover, we should also note that Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty[924] stipulates that national courts have the obligation to apply Articles 81 and 82 of the EC Treaty (point 7 of the preamble and Article 6). Thus, the civil court (commercial court) is authorised to conduct all procedural activities envisaged by the law and connected with considering a given case.

924 OJ L 03.1.1, p. 1–25, OJ L-sp.08-2-205.

Knut Eggum Johansen and Kjell J. Sunnevåg

UNDERSTANDING THE MARKETS FOR SERVICES OFFERED VIA ELECTRONIC NETWORKS[925]

1. INTRODUCTION

In the modern economy there are increasingly more services which are offered via electronic networks. Some examples are broadcasting, banking, telecommunication and a wide range of other services. Electronic communication networks now play a crucial role in our everyday life.

But these fast moving and continuously evolving markets obviously challenge competition authorities in many ways. One difficulty is the market definition. Traditionally it tends to focus on demand-side substitutability. This may lead to incorrect outcome in dynamically competitive industries where competition comes from new products, whose time of introduction is most often uncertain. In addition, geographic boundaries are at best fuzzy, and may even be nonexistent. Moreover, issues like convergence and compatibility pose challenges. If we find that different platforms indeed are disconnected markets; will they be separate also in the future, or will rapid technological change turn all platforms into one single relevant market? Other important features which must be considered are network effects and the presence of two-sided markets. And finally, when all these issues are resolved and a decision finally is reached – the market may have changed dramatically and the conclusion has no impact on current competitive situation.

In this paper, some definitions are presented at first: What is an electronic network? And what are electronic network services? Thereafter, some figures showing important trends will be presented before some key features of the markets are discussed. We will briefly take a look at the concept of market definition and the relevant market, discuss how competition authorities are challenged by these fast moving changes, and the implications for competition policy. Before concluding, some sunshine – or soft – enforcement examples in this area, based on recent experiences of the Norwegian Competition Authority will be portrayed.

925 Based on Knut Eggum Johansen's presentation at the International Competition Law Forum, Warszawa 15-16 April, 2009.

2. KEY FEATURES OF ELECTRONIC COMMUNICATIONS SERVICES AND NETWORKS

First, a few words on the regulatory framework and processes. The Commission Directive on Competition in the Markets for Electronic Communication Networks and Services (2002/77/EC) regulates i.a. rights to establish and offer services in the markets for electronic communication, and must be considered together with the EU regulatory framework in the area for electronic communication. As of 2002 the directive has been also a part of the process to make ex ante sector-specific regulation converge towards ex post competition law enforcement[926] and has represented a continuation of the trend of liberalising the communications sector, launched by the Commission in 1999.

Thus, the directive supplemented the European regulatory framework applicable to electronic communications networks and services put in place by the General Directive and four Specific Directives of 7 March 2002, which are now in the process of being replaced by the "Telecoms Reform Package". This package was launched in 2007, and intends to take account of the changed sectoral landscape through i.a. creating a single European telecoms market, strengthening consumer rights and giving them more choice by reinforcing competition between the operators. A part of the proposed package constitutes also the creation of the European Telecom Market Authority that shall support the Commission and national regulators in ensuring that market rules and consumer regulation are applied consistently.[927]

The Directive on Competition in the Markets for Electronic Communication Networks and Services defines "electronic communications" and "electronic communications networks" to include all electronic communications services or networks which are concerned with the conveyance of signals by wire, radio, optical or other electromagnetic means, thus including the broadcasting of radio and television programmes. The term "electronic communications services" denotes the conveyance of signals on electronic communications networks and relates to a service normally provided for remuneration.

Two features can in particular be noted regarding these definitions. First, the directive makes reference to "electronic" rather than the previously used

926 In this regard it can be mentioned that the Norwegian Competition Authority has excellent relations with the Norwegian Post and Telecommunications Authority (NPT).

927 The Commission's proposals for reform have yet to be approved by the EU's decisional process.

"telecommunications" services or "networks". This change takes into account the convergence phenomenon. It brings together under a single definition all electronic communications services or networks used for the conveyance of signals. Secondly, the directive excludes from the regulatory framework services providing or exercising editorial control over the content transmitted using electronic means.

In 2009, electronic networks are something we use almost every day. They represent a fast and efficient tool for interaction and coordinating action, as well as conducting market transactions. Electronic networks enable new ways of distributing, accessing and exchanging information. They provide new and efficient ways of working, learning and playing. A large and increasing share of services is offered via electronic networks, notable examples being WEB-TV or IP-phone as well as the Internet banking. In addition, electronic networks are important for searching as well as buying goods and services, etc. Social sites like Facebook and Twitter demonstrate clearly that electronic networks also have given rise to new communities of people with shared interests and concerns.

An important feature of these markets is that they are characterized by rapid technological change as well as economies of scale and large investments in R&D. This in particular applies to the platforms for the conveyance of signals, but also for the production of content, services and software for using the network and its services.

Another important feature is that competition often is *for* the market, instead of competing within the market. An example often used to illustrate this is the competition between Beta and VHS (for those of you who still remember the old video-tape cassettes). VHS got an early lead, and network effects allowed it to become dominant even though it was technically inferior. Other examples where the market gravitated toward one winner are the battles between the spreadsheet programs EXCEL and LOTUS and between word processing programs WORD and WORD PERFECT. A more recent case involved the competition between Blue Ray and HD DVD to be the new video standard.

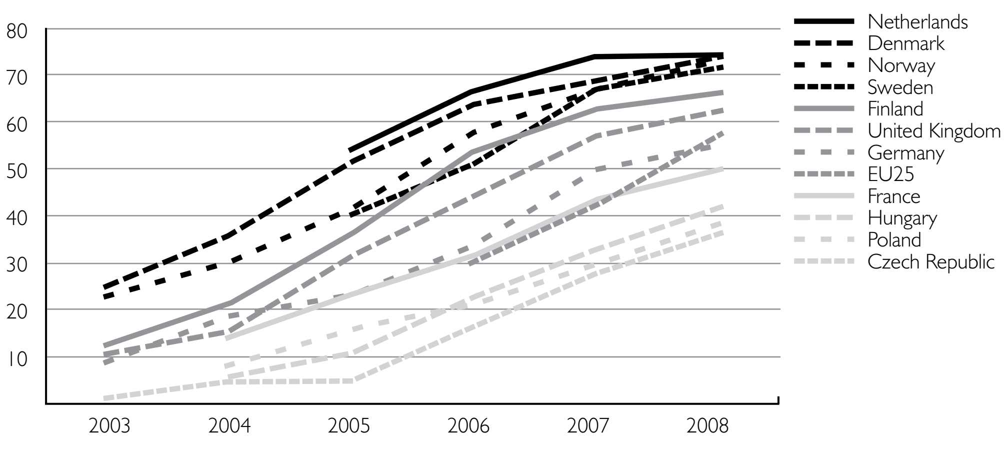
These examples also tell us that electronic networks or associated technologies often seem to tip in the sense that one provider or one platform obtains a dominant position in the market, often close to monopoly. This is often the case when there are strong network effects. The classic illustration of network effects is the telephone. Being the only possessor of a handset in the whole world would not be very exciting. The more people own telephones, the more valuable the product is to each owner.

3. HOW IMPORTANT ARE THESE NETWORKS AND SERVICES IN MODERN ECONOMIES?

Electronic networks have become more and more crucial for the modern society and the use of services provided through electronic networks is increasing significantly. This is obviously connected with access. Building high capacity networks and improving access and geographic penetration is a specific policy goal in many countries. This development can be seen clearly in Figure 1 below, which presents the percentage of households with broadband Internet access in some European countries. For instance, 73 percent of Norwegian households enjoyed this type of access in their homes in 2008, compared to somewhat over 20 percent in 2003.

Also in Norway, widespread use of broadband Internet access has been an explicit policy goal. According to a new report from the Ministry of Government Administration and Reform (published in March 2009), 98.8 percent of the Norwegian households may now access the Internet with speeds above 640 kilobytes per second. Thus, the dependence – and the possibilities – of electronic networks are rapidly increasing.

Figure 1. Households with Internet broadband 2003-2008 (percentage of all households, sources: OECD and Eurostat)



The next figures present some recent statistics relating to the Internet use in Norway. The question posed is: What have Internet users used the web for the last three months?

The numbers in Figure 2 refers to the second quarter of 2008. We see that e-mailing, searching for goods and services, Internet banking as well as reading news on the web are important uses. Between 80 and 90 percent of the respondents used the net for such purposes.

Mainly, there are no major differences between the genders. However, men seem to be more preoccupied with downloading software, whereas women are deemed to be more interested in health related information search.

Figure 2. Internet uses in the last three months, by gender, 2Q 2008 (Source: Statistics Norway)

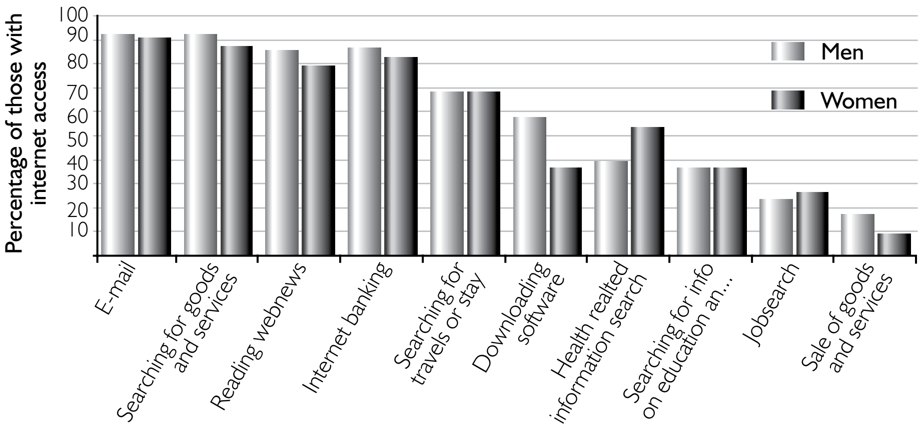
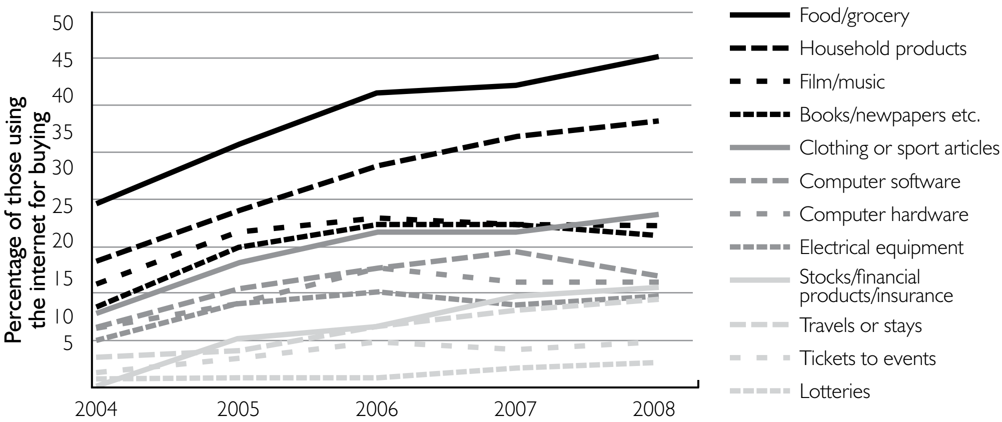


Figure 3 below presents more specific data on services offered via the Internet. Here, Internet users have been asked if and what they have been buying online during the last year. The data refer to the period from 2004 to 2008.

We see that travel-related goods as well as books or newspapers are the most popular purchases, with clothes and sports articles coming up as a strong number three, slightly above film/music and books/newspapers.

The most striking feature of this picture might be the growth experienced in almost all categories during this period.

Figure 3. Use of the Internet for purchasing goods or services in the last 12 months (Source: Statistics Norway)



4. RELEVANT MARKET AND NETWORK SERVICES

The main purpose of market definition is to identify in a systematic way the competitive constraints to the businesses involved – be it in a merger, an abuse of dominance or an antitrust case. Market definition makes it possible to calculate market shares that convey meaningful information regarding market power.

The relevant market is defined according to both product and geographic features. Factors including demand and supply-side substitutability, potential competition and entry barriers have to be taken into account.

The Commission guidelines on market analysis and the assessment of significant market power in communication networks and services set out principles for application by national regulatory authorities and are based on these fundamentals.[928] However, defining markets in dynamically competitive industries presents a number of challenges.

One challenge is represented by insight from Schumpeter. Electronic networks and the markets for services provided with them are obviously characterized by dynamic, technological Schumpeterian competition. Joseph Alois Schumpeter was an economist and political scientist living from 1883 until 1950. He popularized the

928 See http://europa.eu/eur-lex/pri/en/oj/dat/2002/c_165/c_16520020711en00060031.pdf.

term “creative destruction” in economics. Schumpeter[929] argued that competition in innovative industries is dynamic and often consists of a series of races for market dominance. In traditional markets, when undertakings face competition, they seek to attract customers by offering lower prices or higher quality than their rivals, thus benefiting final users. In innovative industries, Schumpeter argues that firms engage in a “perennial gale of creative destruction” that “strikes not at the margins of the profits of the existing firms but at their foundations and their very lives.”

The core of the Schumpeterian argument is that in many markets, competition primarily occurs through cycles of innovation, rather than through traditional price or quality competition. Businesses compete for temporary dominance of the market through the introduction of new generations of technology. Consequently, at any given moment, one firm might dominate sales of a given product. Thus, the winners get huge market shares and enjoy substantial profits. These “prizes” for champions provide the appropriate incentives for investment. But even more importantly: other firms will continue to innovate and prepare to force the incumbent away from the market by developing superior products.

A good example is Windows. Microsoft’s product has dominated the operating systems’ market for 20 years. Windows has been challenged continuously, but with no great success. The most recent threat was posed in early July 2009, when it became clear that Google, in a direct challenge to Microsoft, is developing an operating system for PCs that is tied to its Chrome Web browser.[930] According to the news, Google has already signed agreements with several of the major manufacturers.

Traditional market definition exercises tend to focus on demand-side substitutability. This may lead to a misleading outcome in dynamically competitive industries where competition does not come from already available demand substitutes, but from new products, whose time of introduction is most often uncertain. Obviously, the Schumpeterian perspective provides insight into market dynamics and the innovative process which must be applied by competition authorities.

929 See e.g. M. L. Katz, H. A. Shelanski (2005). ‘Schumpeterian’ Competition and Antitrust Policy in High-Tech Markets. *Competition*, Vol. 14, p. 47, 2005. Available at SSRN: http://ssrn.com/abstract=925707.

930 New York Times, July 8th, 2009: http://www.nytimes.com/2009/07/08/technology/companies/08operate.html?_r=1&scp=2&sq=google&st=cse.

Another challenge is the issue of what kind of technologies or services actually compete with each other. Take distribution of TV-signals as an example. Today, there exist several platforms through which TV-signals can be distributed to the viewers; cable, satellite, DTT, WEB- and IP-TV. Does this mean that the service providers using the different platforms are in the same relevant market, or can it be that each platform constitutes a separate market? In addition, geographic boundaries are at best blurry, and may even be nonexistent in some of these markets.

What about convergence and compatibility? If we find that the different platforms indeed are separate markets; will they also be disconnected in the future, or will rapid technological change turn all platforms into a single relevant market? In general, regulators need to ensure regulatory consistency in a converging and rapidly changing market, and avoid decisions that favour specific technologies and services, thus distorting competition between platforms.

Other important factors which must be considered are network effects and the presence of multi-sided markets. The presence of (strong) network effects typically leads to "tipping" markets, where the winning technology dominates. In multi-sided markets seemingly distinct customer groups provide each other with network benefits via some common platform. Examples of multi-sided markets include payment systems, such as credit cards, as well as information-based industries, such as Internet portals. For Internet portals, such as e.g. real estate advertising, a tipping effect might occur because it is more convenient to advertise and search for real estate in just one portal. If one portal for various reasons succeeds in attracting more customers and advertisers, this will give it more resources to develop further, thus attracting even more customers and advertisers. As a result, in the end, there might be just one portal left overall. A case the NCA encountered in this market is elaborated below.

5. ENFORCEMENT – SOME EXAMPLES FROM NORWAY

Soft enforcement, or "sunshine" enforcement, as it also has been denoted can be particularly useful in network markets and industries. One of the reasons for this is that formal procedures often involve a long time perspective and substantial uncertainty before the case is brought to a final and legally binding conclusion. The second reason is presented in the previous section; defining the market correctly and avoiding destructive intervention or interventions that should have been avoided is obviously not an easy task.

Although no precise definition or typology seems to exist, and instruments in this category differ widely in scope (general v. individual), purpose (publicity, guidance, etc.) and form (written or oral), it can be said that soft enforcement generally is intended to assist businesses in complying voluntarily with competition law,[931] i.e. without a formal decision.

On fast moving markets, soft-law instruments can obviously and in particular be a very flexible and efficient tool to achieve desired outcomes quickly to the benefit of consumers, and is something the NCA has used with success relating to anti-competitive practices. The following section presents two recent soft enforcement cases along with a case relating to the Internet advertising of real estate.

5.1 FROM MONOPOLY TO COMPETITION IN FOOTBALL BROADCASTING RIGHTS

The Norwegian Football Association (NFF) and the organization representing the top football clubs in the country (NTF) jointly manage the media rights to national sports discipline.The original distribution agreement covered the period 2006-2008, and all media rights were purchased jointly and exclusively by the prominent commercial public broadcaster in Norway (TV2), and the biggest telecom operator, (Telenor).

The Norwegian Competition Authority was concerned about the possible anti-competitive effect of a similar arrangement in the forthcoming contracting period. Thus, the agency initiated negotiations with NFF and NTF throughout the process of formulating the tendering procedures.

The resulting new agreements, covering the period 2009-2011, are unique in the sense that the distribution rights are spread across a number of different companies on different distribution platforms. In practice, it means that matches will be shown live on both IP-TV and web-TV. Two different web-TV operators obtained the media rights. This should also contribute to challenge the hegemony of traditional distribution platforms.

The distribution of rights across platforms and companies, and the resulting competition for being the preferred platform and service provider will provide

931 See e.g. N. Petit, M. P. L. Rato, From Hard to Soft Enforcement of EC Competition Law - A Bestiary of 'Sunshine' Enforcement Instruments (September 18, 2008). Available at SSRN: http://ssrn.com/abstract=1270109.

consumers with better access and a greater choice. The new contracts have also led to fierce price competition between web-TV providers, as well as a wider choice of products to choose from.

5.2 INCREASED COMPETITION IN THE NORWEGIAN TV MARKET

The switch from analogue to digital broadcasting is under way in Norway, and is due to be completed by the end of 2009. In 2007, the NCA commissioned a report on the effects of exclusive distribution agreements in the TV market. The agency was concerned about an exclusivity agreement between TV2, the most popular commercial channel in Norway, and Canal Digital, one of the country's two satellite broadcasters. The agreement meant that rival broadcaster, Viasat, was unable to offer its customers access to TV2, and therefore may not have been able to compete effectively in the market. The report found that the exclusive agreement had restricted competition and led to higher prices. The launch of the digital terrestrial transmission network in 2007 launched another competitor into the market – but again Viasat was not able to compete effectively without being able to provide access to TV2.

The expert report provided the NCA with a good basis for a clear, practical and proactive approach towards competition policy in the TV-market. The NCA had several meetings with the parties concerned and TV2 finally entered into non-exclusive distribution agreements with both Canal Digital and Viasat. We believe this agreement – reached without formal decisions or interventions – will stimulate increased competition to the benefit of consumers.

5.3 INTERNET PORTALS AND REAL ESTATE AGENTS

Over the last few years, independent Internet portals have become essential to the marketing of real estate in Norway. They provide an electronic network market place, where sellers and buyers can meet. In Norway, the largest Internet portals have a practice whereby only estate agents are permitted to advertise. Sellers of real estate who wish to advertise on these portals are forced to use an estate agent or a lawyer.

The reason why the portals exclude parties other than estate agents is the following: about 95 percent of all residential property sales is done through estate agents. The agents want to keep efficient Internet portals to themselves and ask the portals for exclusivity. Because this is an electronic network market, even the largest portal could easily lose its market share, and stick to the exclusivity in fear of losing the agents.

We believe that this exclusivity limits choice for users and restricts competition in the downstream market of real estate services. The NCA reviewed the practice under Sections 10 and 11 of the Competition Act (corresponding to Articles 101 and 102 of the Treaty on the Functioning of the European Union) without finding a basis for intervening. However, the Norwegian Competition Act allows intervention by regulation against market conduct which restricts competition.

Consequently, the NCA proposed a regulation that requires Internet portals to provide anyone with access to residential property advertisements on non-discriminatory conditions. In September 2009, the Norwegian Ministry of Government Administration and Reform established such a regulation. The regulation entered into force on 1 January 2010. By using a regulation that will apply to all the players in the market, a level playing field for the Internet portals will be ensured.

6. CONCLUDING COMMENTS – IMPLICATIONS FOR COMPETITION POLICY

The Schumpeterian perspective on competition in innovative and dynamic markets, such as the network industries and services provided through them, shows that by focusing too narrowly on current sales and price competition, authorities may miss the real force behind market performance – the innovation. Consequently, intervening in dynamic markets might have unintended, long term and negative consequences for competition and consumers.

Taking a too narrow view – intra- or inter-temporary – may have negative effects in market dynamics. By ignoring potential competition in dynamically competitive industries, markets might be defined too narrowly, which in turn will lead to unjustified findings of dominance. We risk slowing the innovation process either by distorting the reward structure for risky R&D or by preventing dynamically beneficial mergers. Thus, in such markets there is increased risk of destructive intervention or interventions that should have been avoided.

Not surprisingly, these are arguments competition authorities are met with in many cases, and which obviously have to be considered carefully. But is the implication of the Schumpeterian perspective that the competition authorities should move more in the direction of a laissez-faire or the Chicago School policy regarding mergers, antitrust and abuse of dominance in network industries and services provided in electronic networks?

The answer to this question is unequivocaly negative. It is important to have in mind that Schumpeter provides a way of *understanding* market dynamics and the competitive process in i.a. network industries. The perspective is definitely not an excuse for a lax competition policy. As competition authorities, we are well aware of the fact that it is competition that drives innovation, and that competition and the competitive process must be nourished and protected. Competition supports innovation – and vice versa.

For this reason, competition authorities must obviously have a dynamic and forward-looking perspective on their enforcement activities. And we must be careful not to discourage pro-competitive, welfare-enhancing competition. Fighting for a dominant position through innovation is good – abusing the dominant position, when after it has been gained, is bad.

Moreover, as the Microsoft experience so clearly has taught us a dominant position acquired through a cumulative sequence of successful innovations can be long lasting. We also know very well, also from the Norwegian experience, that a dominant undertaking easily may venture into abusive behaviour to extend the period with market power whenever the opportunity arises and to expand the dominant position into adjacent markets.

Thus, in these industries we must pay close attention to attempts to abuse a dominant position; abuses attempting to extend the period of dominance, or extend the dominant position into adjacent markets, and abusing the dominant position must be struck down.

However, experience also shows that hard enforcement often requires a long time perspective. When a decision is finally reached, the market may have changed dramatically. Thus, the authorities should use the whole range of their available instruments, from information, education and guidance to enforcement soft as well as hard. In particular, competition authorities should be active in the field of advocacy, to inter alia contribute to removing barriers to competition, thus securing potential competition.

In these markets we also frequently observe strategies such as tying and bundling, which also result in prices less transparent to consumers. Consequently, as competition – or sector regulation authorities – we might also have a very important role in securing price transparency.[932]

An important point in this paper illustrated with some cases has been that soft enforcement based on a well founded perception of where the market should move – to the benefit of competition and consumers – can be a very efficient way of executing competition policy in these fast moving markets.

932 In this regard it can be mentioned that the Norwegian Post and Telecommunications Authority (NPT) has a popular price comparison service for mobile phone prices accessible from their website: http://www.npt.no/portal/page/portal/PG_NPT_NO_EN/PAG_NPT_EN_HOME.

William E. Kovacic

CONVERGENCE AND DIVERGENCE IN THE EU AND US COMPETITION POLICY[933]

1. INTRODUCTION

From the late 19th century through the first half of the 20th century, the enforcement of statutes forbidding anticompetitive practices was an endeavor unique to the United States (US). In this period, a handful of other jurisdictions – for example, Canada in 1899 – had adopted competition laws, but none applied these commands in a manner that compelled domestic or foreign firms to take notice. To come ahead a quarter century to 1975, the few jurisdictions with actively enforced competition laws included the European Union (EU),[934] Germany, and the US. Even at this time, questions of cross-border enforcement dealt mainly with skirmishes over the imposition of treble damages in private US antitrust suits upon foreign firms.

I doubt that in 1975 even the most ardent enthusiast for competition law imagined what would transpire in the coming decades. Who foresaw in 1975 that by 2010 the Soviet Union would dissolve, China would pursue far-reaching market-oriented reforms, and the European Union would include several former Soviet Republics and nations that once were known in the West as members of the Warsaw Pact? And who anticipated in 1975 that by 2010 most nations would turn to market-based systems to promote economic growth, or that the number of jurisdictions with competition laws would approach 110?

The transformation of economic policy and the regulatory framework in individual states has coincided with advances in communications, finance, and transport that have intensified cross-border integration in the production and sale of goods and services. These developments have increased the interdependence of national or regional regulatory regimes. Decisions taken in one jurisdiction concerning

933 Parts of this paper are adapted from William E. Kovacic, Competition Policy in the European Union and the United States: Convergence or Divergence?, in Competition Policy in the EU: Fifty Years on from the Treaty of Rome 314 (Xavier Vives ed. 2009). The views presented here are the author's alone and not necessarily those of the US Federal Trade Commission or any of its members.

934 The Treaty of Lisbon, which merged the EC with the other pillars of the EU, came into force on 1 December 2009. Accordingly, this paper will refer to the "European Union (EU)" instead of the "European Community (EC)" when references are made to the organization in general. See Treaty of Lisbon Amending the Treaty on European Union and the Treaty establishing the European Community, December 13, 2007, 2007 O.J. (C 306) 1 [hereinafter Treaty of Lisbon].

a cartel, a merger, or an abuse of dominance can have substantial cross-border spill-overs.

As a group, the world's competition systems feature noteworthy substantive and institutional similarities. Only an observer unfamiliar with the larger history of the evolution of national legal systems would find this shocking. At the same time, in an environment of ever greater economic and regulatory interdependence, there is broad awareness of how the substantial multiplicity of competition systems with dissimilar substantive standards, procedures, institutional arrangements, and capabilities can discourage business transactions that spur economic growth and can needlessly increase the cost of controlling anticompetitive conduct.

Recognition of the potential costs associated with the multiplicity of competition systems has inspired various measures to promote international convergence upon superior norms.[935] Many initiatives principally involve public authorities. These include voluntary multinational networks such as the International Competition Network (ICN) and the competition committee of the Organization for Economic Cooperation and Development (OECD); regional collaborations (e.g., the Andean Community, the Caribbean Community (CARICOM), and the Common Market for Eastern and Southern Africa (COMESA)), and bilateral discussions between individual competition agencies. These largely-public activities coexist with projects in various non-government networks, such as professional associations and academic organizations. Non-government advisors have played a vital role in the work of some of the public agency networks, such as the ICN.

Amid abundant convergence-related activity within all of these institutions, why should the level of convergence between the competition systems of the EU and the US be a specific focus of attention? More than any other single force, the interaction of both regimes deeply influences the convergence process within all of the multinational and regional networks. This is a function of domestic expenditures (the EU and the US spend more financial resources on public enforcement than other jurisdictions), outlays for international projects (both systems invest the most in international networking and have the largest foreign technical assistance programs related to competition policy), experience (the EU and the US have a larger base of current and older cases and engage in substantial non-litigation

935 By "norms" I mean consensus views within a group about how members of the group – such as jurisdictions with competition laws – ought to behave. See William E. Kovacic, The Modern Evolution of U.S. Competition Policy Norms, 71 Antitrust Law Journal 377 (2003).

policymaking activity), and economic significance (both regimes are the largest economic markets on the planet). This gives the EU and the US unequaled capacity to project their competition policy preferences beyond their own borders. What happens in the EU and the US does not influence exclusively their territory.

This paper examines the state of the relationship between the competition policy systems of the EU and the US.[936] Part 2 of the paper begins by discussing, as a normative matter, what type of convergence on policy norms we should hope to see between both regimes – or among all of the world's authorities. Part 3 then offers a positive description of existing similarities and differences between the EU and US competition policy systems. Part 4 reviews centrifugal and centripetal forces that promise to affect the extent to which the two regimes converge or diverge in the future. Part 5 discusses possible paths for improvement in the relationship and for the attainment of better practices in competition policy.

To foreshadow my overall assessment, I regard progress toward greater cooperation in the implementation of competition policy and the mutual adoption of superior norms between the EU and the US to be a genuine success story in the modern transatlantic relationship. Despite differences in philosophy, procedure, analytical technique, and, occasionally, substantive outcomes, the past decade has featured important enhancements in measures by public and non-government bodies in both jurisdictions to improve cooperation in the formulation and implementation of policy standards governing transatlantic commerce. Moreover, the EU-US cooperation has provided important insights into building a framework of global and regional collaboration through multinational networks such as the ICN and the OECD. These efforts can foster widespread convergence upon superior analytical concepts and implementation techniques.

Progress to date has not been inevitable or automatic. Nor will it be so in the years to come. Past achievements have required a substantial commitment of resources to institution-building that does not show up in the usual roster of accomplishments – most notably, case counts – by which authorities most often are judged. Future improvements will depend on the willingness of agency leaders to provide these resources, and more. Good relationships in this area do not come on the cheap.

936 This paper develops themes presented in two earlier papers: William E. Kovacic, Competition Policy Cooperation and the Pursuit of Better Practices, in The Future of Transatlantic Relations – Continuity Amid Discord 65 (David M. Andrews et al. eds., 2005); William E. Kovacic, Extraterritoriality, Institutions, and Convergence in International Competition Policy, 97 American Society of International Law Proceedings 309 (2002).

Resources will not be the only challenge for the EU and US competition agency leadership. The public agencies in the European Union and the United States cooperate extensively, yet they also compete for influence and recognition. The drive to be seen as the global leader in policy is an underlying source of tension that can sharpen the edge of disagreement about specific matters or larger policy issues. Despite these tensions, an inter-jurisdictional rivalry channeled in constructive directions can have positive consequences. Rivalry to attain superior substantive approaches and implementation techniques is a competition worth having.

2. WHY DOES CONVERGENCE OR DIVERGENCE BETWEEN THE EU-US SYSTEMS MATTER?

The interest in mapping out the EU and US competition policy systems stems from more than curiosity about comparative study. For at least three reasons, the differences today can have considerable practical and economic significance. First, there is a high and increasing degree of interdependence between the regulatory regimes of individual jurisdictions. In many areas of regulatory policy, the jurisdiction with the most intervention-minded policy is powerful enough to set a global standard. It is the rare multinational enterprise that does not operate in the EU, or in the US. For matters such as abuse of dominance or mergers, firms generally must conform their behavior to the practice of the most restrictive major jurisdiction with competition laws. By any measure, the EU and the US are major jurisdictions – "major" in the sense of having the nominal authority and enforcement capability to compel fidelity to their demands.

The second reason concerns the process of enforcement. Even when the EU and US apply the same substantive standards and ordinarily reach the identical assessment of the same commercial practice, differences in the procedure for investigations and agency decision-making can impose costs on affected enterprises. In the case of merger reviews, these costs include the time and out-of-pocket expense of complying with varied filing requirements and accounting for differences in the timing of government reviews. Where it is possible to achieve simpler, more common procedures, the EU and US agencies can lower the cost of executing routine transactions without any reduction in the quality of their substantive analysis.

The third reason involves the development of new competition systems around the world. The EU and the US spend substantial resources for technical assistance for countries that have new systems or are considering the adoption of the regulations. By far, most of the approximately 80 jurisdictions that have implemented new competition laws in the past 30 years have civil law systems that usually rely on an administrative enforcement model resembling the European Union regime. By comparison, few civil law countries have established competition systems that use the adversarial prosecution model employed by the US Department of Justice (DOJ). Since the EU institutional platform is more compatible with the institutional arrangements in most civil law countries, many transition economies have an inclination to look first to the EU in designing and implementing their regimes. This means that European norms, more than US principles, tend to be more readily absorbed into the newer competition policy systems.

2.1 THE OPERATING SYSTEMS AND APPLICATIONS OF COMPETITION LAW

Experience with technical assistance programs permits us to derive a more general observation about the global development of competition policy. To use a computer technology metaphor, the operating system of a jurisdiction's competition laws consists of the institutional framework through which legal commands are formulated and applied. As noted above, most jurisdictions are civil law systems. This ensures that the EU institutional framework which relies (compared to the US) upon more highly specified legal commands and emphasizes policy development through an expert administrative body will be the most popular institutional model among the world's competition authorities. The US competition law framework is grounded mainly in a common law methodology. The US relies substantially upon open-ended statutory commands and the elaboration of doctrine through case-by-case litigation. By reason of history and modern practice, relatively few jurisdictions will embrace this model.

With respect to the operating systems of the world's competition laws, the EU's institutional arrangements were destined to attain a dominant share. That dominance is likely to continue. An interesting issue for global competition norms is the choice by individual jurisdictions of substantive analytical "applications" and related investigative techniques to run upon a chosen operating system. Where will countries look to obtain the basic applications that they will run through their institutional operating systems? In areas such as the treatment of cartels and horizontal mergers, the US has provided the analytical applications that most of the world's competition law systems use today. The US also has designed implementation applications, such as leniency policies to detect cartels, that enjoy broad popularity around the world. Moreover, the US applications such as the use of private rights of action and the use of criminal sanctions to punish cartels are receiving a close look in many civil law countries, although the adoption of these applications will require these countries to make some important adjustments to their institutional arrangements.

Thus, the European Union enjoys a dominant share concerning the operating system for competition law, and the market for applications remains highly competitive. The EU and the US account for the leading share of applications regarding substantive analysis and investigative methods, but a number of jurisdictions have produced important refinements of EU or US applications for their own use. The applications have an open source element to the extent that individual countries often retain freedom to make adaptations suited to their own needs. The level of adaptation sometimes is constrained by the obligation that individual states owe to superior legal authorities. For example, accession to the EU has required candidates to conform their laws to EU law. This might be seen, in rough terms, as a form of tying analytical applications to an institutional framework. Even so, the EU's own analytical applications often draw upon concepts and experience from the US. Individual jurisdictions, large or small, have considerable capacity to shape the development of substantive applications by their own success in advancing the state of the analytical art.

2.2 DIVERSIFICATION AND CONVERGENCE: NORMATIVE PRINCIPLES

From a normative perspective, how should we regard the simple existence of differences between the EU and the US as to substantive principles, analytical approaches, and implementation techniques? Two normative principles strike me as appropriate. First, some degree of difference is not only inevitable but healthy. Complete homogeneity across individual systems – a harmonization that unified jurisdictions by doctrine and process – "drives out experimentation and diversity of our regulatory levers."[937] The history of competition policy has featured a continuing search for optimal substantive rules and implementation methods. This search has benefitted from continuous, decentralized

937 Kenneth Neil Cukier, Governance as Gardening: A Report of the 2007 Rueschlikon Conference on Information Policy 50 (2007) (quoting Professor Viktor Mayer-Schoenberger).

experimentation with respect to analytical principles (e.g. DOJ's adoption of revised merger guidelines in 1982), enforcement procedures (e.g. the creation in the 1970s of the US system for mandatory pre-merger notification and waiting periods), investigation techniques (e.g. the DOJ's leniency reforms of the 1990s), and organizational innovation (e.g. the United Kingdom Office of Fair Trading's recent restructuring to integrate competition and consumer protection operations).

Insistence on uniformity across systems, or a requirement that innovations within individual jurisdictions proceed only after a broad consensus among the global community of competition authorities has been achieved, would stymie these and other valuable measures. Competition policy has a strong experimental aspect. Improvements in substantive standards are likely to be achieved by an incremental process of adjusting enforcement boundaries inward and outward, and by assessing the consequences of pressing for more or less intervention. Refinements in organizational structures and investigational techniques likewise require experimentation (should an agency's economists be located in a separate division that reports directly to the head of the agency, or should they reside in teams of case handlers?) and the observation of results. The only way to answer basic questions about substantive policy and implementation is to test alternatives, and that testing benefits from decentralization that does not require consensus-building across jurisdictions for every adjustment from the status quo.

The second normative principle is that there should be mechanisms to promote adoption of superior norms. In a series of speeches presented during his chairmanship of the Federal Trade Commission (FTC), Timothy Muris formulated a three-stage framework by which independent jurisdictions could realize the benefits of decentralized experimentation and promote the broad adoption of superior norms.[938] By "superior norms" I mean standards that (a) promote the accurate diagnosis of the actual or likely competitive significance of observed behavior, and (b) foster the design of government intervention (by initiating a case, by performing a study, or by acting as an advocate before other public institutions) that corrects the problem at issue.

938 See Timothy J. Muris, Competition Agencies in a Market-Based Global Economy (Brussels, July 23, 2002) (prepared remarks at the Annual Lecture of the European Foreign Affairs Review); Timothy J. Muris, Merger Enforcement in a World of Multiple Arbiters (Washington, D.C., December 21, 2001) (prepared remarks before the Brookings Institution Roundtable on Trade and Investment Policy).

The first stage of the Muris framework consists of decentralized experimentation within individual jurisdictions. The second involves the identification of superior substantive standards and implementation methods. In the third stage, individual jurisdictions voluntarily opt in to superior norms. This framework anticipates and welcomes experiments that depart from the status quo and supplies the means for promoting the widespread adoption of superior approaches. I will have more to say below about what the EU and the US can do with regard to the vital second stage of this process.

To the Muris framework I would add a fourth element. Notwithstanding differences that might exist at any one moment between the EU and the US or across other systems, individual jurisdictions should build institutional mechanisms that increase interoperability. This entails careful attention to enhancing channels of communication and discussion that link related functional units across agencies (i.e. between DG Competition and the DOJ and the FTC) and connect related institutions outside the competition agencies. A useful approach to achieving the fourth element is suggested in the New Transatlantic Agenda (NTA)[939], which was established in 1995. The initiative sought to improve the quality of regulatory policy, and to reduce the cost of the regulatory framework governing transatlantic commerce by improving EU-US cooperation. As Professors Mark Pollack and Gregory Shaffer characterize its approach,[940] the NTA seeks to strengthen EU/US regulatory coordination by enhancing:

– *Intergovernmental contacts* among the chiefs of government and other high level public officials (such as agency or department heads);
– *Transgovernmental contacts* on a day-to-day basis among lower level officials; and
– *Transnational contacts* among non-government institutions and individuals, including academics and the business community.

Beyond providing a way to structure the routine interaction between the EU and US competition policy systems, the NTA's three-level approach provides a useful means for identifying superior norms – the second element of the Muris

939 The New Transatlantic Agenda (1995), available at http://ec.europa.eu/external_relations/us/new_transatlantic_agenda/text.htm.

940 Mark A. Pollack, Gregory C. Shaffer, Transatlantic Governance in Historical and Theoretical Perspective, in Transatlantic Governance in the Global Economy 3, 5 (Mark A. Pollack & Gregory C. Shaffer eds., 2001).

framework. Without a conscious process to identify and adopt superior ideas, decentralization cannot serve its purpose as source of useful policy innovations. By promoting improved interoperability in routine operations and helping identify superior norms, this approach can also provide the foundation on which the EU and US policy makers choose to opt in to such norms.

As sketched out here, the process that generates transatlantic competition norms would be adaptable and evolutionary. There is a tendency to speak of convergence upon "best" practices. I believe it is more accurate and informative to say that the objective is convergence upon "better" practices.[941] The development of competition policy in any jurisdiction is an ongoing enterprise. This stems from the inherently dynamic nature of the discipline. Lest they be frozen in time, good competition policy systems consciously evolve through their capacity to adapt analytical concepts over time to reflect new learning.[942] To speak of "best" practices suggests the existence of fixed objectives that, once attained, mark the end of the task. Envisioning problems of substance or process as having well-defined, immutable solutions may neglect the imperfect state of our knowledge and obscure how competition authorities must work continuously to adapt to a fluid environment that features industrial dynamism, new transactional phenomena, and continuing change in collateral institutions vital to the implementation of the policy.

Perceiving the proper role of the EU and US competition agency leaders to be the continuing pursuit of *better* practices can focus attention on the need for the ongoing reassessment and improvement of institutions. A common commitment by the EU and US officials to make the cycle of re-evaluation and refinement a core element of their operations should be a central element of future cooperation. The routine process of evaluation should focus on the adequacy of the binding legislative framework, the effectiveness of existing institutions for implementation, and the quality of substantive outcomes from previous litigation and non-litigation interventions. This type of inquiry would help ensure that each competition agency considers how it can upgrade its substantive standards and operational methods. For each agency, the improvement could take the form of increasing activity with respect to some practices, and being more passive with respect to others.

941 William E. Kovacic, Achieving Better Practices in the Design of Competition Policy Institutions, in On the Merits – Current Issues in Competition Law and Policy 195 (Paul Lugard ed. 2005).

942 In part, this is an inevitable consequence of drawing upon the discipline of economics, which itself evolves over time, to formulate substantive rules and analytical techniques. William E. Kovacic, Carl Shapiro, Antitrust Policy: A Century of Economic and Legal Thinking, 14 Journal of Economic Perspectives 43 (2000).

3. SIMILARITIES AND DISSIMILARITIES IN THE SUBSTANCE OF EU AND US COMPETITION POLICY

I share the often-expressed view of EU and US officials that the general trend of competition policy in the two jurisdictions has been toward common acceptance of substantive standards and the analytical concepts that support the implementation of those imperatives. An overview of overall goals and specific areas of activity not only verifies that proposition, but also underscores noteworthy differences.

3.1 THE OBJECTIVES OF COMPETITION POLICY

It is over 30 years since Robert Bork's *Antitrust Paradox* emphasized the importance of objectives to the operation of a competition policy system. "Antitrust policy", Bork wrote, "cannot be made rational until we are able to give a firm answer to one question: What is the point of the law – what are its goals? Everything else follows from the answer we give."[943]

Modern discourse between EU and US government officials has featured many statements about the proper aims of competition law. The speeches of top agency leaders indicate broad agreement on the question of goals. Each jurisdiction accepts the proposition that the core of competition law is "the objective of benefiting consumers."[944] Consistent with the single-minded focus on "consumer welfare", EU and US antitrust officials routinely disavow any purpose of applying competition laws to safeguard individual competitors as an end in itself. EU officials also have grown accustomed to hearing, by direct quotation or paraphrase, the US Supreme Court's admonition that the proper aim of antitrust law is "the protection of *competition*, not *competitors*."[945]

At one level, the apparent agreement on overall objectives would seem to be, and is, an important step toward achieving convergence between the two systems. A commitment to apply competition policy commands to improve consumer well-being forces the agency to consider to some extent how a proposed form of intervention will deliver benefits to consumers. This can be at least a mild

943 Robert H. Bork, The Antitrust Paradox 50 (1978).

944 Neelie Kroes, European Commissioner for Competition Policy, Antitrust in the EU and the US – our common objectives 1 (Brussels, September 26, 2007).

945 The much-quoted aphorism appears in Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., 429 U.S. 477, 488 (1977) (quoting Brown Shoe Co. v. United States, 370 U.S. 294, 320 (1962) (emphasis in original).

discipline upon the exercise of agency discretion, and a means to develop an internal norm that focuses on effects upon end users. At the same time, however, the concept of "consumer welfare", and the principle of protecting "competition, not competitors" are so open-ended that their true meaning in practice depends on how they are applied. It is a relatively barren exercise for EU and US officials to invoke these phrases without taking the further difficult step towards achieving agreement on what these phrases mean.

I regard the habit of EU and US leaders to invoke consumer welfare and related expressions as a useful start to a larger and continuing discussion about the objectives of competition law. I do not think that these phrases alone tell us much about the deeper levels of meaning that each jurisdiction attaches to them. Nor do I think that the phrases deny each country considerable discretion to achieve varied policy ends through the process of interpretation and application.

3.2 SUBSTANTIVE COMPETITION POLICY

The general trend of EU and US competition policy in the past two decades has been targeted at greater convergence with regard to the appropriate focus of government enforcement and the application of litigation and non-litigation policy instruments. This part of the paper discusses similarities and dissimilarities. Part 4 below examines the reasons for these developments. Part 4 also describes centripetal forces that have tended to pull the EU and US systems together and centrifugal forces that draw the two systems apart.

3.2.1 SUBSTANTIVE SIMILARITIES

3.2.1.1 CARTELS

Both jurisdictions treat cartels harshly. Speeches of EU and DOJ officials today depict cartels as the most serious form of anticompetitive behavior, and both institutions have devoted substantial effort to prosecuting offenders and to devising new techniques for detecting covert arrangements. Recoveries in the high nine figures occur today with some regularity. The modern trend in sanctions in both jurisdictions has been to increase punishments for violators, and two EU member states (Ireland and the United Kingdom) have adopted policies, like that of the DOJ, of seeking incarceration for individual offenders. There is a continuing debate within the European Commission and in the

Member States about the desirability of relying to a greater degree on criminal sanctions.

This is an area in which EU practice in the past decade has converged substantially upon US norms by a process of voluntarily opting in. Cartel enforcement is a major example in which the EU embraced techniques – most notably, leniency – that had been tested extensively in the US. More broadly, global acceptance of a powerful anti-cartel norm is a vivid illustration of the operation of the Muris framework for convergence: an initial period of decentralized experimentation (i.e. the US leniency enhancements of the early and mid-1990s), the identification of superior practices (e.g. through the deliberations of the OECD competition committee), and voluntary opting in (dozens of jurisdictions have adopted leniency programs).

3.2.1.2 HORIZONTAL MERGERS

Horizontal merger policy in the EU and the US reveals a substantial degree of similarity. The elaboration and revision of guidelines in both jurisdictions in the past 20 years has yielded extensive convergence on the analytical framework. Merger decisions by the referenced courts – notably, AirTours[946] in the EU and Arch Coal,[947] Giant/Western,[948] SunGard,[949] and Whole Foods[950] in the US – have tended to press both enforcement authorities to satisfy more demanding evidentiary standards and withstand closer judicial scrutiny of proof offered to demonstrate likely anticompetitive effects. AirTours and Arch Coal are both similar in their insistence that prosecutors show how the collaboration among firms in a coordinated effects case will unfold after the merger is completed.

3.2.1.3 STATE INTERVENTION IN THE ECONOMY

Competition policy in the EU and the US reflects a growing awareness of how various forms of government intervention can harm competition as severely as private restraints. Statements by the leadership of the enforcement agencies in both jurisdictions indicate that the EU and the US treat state-imposed

946 Case T-342/99, Airtours plc v. Commission [2002], E.C.R. II-2585, 5 C.M.L.R. 7.

947 FTC v. Arch Coal, 329 F. Supp. 2d 109 (D.D.C. 2004).

948 FTC v. Foster, No. 07-352, 2007 WL 1793441 (D.N.M. May 29 2007).

949 United States v. SunGard Data Sys., 172 F. Supp. 2d 172 (D.D.C. 2001).

950 FTC v. Whole Foods Market, Inc., 502 F. Supp. 2d 1 (D.D.C. 2007), FTC v. Whole Foods Market, Inc., 548 F. 3d 1028 (D.C. Cir. 2008).

barriers to rivalry as serious obstacles to competition. The common concern about anticompetitive government intervention has been manifested by the prosecution of cases, the performance of sector studies, and the initiation of advocacy projects.

Although EU and US enforcement officials have a shared suspicion of government restraints on competition, the EU system provides a more powerful platform to address such restrictions. The US has no counterpart to the state aids portfolio of the EU. Moreover, the EU has no exemption for decisions taken by Member State public authorities that matches the breadth of state action immunity available under the Parker[951] doctrine. Owing to the mutual distrust of EU and US officials concerning anticompetitive state intervention, I have classified this category of activity as an area of substantive similarity. Due to the stronger legal platform available to the EU to challenge such restraints, and the breadth of the Parker immunity in the US, this area also could have been included in the Substantive Dissimilarity section below.

3.2.2 SUBSTANTIVE DISSIMILARITIES

3.2.2.1 ABUSE OF DOMINANCE

In some respects, the formative statutory texts of the EU and the US create a basis for differences in the treatment of a dominant undertaking conduct. By their own terms, and by judicial interpretation, the US antitrust statutes have no equivalent to the excessive pricing prohibition in Article 102.[952] The Commission has not used its excessive pricing authority expansively, but the EU Members States have shown a greater willingness to apply this measure under their own competition laws. The bare terms of Article 102 also provide a less certain basis for determining that the prosecutor must show that denominated forms of abuse (e.g. tying) had actual, or likely anticompetitive effects.

951 Parker v. Brown, 317 U.S. 341 (1943). See also Federal Trade Commission, State Action Task Force, Office of Policy Planning, Report of the State Action Task Force 1 (2003), available at http://www.ftc.gov/os/2003/09/stateactionreport.pdf ("The state action doctrine – first articulated in Parker v. Brown – shields certain anticompetitive conduct from federal antitrust scrutiny when the conduct is: (1) in furtherance of a clearly articulated state policy, and (2) actively supervised by the state.").

952 With the entry into force of the Treaty of Lisbon on December 1, 2009, Articles 81-89 of the Treaty Establishing the European Community were renumbered as Articles 101-109 of the Treaty on the Functioning of the European Union. See Consolidated Versions of the Treaty Establishing the European Union and the Treaty Establishing the European Community, Dec. 29, 2006, 2006 O.J. (C 321) 153; Treaty on the Functioning of the European Union, May 9, 2008, 2008 O.J. (C 115) 47.

The interpretations of Article 102 by the Court of First Instance (CFI) and the Court of Justice have created a wider zone of liability than the decisions of the US courts under the Sherman Act. At the margin, US courts have been inclined to say that courts and enforcement agencies commit greater errors by intervening too much, rather than too little. This perspective does not appear in EU jurisprudence, or in speeches by EU officials.

In their technical findings and in their attitude, modern US Supreme Court decisions in cases such as Brooke Group,[953] Trinko,[954] and Weyerhaeuser[955] have demonstrated greater skepticism about abuse of dominance claims than rulings in matters such as France Telecom/Wanadoo,[956] Michelin II,[957] and British Airways.[958] The EU decisions in IMS Health[959] and Microsoft[960] show a greater inclination to condemn refusals to deal than modern US rulings such as Trinko. Unlike Brooke Group and Weyerhaeuser, the France Telecom/Wanadoo decision rejects the need to apply a recoupment test to resolve allegations of exclusionary pricing. A finding of dominance can occur in the EU at or somewhat below a 40 percent market share, while the US offense of attempted monopolization usually treats shares below 50 percent as being inadequate to establish substantial market power.

A major question for the two jurisdictions is how much an effects-oriented standard will become the common core of analysis. The European Commission's Guidance Paper on dominance[961] and speeches by EU officials indicate receptivity to greater express reliance on an effects test, and to reduced emphasis on the category-based assessment, sometimes evident in cases such as British Airways. If there were broad EU/US agreement in concept on the value of an effects test, there still will remain the question of application. For example, the CFI decision in Microsoft on tying issues stated that the court was focusing on the actual, or likely competitive effects of the challenged conduct. Yet the CFI's analysis of tying claims superficially resembles the treatment of tying allegations in the decision of

953 Brooke Group Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209 (1993).

954 Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398 (2004).

955 Weyerhaeuser Co. v. Ross-Simmons Hard-Wood Lumber Co., Inc., 127 S.Ct. 1069 (2007).

956 Case T-340/03, France Telecom SA v. Commission, [2007] 4 CMLR 21.

957 Case T-203/01, Manufacture Francaise des Pneumatiques Michelin v. Commission, [2003] E.C.R. II-4071.

958 Case T-219/99, British Airways PLC v. Commission, [2003] E.C.R. II-5917.

959 Case C-418/01, IMS Health GmbH v. NDC Health GmbH, [2004] E.C.R. I-5039.

960 Case T-201/04, Microsoft v. Commission, [2007] 5 CMLR 11.

961 European Commission, Guidance on the Commission's Enforcement Priorities in Applying Article 82 of the EC Treaty to Abusive Exclusionary Conduct by Dominant Undertaking, 2009 O.J. (c 45) 07.

the US Court of Appeals for the District of Columbia Circuit in 2001[962] on the DOJ complaint against Microsoft.[963] Even in the context of what is called an effects test, outcomes often will hinge upon the quantum and quality of evidence that a court demands before it is willing to find actual anticompetitive effects, or to infer likely adverse effects.

3.2.2.2 VERTICAL CONTRACTUAL RESTRAINTS

EU and US vertical restraints policy has displayed an important degree of convergence over the past two decades, particularly in the current EU guidelines, which moved toward more tolerant treatment of such agreements. Notably dissimilarities remain. Particularly after the Supreme Court's abandonment in the Leegin[964] case of the *per se* prohibition on minimum resale price maintenance, the US doctrine now evaluates vertical contractual restraints under a rule of reason analysis. Tying arrangements nominally remain subject to categorical prohibition, but what the Supreme Court still calls a *per se* rule, increasingly has come to resemble a variant of a reasonableness inquiry. By contrast, EU law relies more heavily on *per se* condemnation, with minimum resale price maintenance being one noteworthy example.

3.2.2.3 NON-HORIZONTAL MERGERS

Compared to the US competition law and policy, the EU policy creates more conceptual possibilities for intervention in conglomerate and vertical transactions. Looking forward, there are questions how expansively these opportunities will be exercised. The CFI decisions in Tetra Laval[965] and GE-Honeywell,[966] while they recognized the legitimacy of the European Commission's portfolio effects theories in principle, found that the Commission had failed to supply adequate proof to establish a violation. At a minimum, these decisions suggest that the Commission will be required to satisfy relatively demanding standards of evidence when challenging a conglomerate merger. The Court's views in Tetra and Honeywell have been incorporated into the Commission's enforcement

962 United States v. Microsoft Corp., 253 F.3d 34 (D.C. Cir. 2001).

963 United States v. Microsoft Corp., Civil Action No. 98-1232 (D.D.C. filed May 18, 1998) (Complaint) available at http://www.usdoj.gov/atr/cases/f1700/1763.htm.

964 Leegin Creative Leather Products, Inc. v. PSKS, Inc., 127 S.Ct. 2705 (2007).

965 Case T-5/02, Tetra Laval BV v. Commission, [2002] E.C.R. II-4381.

966 Case T-210/01, General Electric v. Commission, [2005] E.C.R. II-5575.

guidelines for non-horizontal mergers issued in 2007.[967] Enforcement since that time (as for example in the Google/DoubleClick case) suggests convergence in this area.[968]

4. CENTRIFUGAL AND CENTRIPETAL FORCES

This part of the paper is twofold. The first is to offer some explanations for how the trends in policy came to pass. The second is to identify institutional and other forces that promise to foster a greater degree of convergence in the future, and to highlight forces that are likely to retard convergence. In Part 5 of the paper, I will discuss means to reinforce processes that promote convergence.

4.1 DIVERGENCE: THE CENTRIFUGAL FORCES

Discussions about EU and US competition law frequently default to a collection of familiar hypotheses to explain differences between the two jurisdictions. Thus, it is often said that the EU protects competitors, the US protects competition; the US is beholden to the stale, backward-looking Chicago School of economics, the EU embraces the progressive, forward-looking Post-Chicago School; the US gave up on bringing abuse of dominance cases after 2000, the EU is pressing ahead to keep this and other areas of competition law alive.

I do not deny the appeal of these propositions to those of us who periodically must construct an easily-grasped narrative to organize academic papers, write newspaper articles, or script speeches. I do dispute their accuracy. I am convinced that the conventional explanations divert our attention away from an examination of deeper, more persuasive explanations – many of them rooted in the institutional arrangements of the two systems – why the two systems diverge. To see the underlying conditions more clearly is the first, necessary step to considering how, and where both regimes might converge more completely on common standards. Below I describe four considerations that tend to be overlooked in conventional discussions about why the EU and the US diverge.

967 See generally European Commission, Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings, 2008 O.J. (C 265) 6, available at http:// eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2008:265:0006:0025:EN:PDF (adopted on Nov. 28, 2007 and published on Oct. 18, 2008).

968 See Statement of Federal Trade Commission Concerning Google/DoubleClick, 5 (Dec. 20, 2007), FTC File No. 071-0170, available at http://www.ftc.gov/os/caselist/0710170/071220statement.pdf.

4.1.1 DELEGATION OF THE DECISION TO PROSECUTE: THE ROLE OF PRIVATE RIGHTS

In roughly the past 30 years, judicial fears that the US style of private rights of action – with mandatory treble damages, asymmetric shifting of costs, broad rights of discovery, class actions, and jury trials – excessively deter legitimate conduct have spurred a dramatic retrenchment of antitrust liability standards.[969] This is most evident in the progression toward more lenient treatment of dominant undertaking behavior. The intellectual roots of this development are as much (or more) derived from the work of modern Harvard School scholars, such as Phillip Areeda, Stephen Breyer, and Donald Turner, as they are in the scholarship of Chicago School academics, including Robert Bork and Richard Posner.

EU competition law has evolved without the tempering force of these concerns. For most of the history of the Treaty of Rome, the decision to prosecute in competition cases has been dedicated to public authorities. Had the US private rights of action been more constrained (for example, by making treble damages discretionary rather than mandatory), my prediction is that the US doctrine for abuse of dominance would more closely resemble existing EU standards. The persistent inclination of US courts to raise liability standards to offset perceived excesses of private rights creates what could turn out to be a permanent fissure between the EU and the US approaches to a dominant undertaking conduct, and other forms of business behavior.

The major variable on this point is the possible future enhancement of private rights in the EU. An interesting question for the future is whether, and how much the EU's modernization program (which dilutes the policymaking powers of DG Competition) and its efforts to encourage Member States to augment private rights will affect the evolution of substantive doctrine. EU policymakers generally have disavowed the adoption of measures (such as mandatory trebling) that are associated with overreaching in the US system. Nonetheless, any expansion of private rights necessarily denies public authorities the gatekeeping function – in determining the type and ordering of cases to be prosecuted – that they have enjoyed in the past. And it is possible that the courts of the Member States will regard private litigants as being, in at least some sense, less trustworthy custodians of the public interest than the authorities.

969 This view is elaborated in William E. Kovacic, The Intellectual DNA of Modern U.S. Competition Law for Dominant Firm Conduct: The Chicago/Harvard Double Helix, 1 Columbia Business Law Review 1-80 (2007).

4.1.2 DISSIMILAR PROCEDURES: ADMINISTRATIVE VS. ADVERSARIAL MODELS

The EU model of policy making relies chiefly on elaboration by an administrative body whose decisions are subject to judicial review. To some degree, the operations of the US FTC use the same model. For the US system as a whole, the bulk of key decisions, such as measures to prevent the consummation of a merger, cannot be taken without the court's approval. In other words, where decisions to intervene have relatively powerful consequences, the US system gives the judges an earlier, more significant role in determining whether the prosecutors' preferences will be fulfilled.

In some respects, the US reliance on the adversarial model imbues the US public enforcement system with greater caution in deciding to intervene. DOJ and FTC investigative techniques, for example, rely less heavily than the EU on responses to questionnaires and place greater weight on investigational hearings and depositions to gather and test evidence. Judicial control in the EU is hardly absent (witness the Court of First Instance decisions in 2002 in AirTours, Tetra, and Schneider[970]), but it is generally less intrusive and immediate as it is in the US model. On the whole, this inclines the US agencies to demand, perhaps, a greater quantum and quality of evidence before deciding to prosecute.

By the same measure, the administrative model has made the EU more cautious in some instances about deciding not to intervene. Administrative practice in many civil law systems, and in the EU, compels public authorities to give reasons why they have declined to act upon complaints lodged by citizens or juristic persons. As the CFI decision in Sony/Impala[971] demonstrates, third parties can obtain judicial review of certain decisions by the Commission to close a file in a merger case. Thus, if the Commission were to decide that positive efficiency effects dictated that a transaction be allowed to proceed, the EU officials would need to be prepared to document the expected efficiency consequences. Although the Tunney Act[972] procedures in the US somewhat encumber DOJ's capacity to settle cases, the public agencies generally have much greater freedom to ignore third party complaints and decide not to prosecute.

970 Case T-310/01, Schneider Electric v. Commission, [2002] E.C.R. II-4071.

971 Case T-464/04, Independent Music Publishers and Labels Association (Impala), [2006] E.C.R. II-02289.

972 Antitrust Procedures and Penalties Act, Pub. L. No. 93-528, 88 Stat. 1706 (1974).

4.1.3 ASSUMPTIONS ABOUT UNDERLYING ECONOMIC CONDITIONS

Decisions of courts and enforcement agencies in the US system to relax antitrust prohibitions may stem from assumptions about the operation of the US economic system. Important characteristics of the US system include relatively strong capital markets, comparatively few impediments to the formation of new business enterprises, and an effective mechanism for recycling the assets and personnel of failed firms back into the economy. These features give the US system a substantial degree of adaptability and flexibility.

These conditions may help account for the assumption, reflected in decisions by courts and enforcement agencies, to disfavor intervention in a wide range of disputes. The US abuse of dominance doctrine and policy, for example, assumes a considerable capacity on the part of rivals, suppliers, and consumers to adapt, reposition, and otherwise protect themselves in the face of apparent overreaching by specific firms. The same assumptions probably help explain the trend since the 1970s to disfavor intervention concerning vertical restraints – particularly in light of the expectation that distribution channels will be highly resilient and adaptable. By contrast, it is possible that, because European officials perceive the economy of the EU and its Member States to be less flexible and adaptable, there is less confidence that market processes alone will provide a sufficient antidote, in the absence of public intervention, to offset seemingly anticompetitive business practices. The many measures underway in the EU to liberalize markets – to facilitate capital formation, to promote broad acceptance of a competition culture, and to realize the Treaty's longstanding aims for EU-wide economic integration – gradually could change assumptions about the robustness and resilience of markets and induce a relaxation of restrictions on commercial conduct.

4.1.4 THE SOURCES OF AGENCY HUMAN CAPITAL

In the aggregate, the backgrounds of the personnel of the EU and US public agencies differ in an important respect. In the leadership, management, and case-handling positions, a larger percentage of personnel in the US agencies have experience outside the civil service. The revolving door in the US creates a circulatory process that routinely brings academics and private sector practitioners into the competition agencies to a greater degree than one sees in the EU.

I do not claim that this circumstance has immense effects. It does mean that the US agencies have a larger group of officials, from top management to relatively junior case handlers, who have worked in private companies. This element of experience can provide a stronger basis with which to make confident judgments about which arguments advanced by private firms have merit and which do not. A lack of this practical perspective can increase an institution's general wariness about the motives for business behavior and the significance of specific business tactics.

The mix of personnel in the Commission and in the Member State competition authorities has been changing over time. One sees somewhat more acceptance of a revolving door process which, although it does not spin with the speed of the US system, has brought a larger number of personnel with academic and private practice experience into the EU agencies. In slow and almost imperceptible ways, this can change the culture of enforcement inside the agency, as well as alter the perceptions and attitudes of private sector bodies which absorb personnel who have departed the competition authorities.

4.2 CONVERGENCE: THE CENTRIPETAL FORCES

Various existing phenomena tend to press the EU and the US competition policy systems together in their treatment of substantive antitrust issues. Some of these events take place inside the agencies; some occur in interactions between the authorities; and some happen outside the government enforcement bodies. Many of them are interdependent, such that developments outside the relevant agencies can have major effects on the agencies themselves.

4.2.1 CONSULTATION BETWEEN THE EU AND US COMPETITION AUTHORITIES

Using the three-level NTA framework of intergovernmental, transgovernmental, and transnational contacts introduced in Part 2 above, modern experience reveals considerable interaction between the EU and US competition agencies and an expansion of activity in this decade. To some extent, the intensification of cooperation has stemmed from the highly visible disputes between the two jurisdictions in the Boeing/McDonnell Douglas,[973] and General Electric/Honeywell

973 Boeing/McDonnell Douglas, Case IV/M.877, [1997] OJ L/336.

mergers and the necessity to explore ways to avoid similar policy disagreements in the future. Based on past experience, it is possible – even likely – that publicly voiced disagreements over the disposition of the Microsoft matters in the two jurisdictions will inspire deeper contacts and discussions concerning abuse of dominance cases. Fuller mutual discussion about these and other matters would certainly enhance the EU/US relationship.

Intergovernmental contacts have continued at the highest levels between the Commission and the US federal antitrust agencies. These include regular, formal, bilateral consultations, and a variety of other interactions. The EU Commissioner for Competition, the DG Competition Director General, DOJ's Assistant Attorney General for Antitrust, and the FTC's Chairman played pivotal roles in the formation of the ICN in 2001 and have cooperated extensively in the past decade in the design and implementation of ICN work plans. Contact among high level EU and US officials is also commonplace at conferences and in discussions about specific policy matters. Measured by the sheer volume of contacts or the breadth and depth of discussions, the intergovernmental level of discourse in competition policy is more expansive today than at any period of the EU/US relationship.

A recent, important dimension of the intergovernmental relationship that goes beyond the policy alone deserves emphasis. In past decade, the FTC has undertaken extensive discussions with DG Competition, DG Health and Consumer Protection, and DG Internal Market to explore connections between competition policy, and intellectual property, and competition policy and consumer protection policy. This has been identified as an increasingly important concern in matters such as health care and nutrition, where decisions taken on issues such as advertising have significant competition and consumer protection implications. What we are faced with is the beginning of a new framework of regulatory relationships that recognizes the interdependency of what may have been conceived of as largely independent policy regimes. At the same time the FTC has expanded cooperation with EU Member States, such as the United Kingdom that, like the FTC, combine the competition and consumer protection portfolios in one agency, and have expressed an interest in promoting the integration of policymaking between these two disciplines.

The similar expansion has taken place for what the NTA framework refers to as *transgovernmental* contacts. In recent years, the EU and US competition authorities have expanded the work plan of the existing staff-level merger working group and have established new working groups dealing with such matters as antitrust/intellectual property issues. The frequency of staff-level meetings, by teleconference or face-to-face, also has increased to address a variety of matters within and outside the context of the formal clusters. For DOJ and the DG Competition, there has been a noteworthy expansion of interaction, as the latter has implemented its own variant of the Department's leniency program for the prosecution of supplier cartels. Regular staff-to-staff contacts also have extended dramatically in the context of joint work on ICN and OECD projects.

A similar intensification of activity can be documented for *transnational contacts*. Measured by the agenda of conferences and non-conference activities, the major professional legal societies – among them, the American Bar Association and the International Bar Association – have expanded the energy they devote to EU/US competition policy. Beyond activities sponsored by these bodies, there has been a significant increase in the number of events and continuing legal education programs with a large transatlantic component that attract a substantial transnational audience of academics, practitioners, and government officials. The same applies to trade associations, such as the International Chamber of Commerce (ICC), and academic bodies, including institutions such as the Association of Competition Economics (ACE) based in Europe. Collectively, these non-government networks have played a crucial role in educating the academics, the business community, and the legal profession about the foundations of competition policy in both jurisdictions and about current developments. By engaging government policymakers and participants from non-government constituencies in formal public debate and informal discussion, these bodies help formulate a consensus about principles, and provide a key source of relational glue for the competition policy community. Their significance can be observed in the growing tendency of government-based networks, such as ICN and OECD, to include non-government parties in their work.

It is possible to trace a number of specific policy outcomes to the three levels of contacts (intergovernmental, transgovernmental, and transnational) sketched above. Though not a complete accounting, the following list includes noteworthy measures rooted in the expanded interaction between government and non-government parties across the two jurisdictions.

– Enhancements in formal EU/US protocols involving merger review, including the coordination of premerger inquiries in both jursidictions.
– New EU guidelines on merger policy and intellectual property licensing that featured significant discussion with US competition authorities and non-government bodies (such as the internationally-oriented legal societies and business associations) and reflected, in a number of respects, contributions by the US agencies, and by the non-government groups.
– Continuing augmentation and implementation of the EU leniency program in ways that reflected substantial consultation and interaction with DOJ's anti-cartel unit.
– Greater transparency in the US practice for merger and non-merger matters, including emulation in a growing number of instances of the EU practice of providing explanations for a decision not to prosecute where the enforcement agency has undertaken a substantial investigation.
– The successful launch of a new multinational competition policy network (the ICN) and the healthy invigoration of the work plans of existing networks such as OECD.

The continuation of EU-US cooperation through these channels – high level agency contacts, operational unit interaction within the competition authorities, and contacts involving non-governmental bodies – will continue to operate as forces that tend to promote convergence over time. It is also foreseen that such contacts will intensify. For example, the implementation of the 2006 SAFEWEB[974] legislation has enabled the FTC to engage in a regular program of staff exchanges and internships with DG Competition, the competition authorities of the EU Member States, and with other agencies globally. I am convinced that a program that has a DG Competition attorney, or economist resident in the FTC at all times and permanently has an FTC attorney, or economist resident in DG Competition will improve the agencies' mutual understanding, and will help supply the human glue that binds the two bodies together.

4.2.2 ABSORPTION OF A COMMON BODY OF INDUSTRIAL ORGANIZATION KNOWLEDGE

With some variation, the world's elite graduate programs in economics offer a roughly similar curriculum in industrial organization economics. Students

974 Pub. L. No.109-455, 120 Stat. 3312 (2006).

in these graduate programs become familiar with the same body of industrial organization literature. Owing to personal tastes and philosophies, instructors inevitably differ in the emphasis they give to specific topics and with respect to the policy preferences they articulate in class. Despite these differences, students emerge from these graduate programs with a generally common intellectual framework and a roughly similar set of analytical norms. Above all, recipients of advanced degrees in economics are likely to believe that sound microeconomic analysis is an essential foundation for sensible competition policy.

In recent years, a number of competition authorities have adopted organizational reforms that elevate the role of economic analysis in the decision to prosecute. The European Commission is one of these agencies. Earlier in the decade, DG Competition created the office of the Chief Economist and gave the holder of that office a direct reporting line to Directorate's top leadership. The Chief Economist (initially Lars Hendrik-Roeller and now Damien Neven) has a staff that now exceeds 20 economists. In the EU and in other jurisdictions, the establishment of a separate unit can become the instrument by which economic analysis exerts more influence in guiding the selection and prosecution of cases.

As this institutional reform takes root, economic analysis and the preferences of economists are likely to assume increasing importance in the Commission's investigation of proposed cases, the formulation of complaints, and the prosecution of alleged infringements. The learning of economists in the office of the Chief Economist will closely resemble the process within DOJ's Economic Analysis Group and the FTC's Bureau of Economics. To the extent that economists' perspectives become reflected more expansively in the work of DG Competition, as one predicts they will over time, the analytical approach that the Commission takes in deciding whether to bring cases probably will converge more closely upon the approach that the DOJ and the FTC take.

4.2.3 CRITICAL JUDICIAL OVERSIGHT

At a conference in Brussels early in 2001, I watched a panel of EU practitioners offer the view that DG Competition enjoyed virtually unbounded freedom to set merger policy without the prospect of effective judicial review. One panelist called the Court of First Instance a "lap dog." Another likened the Luxembourg court to a "door mat." Two members of the lap dog/door mat tribunal were sitting in the audience, and I wondered what was going through their minds.

Commentators would not make the same assertions about judicial review in the EU today. The CFI decisions in AirTours, Tetra, Schneider (including the recent CFI ruling on costs[975]), and GE-Honeywell inspired a basic rethink of merger policy and, more generally, organization and process within the Commission. These decisions have had the effect of pressing the EU closer to the US, whose reach recently has been questioned severely in the Oracle,[976] SunGard, Arch Coal, Giant/Western, and Whole Foods decisions.

5. A SUGGESTED AGENDA FOR THE FUTURE: CONCEPTS AND MEANS

There is a variety of ways to build upon existing forms of EU-US cooperation in competition policy to identify and promote convergence upon superior norms. The discussion below describes conceptual focal points for further cooperation, and describes specific means that the EU and US competition policy communities might take to address these points.

5.1 CONCEPTS

For all of the progress in cooperation achieved to date, there is considerable room for learning about basic forces that shape policy in the EU and US, and therefore influence the transatlantic relationship. Discussions among government officials and within non-government networks tend to focus on specific enforcement developments (e.g. the resolution in the EU and the US of each jurisdiction's Microsoft cases) or matters of practical technique and not to ask basic questions about the origins and institutional foundations of the systems. The discussion below suggests that the agenda for discourse inevitably must expand to incorporate examination of these considerations if cooperation is to be enriched and common progress toward better practices is to be achieved.

Toward a Deeper Understanding of the Origins and Evolution of Both Systems. The many recurring discussions about transatlantic competition policy often rest upon a terribly incomplete awareness about how the EU and US systems originated and have evolved over time. A relatively small subset of the US community engaged in transatlantic issues is familiar with the distinctive path by which policy concepts

975 Case T-351/03, Schneider Electric v. Commission, [2007].

976 United States v. Oracle Corp., 331 F. Supp. 2d 1098 (N.D. Cal. 2004).

developed within the EU Member States and supplied the foundation for the EU competition policy regime itself.[977] European specialists in the field likewise often display a fractured conception of the origins and evolution of the US system – a conception often derived from the works of US scholars whose grasp of the actual path of policy evolution is itself infirm. An accurate sense of where the policies originated, and how they have unfolded, is essential to understanding the influences that have shaped modern results in specific cases. To move ahead, discourse at all three levels embodied in the NTA must look back for a richer understanding of competition policy history.

Scrutinizing the Analytical and Policy Assumptions in Specific Cases. The modern EU/US relationship has featured important instances of disagreement and will do so again in the future. Amid the many discussions of cases such as Boeing/McDonnell Douglas, GE/Honeywell, and Microsoft, two things seem to have received inadequate attention. The first, which only the competition agencies can perform, is a careful, confidential examination of the specific theories of intervention, and an examination of the evidence upon which each jurisdiction relied on deciding how to proceed. The side-by-side, behind-closed-doors deconstruction of the decision to prosecute (or not to prosecute) would seem to be a valuable way to identify alternative interpretations and test them in an uninhibited debate involving agency insiders (and, perhaps, experts retained by each authority to assist in the review of the case). Yet discussions of this type generally do not take place.

Even more general discussions of cases that occupy considerable attention at conferences and seminars infrequently come to grips with what appear to be differences in assumptions about the operation of markets and the efficacy of government intervention as a tool to correct market failure. Embedded in the EU and US agency evaluations of the highly visible matters mentioned earlier are differing assumptions about the adroitness of rivals and purchasers to reposition themselves in the face of exclusionary conduct by a dominant rival, the appropriate tradeoff between short-term benefits of a challenged practice and long-term effects, and the robustness of future entry as a means for disciplining businesses that presently enjoy dominance. Putting these and other critical assumptions front and center in the discussion, along with the bases for the assumptions, would advance the transatlantic relationship in the future.

977 The preeminent account of this history is David J. Gerber, Law and Competition in Twentieth Century Europe – Protecting Prometheus (Oxford paperback ed. 2001).

Focusing on How Institutional Design Affects Doctrine. In discussing competition law, there is a tendency for academics, enforcement officials, and practitioners to focus on developments in doctrine and policy as well as to assign secondary significance to the institutional arrangements by which doctrine and policy are shaped. As I have suggested above, this tendency can cause one to overlook the important role that the design of institutions can play in influencing substantive results. It is impossible to understand the development of EU and US competition law without considering the impact of:

– Private rights of action and mandatory treble damages in shaping the views of US courts and enforcement agencies about the appropriate boundaries of substantive doctrine concerning antitrust liability.
– The experience gained by European competition authorities in carrying out responsibilities for policing excessive pricing as an abuse of dominance in informing their views about the wisdom and administrability of measures that mandate access to specific assets.
– The nature and timing of judicial oversight in merger control.
– The internal organization of competition agencies, including the placement of economists within the authority organization chart and the procedure for their participation in the decision to prosecute.
– The decision to accept a revolving door in recruitment – the manner in which the competition agency recruits personnel and the backgrounds of the agency's professionals who work for the organizations and the parties who appear before the authorities.

Consider, again, the possible impact of creating robust private rights of action in the US style – with mandatory treble damages, with relatively permissive standards for the aggregation of class claims, and asymmetric fee-shifting in which only a prevailing plaintiff recovers its fees.[978] In establishing this variant of private enforcement, the jurisdiction must keep in mind the possible interaction between the operation of private rights of action and public law enforcement. If judges fear that the private party incentives to sue are misaligned with the larger interests of the public (put another way, when the juridical tribunals do not trust the private plaintiff as much as they trust a public prosecutor), or they fear that the remedial scheme (e.g. mandatory treble damages for all offenses) deters legitimate business

978 The discussion here is based in part on William E. Kovacic, Public Participation in the Enforcement of Public Competition Laws, in Current Competition Law Volume II, at 167 (Mads Andenas et al. eds., 2004).

conduct excessively, the courts will use measures within their control to correct the perceived imbalance. The juridical tribunals may "equilibrate" the antitrust system by constructing doctrinal tests under the rubric of "standing" or "injury" that make it harder for the private party to pursue its case; adjust evidentiary requirements that must be satisfied to prove violations; or alter substantive liability rules in ways that make it more difficult for the plaintiff to establish the defendant's liability.

The first of these methods only governs suits by private plaintiffs. Of particular significance to public enforcement authorities is the possibility that the courts, in using the second and third measures listed above, will endorse principles that apply to the resolution of all antitrust disputes, regardless of the plaintiff's identity. In the course of making adjustments in evidentiary tests or substantive standards to correct for perceived infirmities in private rights of action, the jurisdiction may create rules of general applicability that encumber public prosecutors as much as private litigants.

This hypothesis helps explain the modern evolution of US antitrust doctrine. Since the mid-1970s, the courts have established relatively demanding standards that private plaintiffs must satisfy to demonstrate that they have standing to press antitrust claims, and have suffered "antitrust injury."[979] In this period, the jurisdiction has endorsed evidentiary tests that make it more difficult for plaintiffs to prove concerted action involving allegations of unlawful horizontal and vertical contractual restraints. With some variation, courts also have given dominant firms comparatively greater freedom to choose pricing and product development strategies.

Collectively, these developments have narrowed the scope of the US antitrust system. Most of the critical judicial decisions in this evolution of doctrine have involved private plaintiffs pressing treble damage claims. Perhaps the most interesting area to consider the possible interaction between the private right of action and the development of doctrine involves the fields of monopolization and attempted monopolization law. Litigation involving exclusionary conduct by IBM provides a useful illustration.[980] In the late 1960s, the Department of Justice initiated an abuse of dominance case that sought, among other ends, to break IBM up into several new companies. By 1975, roughly 45 private suits had been filed

979 These requirements are described in ABA Section of Antitrust Law, Antitrust Law Developments 812-850 (6THed. 2007).

980 For a discussion of the government and private suits against IBM in the late 1960s and in the 1970s, see William E. Kovacic, Designing Antitrust Remedies for Dominant Firm Misconduct, 31 Connecticut Law Review 1285, 1289-90 (1999).

against IBM alleging unlawful exclusionary conduct and seeking treble damages against IBM. The sum of all damage claims in the private cases exceeded $4 billion – a considerable amount at the time.

As far as I am concerned, courts reacted to the private cases with apprehension and were ill at ease with the possibility that a finding of illegal monopolization would trigger the imposition of massive damage awards against IBM. The jurisdiction in these matters could not refuse to treble damages if they found unlawful conduct, but they could interpret the law in ways that resulted in a finding of no liability. IBM paid settlements to a small number of the private claimants, but it achieved vindication in most of the private cases. The results in the private damage cases against IBM and several other leading US industrial firms in this period imbued monopolization doctrine with analytical approaches and conceptual perspectives that viewed intervention skeptically.

My hypothesis about the US competition policy experience is that US antitrust doctrine would have taken a somewhat different path had there been no private rights of action, or if the remedy had been less potent – for example, limiting recovery to actual damages, or permitting trebling only for violations of *per se* offenses, such as horizontal price-fixing. Specifically, US doctrine would have assumed a more intervention-oriented character if the power to enforce the US competition statutes were vested exclusively in public enforcement authorities, or if the private right of action had been circumscribed in one or more of the ways indicated above.

This raises the question what will happen in the EU and its Member States, if private enforcement grows more robust. My tentative prediction is that an expansion of private rights could lead judicial tribunals to adjust doctrine in ways that shrink the zone of liability. For example, an expansion in private enforcement could cause European abuse of dominance doctrine to converge more closely upon the US liability standards governing monopolization.

Devoting Attention to Inter- and Intrajurisdictional Multiplicity and Interdependency. Efforts to formulate effective competition policy will increasingly require EU and US competition agencies to study more closely how other government institutions affect the competitive process. To an important degree, both jurisdictions resemble a policymaking archipelago, in which various public bodies, other than the antitrust agency, deeply influence the state of competition.[981] Too often each policy island acts in relative isolation, with a terribly incomplete awareness of how its behavior affects the entire archipelago. It is ever more apparent that antitrust agencies must use non-litigation policy instruments to build the intellectual and policy infrastructure that connects the islands and engenders a government-wide ethic that promotes competition.

To build this infrastructure requires antitrust authorities to make efforts to identify and understand the relevant interdependencies, and to build relationships with other public instrumentalities. This is particularly evident in the relationship between competition policy and intellectual property.[982] Better coordination could limit inconsistencies between the two systems and ensure that both can more effectively encourage innovation and competition. While cooperation and convergence activities involving competition policy and intellectual property policy have grown more intense in recent years, to date they have tended to be intra-disciplinary. Few cooperation and convergence activities account for the interdependency of both regimes.

5.2 MEANS

Members of the EU and US competition policy community could use several means to address the conceptual issues outlined above. Most of the instruments involve a reorientation of bilateral activity to invest more expansively in a knowledge base that would inform routine discussions at all three levels of the NTA framework. Possible specific techniques are summarized below.

Periodic Comprehensive Reviews of Institutional Arrangements. Both jurisdictions at regular intervals should undertake a basic evaluation of the effectiveness of their competition policy institutions. In many respects, the EU stands far ahead of the US in carrying out this type of assessment. The major institutional reforms introduced in the past year – modernization, reorganization of DG Competition, and the introduction of a new position of economic advisor – indicate the EU's close attention to these issues.

981 The dimensions and consequences of policymaking fragmentation within individual jurisdictions are analyzed in Andrew I. Gavil, William E. Kovacic, Jonathan B. Baker, Antitrust Law in Perspective: Cases, Concepts and Problems in Competition Policy (2002). See also William E. Kovacic, Toward a Domestic Competition Network, in Competition Laws in Conflict: Antitrust Jurisdiction in the Global Economy 316 (Richard A. Epstein & Michael S. Greve eds., 2004) (describing fragmentation of policymaking affecting competition in U.S.).

982 See William E. Kovacic & Andreas Reindl, An Interdisciplinary Approach to Improving Competition Policy and Intellectual Policy, 28 Fordham International Law Journal 1062 (2005).

Key focal points for a parallel inquiry in the US ought to include the scope of coverage of the competition policy system, the adequacy of existing substantive rules and remedies, the type and consequences of public enforcement, the role of private rights of action, and the design and administration of public enforcement bodies. Such an assessment should involve participation of government officials, private parties, consumer groups, and academics. Given the continuing changes that confront competition agencies, the two systems should undertake this comprehensive assessment no less than once per decade.

Ex Post Evaluation. The EU and the US routinely should evaluate past policy interventions and the quality of their administrative processes.[983] In every budget cycle, each authority should allocate some resources to the ex post study of law enforcement and advocacy outcomes. Beyond studying what it has achieved, the authority may choose selected elements of its enforcement process and methodology for assessment. Rather than treating ex post evaluation as a purely optional, luxury component of policy making, we must regard the analysis of past outcomes and practices as a natural and necessary element of responsible public administration. Even if definitive measurements are unattainable, there is considerable room for progress in determining whether actual experience bears out the assumptions that guide our acts. One element of the process of examining past decisions would be the type of detailed case study mentioned earlier in this paper. An elaborate deconstruction of specific cases would provide an informative basis for analyzing differences in philosophy and substantive perspective, and for identifying variations in procedure.[984]

Enhancement and Disclosure of Data Bases. The EU and the US should prepare and provide a full statistical profile of their activity. The maintenance and public disclosure of comprehensive, informative data bases on enforcement are distressingly uncommon in our field. Every authority should take the seemingly pedestrian, but often neglected step of developing and making publicly available a data base that (a) reports each case initiated, (b) provides the subsequent procedural and decisional history of the case, and (c) assembles aggregate statistics each year by type of case. Each agency should develop and apply a classification scheme

983 The potential contributions of ex post analysis of completed government interventions to the development of competition policy are examined in William E. Kovacic, Using Ex Post Assessments to Improve the Performance of Competition Policy Authorities, 31 J. Corp. L. 503 (2006).

984 For a suggestion of the content of such a case study, see William E. Kovacic, Transatlantic Turbulence: The Boeing-McDonnell Douglas Merger and International Competition Policy, 68 Antitrust Law Journal 805 (2001).

that permits its own staff and external observers to see how many matters of a given type the institution has initiated and to know the identity of specific matters included in category of enforcement activity. Among other ends, a current and historically complete enforcement data base would promote better understanding and analysis, inside and outside the organization, of trends in enforcement activity.[985] For example, access to such data bases would give competition agencies greater ability to benchmark their operations with their peers.

Assessment and Enhancement of Human Capital. Continuous institutional improvement will require the EU and US competition agencies to regularly evaluate their human capital. The capacity of staff deeply influences what they can accomplish. The agencies routinely must examine the fit between their activities, and the expertise of their professionals. The authorities could share views on developing a systematic training regimen for upgrading the skills of their professionals. For example, where the agencies are active in areas such as intellectual property that require special expertise, it is essential to explore whether they have acquired the requisite specialized skills – for example, by hiring some patent attorneys. The experiences of the authorities with entry and lateral recruitment – including the costs and benefits of the revolving door – would be useful focal points for discussion. A fuller program of staff exchanges also might supply an effective means for improving the discussion at the staff level and educating each agency on how the other builds its capability.

Investments in Competition Policy R & D and Policy Planning. An essential element of continuous institutional improvement is the enhancement of the competition agency's knowledge base. In many activities, particularly in conducting advocacy, the effectiveness depends on establishing intellectual leadership. To generate good ideas and demonstrate the empirical soundness of specific policy recommendations, authorities must invest resources in what former FTC Chairman Timothy Muris has called "competition policy research and development."[986] Regular outlays for the purpose serve to address the recurring criticism that policy lags unacceptably in understanding the commercial phenomena it seeks to react.

985 For a formative treatment of the value of good statistical records for the analysis of competition policy, see Richard A. Posner, A Statistical Study of Antitrust Enforcement, 13 Journal of Law & Economics 365 (1970).

986 The concept of "competition policy research and development" and its role in determining institutional capability are analyzed in Timothy J. Muris, Looking forward: The Federal Trade Commission and the Future *Development of U.S.* Competition Policy, 2 Columbia Business Law Review 359 (2003).

Examining the R&D function is one element of exploring larger questions about how the agencies should set priorities and, within the larger competition policy community, about what they should do. The question of setting priorities is likely to gain greater importance in the EU as certain functions that once occupied considerable EU attention devolve to the Member States, freeing resources for the Commission to design new programs. The deliberation of how we measure agency performance, and assess the mix of its activities, is a topic for a larger discussion within the competition community. For example, on the scorecard by which we measure competition agencies, there is continuing awareness that we should count the suppression of harmful public intervention just as heavily as the prosecution of a case that forestalls a private restraint.[987]

6. CONCLUSION: FUTURE INTERNATIONAL RELATIONSHIPS

The *best* practice in competition policy is the relentless pursuit of *better* practices. A basic implication of past work, and the future program I have suggested here, is that the authorities (and non-government bodies) must be willing to invest significant resources in the development and maintenance of the relationships as a dedicated objective, even though such investments do not immediately generate the outputs – most notably, cases – by which agencies traditionally are measured. The success of the relationships requires outlays in the type of overhead and network building that commentators, practitioners, and, perhaps, legislative appropriations bodies often view with some skepticism. Thus, one challenge is for the competition authorities to develop acceptance of a norm that regards these investments as valuable and necessary.

The competition agencies should also confront the question of how many resources, even in the best of circumstances, they can devote to the construction and maintenance of networks that provide the framework for international relations in this field. The EU and the US are engaged not only in their own bilateral cooperation, but also agreements with other jurisdictions, participation in regional initiatives, and work in multinational networks, such as ICN and the OECD. The EU and US are major partners in all of these overlapping ventures, and each year each agency must decide, through its commitment of personnel,

987 These agencies must confront government restrictions on competition with the same commitment and determination with which they challenge private restraints. See Timothy J. Muris, State Intervention/State Action – A U.S. Perspective (New York, N.Y., Oct. 24. 2003) (remarks before the Fordham Annual Conference in International Antitrust Law & Policy), available at http://www.ftc.gov/speeches/muris/fordham031024.pdf.

to "buy", "sell", or "hold" its position in each venture. Each authority is aware that the participation in these activities cannot be carried out effectively – namely, with good substantive results – except through the allocation of first-rate personnel. There is no point in trying to do this work on the cheap.

The hazard is that the EU, the US, and other countries may experience, or may now be encountering, some measure of international network or relationship fatigue. Thus, a further focus for consideration by the two jurisdictions, individually and jointly, is how best to devote their resources. In this decision, the agencies are likely to regard the transatlantic relationship as a top priority. This is true because of the importance of the interaction to the regulation of transatlantic commerce, and because the EU and the US always will have distinctive interests and common issues owing to their comparatively larger base of experience. Moreover, the EU/US relationship has served, in effect, as a bilateral test bed for substantive concepts and processes that can be rolled out in a larger multinational setting. Experience within the relationship has usefully informed EU and US decisions about what might be accomplished in the larger spheres. As the EU and the US approach perceived limits on how much they can dedicate to this growing collection of international initiatives, the larger competition policy community will need to abandon a case-centric vision of what agencies should do, and accept the need for institution building, at home and abroad, as a vital ingredient of sound competition policy for the future.

Małgorzata Krasnodębska-Tomkiel

PERSPECTIVES OF COMPETITION POLICY IN POLAND: ON THE 20TH ANNIVERSARY OF UOKIK

1. INTRODUCTION

Twenty years after the processes of political and economic transformation started in Poland, rivalry among enterprises is an obvious norm underpinning the functioning of a free market where the participants of the market play compete to attract the purchasers' interest in the products and services they offer, that is competition. According to the *Glossary of terms used in EU competition policy* the term "competition" denotes a market situation where sellers of a product or service independently strive (compete) for the attention (interest) of buyers in order to achieve a particular business objective, for example, profits, sales and/or market share. Competitive rivalry between firms may, in particular, focus on prices, quality, customer service, or combinations of these and other factors (circumstances) which customers may value. Fair and undistorted competition is a cornerstone of a market economy[988].

Thus, competition represents one of the fundamental premises of a market economy. At the same time, it is one of the key features distinguishing a free market from a centrally-planned economy that functioned in the post-war Poland until the transformations of 1989.

Being a characteristic of the correct functioning of a market economy and serving consumers' well-being, competition is subject to legal protection guaranteed and implemented both by the Polish legal system and the EU regulations that are in force in Poland.

From the point of view of Polish legislation, the highest-ranking legal act governing the country's economic system is the Constitution of the Republic of Poland of 1997[989]. It states that the Polish economic system is based on a social market economy, founded on the freedom of economic activity, private ownership, and solidarity, dialogue and cooperation between social partners[990]. The freedom of economic

988 *Glossary of terms used in EU competition policy*, Brussels 2002.

989 Dz.U. No. 78, item 483, as amended.

990 Cf. Article 20 of the Constitution.

activity is thus indicated in the Constitution as one of the most important principles and may be limited only by an act of parliament and due to an important public interest[991]. Thus defined, social market economy refers to the ideas implemented by Ludwig Erhard, minister of economy in the government of Konrad Adenauer. The concept is an attempt to find a balance in the State's economic policy between respecting economic freedom and striving for economic growth while controlling inflation and unemployment rates, which is typical for the capitalist system, and the social needs of citizens, such as good labour conditions, social welfare, and satisfactory level of public services. In a system perceived in such a way, one of the vital rationales justifying legal restrictions of the freedom of economic activity is competition policy implemented in the public interest.

However, post-war Germany is not in fact the cradle of competition policy and laws as instruments of State intervention in the freedom of economic activity serving the public interest. First regulations in this respect were adopted around the end of the 19th century in North America – in 1889 in Canada and one year later in the United States. The Sherman Act adopted in 1890 and introducing the prohibition of commercial monopolies between individual states, as well as providing for criminal sanctions for its breaches, (including jail sentence) is still in force today[992]. The adoption of such a restrictive regulation limiting the previously unrestrained freedom of economic activity was a response to pathologies resulting from the absolute lack of interventions in the freedom of trade – strong concentration and cartelisation of the economy functioning under fully liberal principles. The objective of the first (antitrust) regulations counteracting monopolisation was not to put an end to this freedom, but on the contrary – to put an end to unfair and false competition without giving up the conviction that fair competition is a value that should be protected in the public interest. Such assumptions also inspired the legal acts adopted afterwards, such as the Clayton Act or the Act on Federal Trade Commission of 1914[993]. The public bodies responsible for the enforcement

991 Cf. Article 22 of the Constitution.

992 Sherman Act of 2 July 1890 concerned the protection of trade from direct threats and monopolies. On the basis of provisions thereof, jurisdiction was awarded to individual states in order to prevent the infringement of this act. The right to institute proceedings in the case of breach of the act was granted also to US Attorneys. All decisions regarding prohibitions or orders, including the interim ones, under the Sherman Act are to be made at the discretion of the courts. One of the sanctions for the infringement of the prohibition of trusts is seizure of property. In principle, the Act did not concern foreign trade.

993 Clayton Act of 1914 prohibited unfair pricing and distribution practices and introduced limitations concerning concentrations (mergers) of undertakings in the case when it resulted in monopoly or restraining competition on the market. In 1914 the Act on the Federal Trade Commission was passed and it mainly regulated the organisation of the system and responsibilities. Another antitrust authority was established – the Federal Trade Commission – and the scope of its duties was defined in contrast to the tasks of the Department of Justice. This Act also introduces a prohibition of unfair methods of competing in trade. Both of these regulations do not provide for criminal penalties for the infringement of norms included therein.

of antitrust regulations in the USA are: the US Department of Justice[994] and the Federal Trade Commission.

Similar legal instruments emerged in Europe as late as in the interwar period, starting in Germany in 1923. In Poland, the 1933 Act of Cartels and the 1939 Act on Cartel Agreements constituted the beginning of competition protection legislation in Poland[995]. Without a shadow of a doubt, the long break - lasting several dozen of years - in the functioning of an economic system based on a free market during Poland's participation in the Communist bloc controlled by the USSR after World War II, hindered further development of Polish competition legislation. In a centrally-regulated economy oriented at satisfying a permanent deficit, free market and competition had no *raison d'être*.

At that time, fundaments of modern competition legislation were laid down in the Western Europe. German Anticartel Act was passed in 1949 and two years afterwards, the Treaty of Paris establishing the European Coal and Steel Community contained provisions prohibiting the use of unfair anti-competitive practices, i.e. competition restricting agreements, as well as principles on mergers between enterprises[996]. The bans on monopolistic practices were later repeated in the Treaties of Rome establishing the European Economic Community and the European Atomic Energy Community[997].

The development of modern competition legislation in Poland is linked to the political and economic transformations of 1989[998]. The cornerstone in this process was the adoption of the Act of 1990 on counteracting monopolistic practices and the establishment of the Antimonopoly Office entrusted with the duty to enforce the new Act under administrative procedure[999].

994 To be more precise – its Antitrust Department established in 1933. On the other hand, entities aggrieved as a result of infringement of antitrust laws have the right to claim for compensation due to that injury, which may even reach the triple value of the damage incurred due to infringement. Due to the system of class actions, currently 90% of antitrust lawsuits are instituted under this procedure in the USA.

995 The Act on Cartels of 1933 contained an obligation to report cartel agreements to a register kept by the Ministry of Industry and Trade, and simultaneously authorised the Cartel Court (operating at the Supreme Court) to terminate agreements that were detrimental to the State's interest. An amendment to this Act, passed in 1935, provided such authorisation directly for the Ministry of Industry and Trade. The 1939 Act on Cartel Agreements actually did not enter into force due to the outbreak of World War II.

996 Cf. Article 65 and 66 of the Treaty establishing the European Coal and Steel Community.

997 Cf. Article 101 and 102 of the Treaty on the Functioning of the European Union.

998 In 1987 an Act on counteracting monopolistic practices in the national economy was passed, and the enforcement thereof was assigned to the Ministry of Finance.

999 The Act of 24 February 1990 on counteracting monopolistic practices (Dz.U. No. 49, item 318, as amended) has been

When introducing the system of social market economy and the principle of freedom of economic activity, the Polish Constitution allows, as mentioned before, for restrictions thereof due to important public interests. In this respect, the Act of 16 February 2007 on competition and consumer protection, being the comprehensive piece of legislation regulating Polish competition law, appears to be the key act that authorises restrictions of economic freedom in the public interest in the name of values specified in Article 1 of this Act. Defining the subject and scope of the regulation, this provision indicates that the Act determines the conditions for the development and protection of competition and the principles of protecting the interests of enterprises and consumers in the public interest. The Act lays down the rules and procedures of counteracting competition restricting practices (prohibited anti-competitive agreements and abuses of a dominant position), as well as mergers which could lead to a substantial limitation of competition. Pursuant to the principle of extraterritoriality[1000], the Act applies to all practices and mergers that cause or may cause outcomes in Poland. The Act on competition and consumer protection constitutes the foundation for the functioning of the Polish competition authority – the President of Office of Competition and Consumer Protection – and determines its duties, the scope of its operations, the method of appointment and dismissal, as well as the structure of UOKiK through which the authority accomplishes its tasks. Therefore, it can be said that the Act contains material, procedural and systemic norms on the basis of which the Polish system of competition and consumer protection operates.

Looking back, it could be said that this piece of legislation constitutes the next step in the evolution of modern competition law in Poland, initiated by the adoption of the 1990 Act. In this context, the year 2010 is the twentieth anniversary of the competition legislation being in force in Poland and thus the twentieth anniversary of the operations of the Office of Competition and Consumer Protection. The anniversary is a good occasion for summaries that can be useful in so far as they allow defining what actions should be taken in the coming years. Thus, this paper is an attempt at presenting the broad scope of the challenges faced by the Polish competition authority at the beginning of the 21st century.

amended many times and was repealed as late as in 2001 when the Act of 15 December 2000 on competition and consumer protection entered into force (Dz.U. No. 122, item 1319 as amended). The latter was repealed by the now effective Act of 16 February 2007 on competition and consumer protection (Dz.U. No. 50, item 331, as amended), also referred to as Competition Act.

1000 The principle of extraterritoriality means that the competition authority has the competence to counteract restrictions of competition committed by enterprises registered outside of the territory covered by its jurisdiction if the outcomes of these anti-competitive practices occur within this territory.

They can be defined both through current needs – the problems discovered on the market, but also in a long-term perspective, with regard to the far-reaching objectives of the national competition policy and the objectives of the European Union competition policy. The task of the competition authority consists in the application of the legal instruments at its disposal to solve current market problems – to counteract competition restricting practices or to prevent mergers that might lessen competition. In the light of the national law, UOKiK is the only institution responsible for the accomplishment of this task and, thus, it certainly cannot evade responsibility for the consequences of possible negligence in this respect.

On the other hand, the term "competition policy" denotes more than handling cases, imposing fines for anti-competitive practices, or prohibiting mergers that are potentially harmful to competition. Competition policy constitutes an element of economic policy in a broader sense, and as such, falls within the domain of the Council of Ministers, which accepts the national competition strategy and gets other entities, apart from the competition authority, involved in its implementation[1001]. As regards the implementation of the assumptions of competition policy, an important role is also played by the so-called market regulators, such as the President of the Office of Electronic Communications or the President of the Energy Regulatory Office[1002]. In the long-term perspective, legislative and programming initiatives are equally important as they can substantially influence the regulatory surrounding of the economy, making it more pro- or more anti-competitive. The President of the Office of Competition and Consumer Protection participates in these processes, yet not as the sole decision-maker, as it is the case in administrative proceedings. Nonetheless, while defining the challenges and tasks faced by the Polish competition authority, this area should not be overlooked, all the more that it never ceases to play a principal role in the activity of the Office.

UOKiK, just as all institutions, functions under defined legal and organisational conditions. With regard to the said circumstances and limitations, I would like to focus on several factors that, in my opinion, might have substantial influence on

1001 Pursuant to Article 31(4) of the Competition Act, the scope of duties of the President of UOKiK covers solely the development of draft governmental programmes for the development of competition.

1002 The cooperation between the competition authority and the regulators, expressed e.g. in the coordination of certain operations, is very important for the accomplishment of the objectives of the competition policy. For the issues connected therewith on the example of the British model, see S. Rab, *From Ordered Competition – Towards a New Competitive Order? The Role of the UK Competition Commission at the Interface between Sector Regulation and Competition Law*, European Competition Law Review, No. 10/2009.

the Office achieving the pursued objectives and accomplishing its mission. They are connected with the best possible use of resources, powers and tools, i.e. the specific "assets" the Office possesses, respecting, at the same time, the rules which make its activity understandable, socially acceptable and reliable. In this context, tasks related to the need of achieving increased institutional efficiency come to the foreground along with the capability to respond to problems concerning the development of modern sectors of the economy, which additionally requires involvement in the cooperation at the international level, in particular within the European Union.

2. UNIQUE SYSTEM MODEL

The President of the Office of Competition and Consumer Protection performs the function of the Polish competition authority. In the administrative structure, the President of UOKiK is an element of the central government administration and is appointed and dismissed by the President of the Council of Ministers. The Prime Minister supervises the activities of the President of the Office[1003]. Such institutional setup strengthens the position of the President of UOKiK, in particular in comparison with the position of the regulatory bodies in post-monopolistic markets, such as the presidents of the following offices: Energy Regulatory Office, Office of Electronic Communications, Office for Railway Transport or Civil Aviation Office, who, in the light of the applicable regulations, are supervised by relevant ministers. The President of UOKiK is a permanent member of the committees of the Council of Ministers[1004] and thus is authorised to participate in all legislative works of the government, and is additionally obliged to develop draft legal acts on issues within its competence[1005]. This competence, which will be discussed in the further part of this paper, provides the competition authority with the possibility of exercising direct influence on the shape of existing regulations, in particular, ensuring that they are compatible with the rules of competition and consumer protection in a broader sense, thus significantly extending its scope of operations beyond the enforcement of the Act on competition and consumer protection under administrative procedure.

1003 Cf. Article 29 of the Competition Act.

1004 Currently there are the following committees: Committee of the Council of Ministers, European Committee of the Council of Ministers, Committee of the Council of Ministers for Informatisation and Communication.

1005 Cf. Article 31(8) of the Competition Act.

The Office of Competition and Consumer Protection (UOKiK) is an auxiliary apparatus assisting the President of UOKiK. It is composed of the central office in Warsaw and nine branch offices[1006]. The Office's decentralised structure and the division of case-handling tasks between the central office and the branch offices[1007] is typical for the organisation of the Polish system of competition protection, yet it is rarely used outside of Poland. The task of the central office consists mainly in handling cases concerning competition restricting practices that are taking place on national or even broader scale, as well as all merger cases. The branch offices are responsible for the protection of local and regional markets from anti-competitive practices. Pursuant to the Competition Act, all proceedings are instituted *ex officio* and when instituting them the authority should be guided by the rationale of public interest. In the context of this principle, the division of tasks between the central office and the branch offices sets out, to some extent, two mutually complementing perspectives of defining the public interest and determining the priorities of enforcement – the perspective of the entire national market and local and regional markets that are limited in geographic terms.

Protecting competition on these smaller markets has been the focus of UOKiK's special attention and engagement for many years. These markets face numerous events of abuse committed mainly by enterprises with a strong market position, e.g. on the markets related to the provision of utility services, such as waste disposal, the market of water and wastewater services or the market of graveyard and funeral services; but also enterprises entering into collusions, thus violating the prohibition of anti-competitive agreements, e.g. on the market of taxi transport. What is more, the offenders are often local governments themselves or their organisational units, which are bound by restrictions resulting from competition protection law in so far as they provide public services or organise the provision of such services. Such a broad range of infringements, the specific nature of the entities that commit them (e.g. local governments) and the often monopolistic or strongly dominated structure of the markets where the infringements are committed, all make these types of practices particularly detrimental to consumers. Cases that are frequently reported and dealt with by the branch offices would not be prioritised if assessed from the point of view of the entire market; yet, they are of principal importance for the consumers and competitors in the regions they concern. The decentralised

1006 Cf. Article 33 of the Competition Act indicating the following cities as the branch office seats: Bydgoszcz, Gdańsk, Katowice, Kraków, Lublin, Łódź, Poznań, Warszawa and Wrocław.

1007 The Regulation of the Prime Minister of 1 July 2009 on the territorial jurisdiction and scope of competence of the branch offices of the Office of Competition and Consumer Protection (Dz.U. No. 107, item 887).

structure of the Polish competition authority and the division of tasks between its different units allows the authority to prosecute infringements discovered on smaller markets assigning them proper rank and importance in the context of competition policy[1008] implemented with regards to the entire market. Annually, the President of UOKiK handles approximately 200 cases and issues about 100 decisions solely concerning competition restricting practices[1009], out of which the majority are cases concerning infringements committed by enterprises operating on smaller markets. A big number and high effectiveness of the interventions undertaken by the competition authority on these markets proves the efficiency of the legal solution applied. It is also an element that serves the construction of competition culture by means of increased awareness of local communities of the benefits derived by consumers and enterprises from the existence and effective enforcement of antitrust law and competition as a typical feature of a market economy.

Further prosecution of competition infringements on regional and local markets by UOKiK's branch offices should be considered as one of the key tasks faced by the Polish competition authority also in the months and years to come. Increased effectiveness of this type of interventions can be achieved by coordination, in particular in the case of infringements of the same type which occur at a similar point in time on various geographical markets. UOKiK's system of internal consultation aiming to maintain uniformity and correctness of decisions serves improved coordination. The branch offices, constituting components of this system, when handling competition cases, perform the statutory tasks of the President of UOKiK, and all decisions are made on authorisation of the President of the Office[1010]. Optimisation of effectiveness is also achieved by public dissemination of information on the decisions issued. The latter may have a preventive impact discouraging enterprises from embarking on similar behaviour for which other enterprises have been punished.

Absence of the President of UOKiK's fixed term in office might be indicated as a certain weakness of the existing system, in particular in the context of the solutions that were binding in 2001-2007. Under the previous Act on competition

1008 The protection of local markets is included in one of the priorities in the strategic programme document adopted by the Council of Ministers under the name: "Competition policy for 2008-2010".

1009 E.g. in 2008 the President of UOKiK issued 104 decisions concerning cases of competition restricting practices, while in 2009 – 107 such decisions.

1010 The branch offices do not have jurisdictional independence, since while the structure is decentralised, all the powers rest with the President of the Office.

and consumer protection of 2000, the President of UOKiK was appointed in a competitive procedure for a 5-year term in office. The current regulations provide for a competitive appointment procedure, however, they rule out guaranteeing the appointed candidate any fixed term of performing his or her new function. Terms in office are commonly perceived as a significant institutional guarantee of independence for the head of the competition authority and freedom from current political decisions made by the government which might obstruct the effective enforcement of the provisions of the Competition Act. Still, from the formal point of view, the supervision exercised by the Prime Minister does not concern the competition authority's decision-making, since appeals against all types of decisions issued by the authority are examined by independent courts. In this context, at the formal and legal level, the independence of antitrust jurisdiction is guaranteed. Nevertheless, in the long-term perspective and with regard to the benefits following from sound, consistent and predictable competition policy, re-introducing terms in office for the president of the competition authority should be re-considered, taking into consideration the solutions provided for in the Act of 2000 or in many other EU countries.

3. PRIORITISATION

Pursuant to the current Act on competition and consumer protection, cases concerning competition restricting practices may be instituted solely ex officio[1011]. The possibility to submit formal applications for the institution of antitrust proceedings that resulted from the Act of 2000 has been abolished. Therefore, the nature of these proceedings has changed as well. Currently, the information or notifications submitted to UOKiK and concerning the suspicion of competition law infringements do not "automatically" result in a new investigation being instituted by the Office[1012]. They are rather treated as signals and analysed, both in terms of the possibility of addressing the problems by means of the instruments at the disposal of the competition authority and its enforcement priorities.

Pursuant to Article 1 of the Competition Act, each new intervention by the competition authority has to be justified by the public interest, i.e. it has to be proved that the alleged market practices are likely to disturb competition as a phenomenon characterising the functioning of the market. The concept of public

1011 Cf. Article 49(1) of the Competition Act.
1012 Cf. Article 88 of the Competition Act.

interest in competition law is well developed in the case-law, including the case-law of the Supreme Court[1013]. Courts require that a proper justification of the occurrence of the premise of infringement of the public interest be included in each decision confirming the application of competition restricting practices in a given case. In this context, it can be said that the interpretation of the term of public interest made for the needs of particular cases and done in the light of the existing case law, determines the scope of the competition authority's enforcement discretion. In the cases where the public interest has not been violated since they are individual disputes, it is not justified or possible to institute administrative competition proceedings. Consequently, the nature of antitrust proceedings is inquisitorial and the ultimate decision whether to open a case or not is made by the authority acting in public interest.

The President of UOKiK functions within the structures of government administration. Appeals against decisions issued by the President of UOKiK are examined by independent courts[1014]. The desired priority directions of future actions undertaken by the competition authority are included in the specially devised strategic documents adopted by the Council of Ministers every two or three years. Currently the binding document in this respect is the *Competition Policy for 2008-2010*[1015], which indicates such priority areas of action of the competition authority: a) increasing the effectiveness of the competition authority's operations adjusting to the changes in the economy concerning globalisation and development of new technologies, which requires improvements in inspection procedures, including searches of electronic data storage; b) further development of the leniency programme; c) improvements in the system of state aid monitoring; d) enhancements in the methodology of predicting the outcomes

1013 The term "public interest" is not a term of fixed and uniform definition. In each case, it should be defined and specified in detail. The President of the Office of Competition and Consumer Protection should be an advocate of public interest since it results from his or her tasks as a part of the structure of public administration. The existence of public interest should be assessed from a broader view, with regard to the entirety of negative outcomes of an enterprise's actions within a specified market (Judgement of the Supreme Court of 24 July 2003, reference No. I CKN 496/01, not published). An infringement of public interest takes place when the conduct covered by antitrust proceedings causes or might have caused disadvantageous – from the point of view of the objectives of antitrust legislation – results on the market, i.e. influence the quantity, quality, price of a product, or the choice for the consumer or other purchaser. The number of entities affected by the outcomes of competition restricting practices is not significant from the point of view of the Competition Act's applicability, since the decision on that depends on whether the behaviour displays the attributes of a competition restricting practice (Judgement of the Supreme Court of 16 October 2008, reference No. III SK 2/08, not published).

1014 Pursuant to Article 81 of the Competition Act, one has the right to lodge an appeal against the decision of the President of UOKiK to the Court of Competition and Consumer Protection, which is a specialised department of the Regional Court in Warsaw. The court's judgement may be appealed to the Court of Appeal, whose judgement, in turn, may be challenged by way of a cassation appeal pursuant to the Code of Civil Procedure.

1015 Available at: http://www.uokik.gov.pl/aktualnosci.php?news_id=450.

of market transactions, in particular employing a more economic approach in this respect; e) permanent and coordinated monitoring of local markets in order to effectively eliminate anti-competitive practices occurring on these markets; f) combating anti-competitive practices on markets subject to de-monopolisation and liberalisation; g) supporting the creation of competition in the regulated sectors, i.e. electronic communications, electricity, railway transport, aviation and postal services, as well as endeavours aiming at the liberalisation of the access to liberal professions; h) information and education in a broad sense addressed to all market participants and active involvement on the international fora aimed to serve increased effectiveness of investigation measures in the case of cross-border abuses.

The scope of priorities is, therefore, quite broad and concerns all the areas of activity of the Office. With reference to enforcement competence, special attention is focused on specific types of abuses that should be eliminated in the first place, as they represent a serious threat to the state of competition (e.g. abuses on post-monopolistic markets, cartels, misconduct on local markets). *The Competition Policy* also points to the obligation to systematically improve the instruments available in order to promote better efficiency of actions (e.g. the leniency programme[1016]). The fullest possible implementation of the priorities falls within the duties of the competition authority, which has the obligation to submit a report on the implementation of the *Policy's* objectives to the Council of Ministers, once the *Policy* is concluded.

In this context, it should be pointed out that under the existing legal conditions the competition authority enjoys a substantial margin of discretion in the determination of priorities and implementation of is statutory powers, in particular in terms of antitrust enforcement. While defining these priorities, this authority has the obligation to take into consideration the premise of public interest infringement by defining it in the light of the case law, as well as the priorities defined in strategic governmental documents, currently – in the *Competition Policy for 2008-2010*. Additionally, when setting priorities, the authority should also take into account the current problems emerging on the market, including those indicated in the complaints and notifications submitted to the Office. The fact that since the Act of 2007 entered into force[1017], the authority is not bound by applications for the

1016 More information on this will be presented in the further parts of this text.
1017 Cf. Article 86 and 88 of the Competition Act.

institution of proceedings, should lead the authority to embark on a larger-scale efforts to acquire information on the existing irregularities, in particular by means of extending the scope of the market studies and analyses it conducts, and by increasing the effectiveness of other legal instruments serving the acquisition of information, such as the leniency programme or searches of electronic data storage. Appropriate, meaning adequate from the point of view of the existing problems, determination of priorities by the competition authority is not possible without broad access to information about the market provided directly by its participants. Hence, the President of UOKiK should carefully consider all measures that may serve to acquire such information, as well as improve its ability to analyse them and draw conclusions on that basis. They are elements of a specific methodology of operations, a toolkit without which it would not be possible for the competition authority to effectively implement its statutory competence and to pursue the objectives of the competition policy indicated in the strategy adopted by the Council of Ministers.

4. PREDICTABILITY OF ACTIONS

In continental Europe, including Poland, competition law is a part of a broader area of public commercial law, while competition policy forms an element of the state economic policy. This manifests itself in the fact that competition policy strategy is adopted by the Council of Ministers. Consequently, we are dealing with an area where – at least according to the applicable regulations – the constitutional principle of freedom of economic activity is of essential importance, and which can be limited only by an act of parliament and due to important public interest. This means that introducing limitations of economic freedom each time has to be not only notified (obligatory promulgation of acts of parliament), but it also has to be thoroughly grounded.

By serving fair competition, however, antitrust law bans anti-competitive market practices and introduces obligations to notify intended mergers between enterprises. They result both from the Act on competition and consumer protection of 2007 and from the EU competition law that has been in force in Poland since 1 May 2004. The substantive provisions of the Polish antitrust law are fully convergent with the corresponding European regulations, in particular as regards competition restricting practices. Adopting the principle of complete convergence during the process of harmonising the Polish law with the European norms on the eve of Poland's accession to the European Union was aimed primarily to increase the transparency of the relevant regulations and the effectiveness of their application to the benefit of protecting competition on the market. It has been assumed that enterprises should be subject to uniform standards as regards antitrust regulations, irrespective of the fact whether they conduct business only on the Polish market or whether the scope of their business results in some of their market practices being potentially subject to evaluation in terms of their compatibility with the EU law. Applying uniform standards was supposed to facilitate better business environment in Poland after the accession to the EU. In consequence, the laws applicable in Poland are convergent with the standards that are in force on the entire EU market, which, from the point of view of legal certainty, should be seen as a positive factor.

However, enterprises which are the addressees of antitrust norms need the rules in force to be clear and predictable, which, in this case, depends not only on the exact wording of the specific provisions but, to a great extent, on their interpretation, the body of past administrative decisions and court case law. To accommodate these needs, and in the context of the standards present in other EU Member States and the United States, the Polish competition authority published its policy on the enforcement of specific provisions of the Competition Act. In the first instance, rules concerning the calculation of fines imposed for competition restricting practices were published in the Guidelines on setting fines for competition restricting practices, effective as of 1 January 2009.[1018]. Although this document is not an act of law and, therefore, has no binding effect, it was developed and published is in accordance with the applicable provisions of the Competition Act[1019].

The Guidelines indicate a method of setting fines whereby the starting point is a three-stage gradation of the infringements. The most severe sanctions are administered for hard-core competition infringements, which mainly include particularly detrimental horizontal agreements – price fixing, bid-rigging, dividing markets, collective boycotts and abuses of dominance aimed at complete elimination of competition from the market. Accordingly, lower sanctions are envisaged for serious infringements (remaining horizontal agreements, vertical

1018 Promulgated in the Official Journal of UOKiK No. 4/2008; available also at: http://www.uokik.gov.pl/dzienniki_urzedowe_uokik2.php.

1019 Pursuant to Article 32(4) of the Competition Act, the Official Journal of UOKiK contains *inter alia* guidelines and interpretations of major importance for the application of antitrust provisions. The guidelines concerning the method of calculating fines are included in this catalogue.

pricing agreements) and the remaining types of abuses. Apart from the nature of the infringement, the fine also depends on its detrimental influence on the market and its durations (long-term, i.e. lasting over one year, abuses are treated more strictly). The mitigating circumstances may include: passive role in the infringement, acting under coercion, discontinuing the practice early on in the process, removing its effects on voluntary basis or cooperating with the authority in the course of its proceedings. On the other hand, the fine may by stricter if the enterprise concerned was a leader or initiator of the practice, coerced other enterprises to get involved in the infringement, undertook the abuses intentionally or had infringed the antitrust law in the past. Fines calculated on the basis of the Guidelines must not exceed the top ceiling of fine specified in the Act[1020]. Exceptionally, fines substantially lower than it would result from the calculations may be imposed, in so far as the circumstances of a given case justify it.

Apart from the Guidelines, in 2009 modifications of the procedural provisions concerning the functioning of the leniency programme[1021] were adopted with the view to make this instrument easier to use for enterprises interested in avoiding financial sanctions for the participation in agreements prohibited under the law, due to cooperation with the competition authority under the conditions defined in the binding provisions. The new Regulation of the Council of Ministers of 26 January 2009 concerning the mode of proceeding in cases of enterprises' applications to the President of the Office of Competition and Consumer Protection for immunity from or reduction of fines[1022] provides *inter alia* for new possibilities of submitting leniency applications, harmonising the Polish regulation with the Model Leniency Programme adopted by the European Competition Network[1023]. The most important issue is introducing of a marker system guaranteeing the enterprise which was the first to submit an application the first place in a queue

1020 Pursuant to Article 106(1) of the Competition Act, the President of the Office is authorised to impose on an enterprise, by means of a decision, a fine amounting to no more than 10% of its revenues obtained in the financial year preceding the year of imposing the fine.

1021 The term "leniency" denotes programmes of mitigating penalties for contrite cartel participants, and are commonly regarded as one of the most efficient instruments for combating the most dangerous infringements of competition law, namely the cartels. This instrument is based on the institution of immunity witness found in criminal proceedings. In essence, leniency consists in encouraging members of an illegal anti-competitive agreement to break the mutually beneficial solidarity with the remaining cartel participants and to submit information on the existence of the cartel to the competition authority. In return for such information, the enterprise who "stepped out of line" may avoid the entire penalty for the participation in it (if it reports as first) or a substantial reduction thereof (if itsapplication was second). A leniency programme has been functioning in Poland since 1 April 2004. The current legal basis for the programme is Article 109-110 of the Competition Act.

1022 Dz.U. No. 20, item 109.

1023 Model Leniency Programme has been adopted by the representatives of EU national competition authorities and the European Commission in 2006. It defines the standards that should be adopted by all ECN members in their national leniency programmes in order to achieve "soft" harmonisation within the EU.

even if the application was not complete at the moment of submission[1024]. There is a time limit by which the application has to be rectified otherwise the interested enterprise loses its privileged place in the queue. Such a solution is important in so far as in the leniency programme only the first enterprise to initiate cooperation with the authority under the conditions defined in the Act can count on a complete immunity from fines. In some cases, it can be a matter of days, hours or even minutes (it is the delivery of the application that counts) and, therefore, obtaining the marker is of essential importance and encourages enterprises to use leniency as an advantageous solution that provides legal certainty. Another important issue regulated in the new Regulation concerns summary applications, which constitute an abridged version of the notifications submitted to the European Commission and to the competition authorities of the EU Member States as well. In the case when the Commission does not institute proceedings concerning a case where a leniency application was submitted, the national authority may handle the case in question and request the enterprise which submitted the summary application to provide necessary information.

An essential element for the success of the leniency programme is good communications between the enterprise and the authority. Therefore, for the purpose of further improvements in this respect, apart from the above-mentioned amendment of the Regulation, the President of UOKiK, following other authorities, issued Guidelines on the leniency programme[1025]. They are supposed to be a specific set of instructions explaining the practical aspects of using the Polish leniency programme to interested enterprises. One of the most important – in particular from the point of view of potential leniency applicants – elements of the new Guidelines is the indication of the methodology of reducing fines for enterprises which are not eligible to a complete immunity from fines. In Poland only the enterprise which applies for leniency as the first one and meets the requirements defined in the Act can count on a total immunity from fines. Subsequent applicants in the queue can expect a reduction of fines that, in the context of the Guidelines on leniency, will be made in the light of the above-mentioned Guidelines on setting fines for competition restricting practices. Thus e.g. in antitrust proceedings in which three applications for leniency were submitted, the situation will be the following: the enterprise which applied for leniency as the first one and meets

1024 The legal basis is constituted by Article 5 of the Regulation.

1025 "Guidelines of the President of the Office of Competition and Consumer Protection on the leniency programme (the procedure for submission and proceeding with the applications for immunity from or reduction of fines – 'applications for leniency')" are available at: http://www.uokik.gov.pl/program_lagodzenia_kar2.php.

the requirements defined in the Act can count on a total immunity from fines. In the case of two subsequent applicants, the competition authority calculates appropriate fines on the basis of the above-mentioned Guidelines. Afterwards, thus calculated fines will then be proportionally reduced by no more than 50% in the case of the second applicant, and to no more than 30% in the case of the third applicant[1026]. Such a method of proceeding is a solution that is in accordance with the applicable regulations concerning fines and leniency, and besides it is consistent and beneficial for the enterprises.

In the light of the rules on administrative proceedings and the Act on competition and consumer protection[1027], it is the competition authority's obligation to apply the law in a transparent manner that is predictable for the addressees of the norms – the enterprises. The issuance of the above-mentioned Guidelines fulfils this requirement. These documents contain instructions allowing the interested enterprises to initially estimate the fines for particular types of infringements and the reduction they can count on in the case of applying for leniency. On the basis of data set in such a manner, it should be easier for an enterprise that infringed the statutory prohibition of concluding competition restricting agreements to decide whether it "pays off" to cooperate with the competition authority under the leniency procedure. This way the Polish leniency programme is more predictable and in consequence more enterprise-friendly. Additionally, the issuance of the Guidelines constitutes an implementation of the *Competition Policy for 2008-2010*.

The entry into force of the above-mentioned Regulation and the publication of the Guidelines was accompanied by informational measures planned by the competition authority and aimed at raising the awareness about the new regulations and provisions of the antitrust law that are binding for enterprises[1028].

Admittedly, according to the Latin maxim *ignorantia iuris nocet*, the responsibility, including criminal and administrative responsibility, for the infringement of antitrust law is of objective nature, irrespective of the guilt or awareness of the

1026 Cf. point 31 of the Guidelines of the President of the Office of Competition and Consumer Protection on the leniency programme (the procedure for submission and proceeding with the applications for immunity from or reduction of fines – 'applications for leniency').

1027 Article 32(4) of the Competition and Consumer Protection sets forth an obligation to publish information, notifications, announcements, guidelines and interpretations that are of major importance for the application of the law.

1028 They consisted mainly in launching a special phone number (hotline) for enterprises interested in the issue of leniency or broader information on the prohibition of competition restricting agreements, as well as media information campaigns and supply of sets of information directly to possibly interested enterprises.

person who infringes the rules, however, initiatives simplifying or explaining the binding regulations make sense from the perspective of a long-term competition policy. With regard to the examples of initiatives provided, it should be recognised that they are a step forward on the path towards the solutions functioning in developed market economies. It can be expected that a transparent, predictable and consistently applied fining policy will contribute to the implementation of the objectives of the antitrust law by means of increased enterprises' trust in the market and the mechanisms which regulate it. Accomplishing this objective will depend to a great degree on consistent implementation of a transparent competition policy in a long-term perspective. It is related both to the issue of antitrust enforcement, disclosure of information and knowledge about planned activities (to the degree allowed by the Act and the operating standards of antitrust authorities), as well as unambiguous and publicly voiced support by the President of UOKiK for pro-competitive solutions that are advantageous for consumers during the legislative process, development of strategic governmental documents and other acts that can exert influence on the market and the state of the competition.

5. PRO-COMPETITIVE REGULATORY ENVIRONMENT

The President of the Office of Competition and Consumer Protection is an authority belonging to the central government administration, subordinated directly to the President of the Council of Ministers and thus independent from the ministers responsible for different sectoral policies. Such a solution allows the President of UOKiK to directly participate in all legislative works in the Council of Ministers. This means that all draft legislative acts and other documents submitted for examination to the Council of Ministers are previously submitted, under inter-ministerial arrangements, to the competition authority, which analyses their influence on the state of competition on the market and the interests of consumers. Any remarks or reservations submitted by UOKiK are subject to discussion at committees of the Council of Ministers and meetings of the Council of Ministers unless they have been explained or accepted beforehand by the particular legislation's authors. As part of its legislative work, UOKiK provides opinions for approximately 2 000 documents annually[1029].

1029 Cf. Report on the activity of UOKiK, 2008, p. 10 et seq., available at: http://www.uokik.gov.pl/sprawozdania_z_dzialalnosci_urzedu.php.

This part of the Office's activity, while apparently remaining aside and far from the mainstream, i.e. enforcement actions, is one of the most important elements of the activity of the Polish competition authority and thus distinguishes it from the majority of its foreign counterparts that do not have such competence. This activity is so important since preventing laws that are detrimental from the point of view of the values protected by the Office from being adopted allows to avoid disadvantageous market outcomes in the long-term perspective. In the case of certain regulations, these outcomes might simply come down to monopolisation of markets or substituting competition "on the market" for competition "for the market", which, as a manifestation of a specific control of the access to certain types of activity, should be introduced after deep consideration and preceded with a thorough analysis of market outcomes of such solutions, a point which is unfortunately often forgotten. Structural restrictions of competition, which are allowed on the basis of the applicable law, must not be subsequently efficiently eliminated as a result of anti-trust proceedings. Pursuant to Article 3 of the Competition Act, the provisions of the antitrust law included therein are not applicable to competition restrictions that are allowed on the basis of other acts of parliament. In this context, the issue of efficient prevention of legal solutions that are detrimental to competition rises to the rank of one of the most important missions of UOKiK.

Draft legal acts that are unfavourable to competition have been emerging on a regular basis, however, particularly often in the periods of economic slowdown or recession when there is greater social and political acceptance for the adoption of protectionist or anti-competitive solutions presented as a remedy for resolving economic problems, organisation of the market or putting an end to inequity in the form of excessive prices or simply varying prices.

The credibility of the competition authority, as well as a realistic assessment of the market situation with regard to periodic changes of business cycles, make it necessary for the competition authority to consistently oppose such proposals by indicating their irrationality in the long-term perspective or by presenting proposals that represent an alternative solution (not detrimental or less detrimental)[1030].

1030 Cf. N. Kroes, "Competition law in an economic crisis", Opening address at 13th Annual Competition Conference of the International Bar Association Fiesole, 11.09.2009, available at: http://ec.europa.eu/commission_barroso/kroes/speeches_en.html; B. Tranholm-Schwarz, P. Ohrlander, B. Zanettin, M. Campo, G. Siotis, *The real economy – challenges for competition policy in periods of retrenchment*, Competition Policy Newsletter No. 1/2009.

Talking about UOKiK's legislative interventions, it is at least worth to mention the draft Act on pharmaceutical law[1031], which envisaged the introduction of fixed margins and re-sale prices of pharmaceuticals refunded by the National Health Fund, and put a 1 percent cap on the total number of pharmacies that one capital group could possess in a *voivodeship* (province). In the Office's opinion the draft solutions had no rational economic substantiation. The proposed price standardisation would have lead to the elimination of competition within limits permitted under law, which can hardly be considered advantageous for patients – buyers of pharmaceuticals. Suppliers have no motivation to make standardised prices lower. On the other hand, the restrictions concerning the development of pharmacies belonging to one chain limited the freedom of economic activity and market competition of a specific group of entities, resulting in unjustified favouring of their competitors.

For many years the competition authority has also been continuously opposing changes to the provisions on keeping cleanliness and order, and waste management in *gminas* (smallest units of local administration in Poland), subsequent versions of which boil down to monopolising markets for waste storing and disposal. Specifically, local markets for waste disposal are currently competitive and are constantly monitored by UOKiK's branch offices. Violations occurring therein are often caused by *gminas* which use their dominant position on the market for waste storage to disrupt competition on the market for its disposal. UOKiK has effective tools for eliminating such practices and uses them regularly, issuing decisions prohibiting the abuses and imposing fines on the perpetrators. For example, when an enterprise indicated by the *gmina* is granted the exclusive right to provide waste transport or when the *gmina* implements this task on its own (e.g. through budgetary establishment) – a monopoly is formed on local markets – part of the enterprises (smaller ones in particular) have to leave the market and consumers are deprived of the opportunity to choose better services at lower prices. Introduction of such a restriction under the law would significantly limit competition on markets where it existed for many years.

The negative effects of introducing anti-competition solutions through general legislation have often wider range than e.g. negative practices observed only on certain local or regional markets. They cover the whole country with their scope and give statutory (therefore undisputed in administrative procedure) consent

1031 Draft discussed by UOKiK in 2008.

for restricting the freedom to compete. They can also lead to changes in the market structure, which can be difficult to reverse (even if the provisions are later revoked). For these reasons, the determination displayed by the competition authority in presenting arguments which indicate threats resulting from competition restricting legislation is necessary for a more effective implementation of the objectives and long-term competition policy.

However, on the other hand, participation of the President of UOKiK in legislative works is not limited to attempts to block solutions that are disadvantageous for the market. Equally important is taking initiative or participating in drafting proposals that could lead to creating or consolidating a pro-competitive market structure, as well as for protecting equal and fair competition. This task may be implemented through making proposals with such an objective when working on draft laws. An example of this is the Act of 5 November 2009 on pursuing claims in group proceedings (commonly called the Act on collective redress), which was supported by UOKiK. In the drafting stage, UOKiK made a proposal, which was later included in the Act, to authorise local consumer ombudsmen (instead of only legal professionals) to be a group's representative[1032]. Granting statutory authorisation to represent a group of claimants to a wider range of professional entities may lead to popularising private enforcement as a method for seeking redress, which is consistent with the current trends in EU competition policy[1033].

Proposals presented by UOKiK also include comprehensive analyses of situations on individual markets or specific sectors, completed with recommendations on desired, pro-competitive directions of changes that are worth implementing, particularly on markets which are undergoing gradual liberalisation only now. A good example in this respect is the report "Directions for development of competition and consumers protection in Polish energy sector" prepared in 2008[1034]. This document synthetically defines the most important problems resulting from insufficient competition and insufficient protection of consumer interest on this market, as well as provides a diagnosis of the overall situation in the energy sector. At the same time, it includes a number of recommendations on activities which should be undertaken by the government in order to change the situation. For example, it indicates the need to undertake or stimulate investments

1032 Proposals for authorising also consumer organisations or enterprises' organisations to be a group's representative, submitted by the competition authority during the works on the draft act within the government, were not accepted.

1033 I.e. pursuing claims in private law proceedings (proceedings before civil courts) regarding violations of EU competition law, mainly claims for compensation.

1034 Available at: http://www.uokik.gov.pl/aktualnosci.php?news_id=530.

leading to balancing the supply and demand on this market, highlights the threat of drastic increases in prices of energy for consumers in the case of complete price liberalisation for households with insufficient competition on the market, emphasises the need to consider further integration of the Polish power supply system with the systems of neighbouring countries, underlines the need of introducing greater separation between production and trade, on the one hand, and supply and distribution, on the other, as well as advocates increasing the powers of the regulator of the energy market to enable it to combat discrimination against trade companies from outside capital groups, and suggests a number of activities for increasing consumer mobility on this market. In addition, UOKiK proposed introducing a range of specific changes to the existing provisions in order to improve the protection of consumer rights on the energy market.

The report on the energy market liberalisation is one of a numerous studies and recommendations made by UOKiK, the objective of which is to promote solutions aimed at creating better conditions for the development of competition on the market, outside of the scope of the current legislative works of the government. The competition authority presented recommendations, particularly within various task forces and working groups, on *inter alia,* the timber distribution market, liberalisation of rail transport, postal services or access to liberal professions. In many cases, the implementation, even partial, of the recommendations presented by the Office contributed to the creation of a more competition friendly regulatory environment. This work must continue in the next months and years. Capitalising on its past experiences, the competition authority should try and be an even more effective advocate of the benefits that fair and undistorted competition can bring to consumers and the whole economy. In the ever changing social and economic reality it may even be the most important task of the competition authority. Without it, the mission entrusted to the Office cannot be fully implemented.

6. THE EUROPEAN COMPETITION NETWORK

The most important platform for international cooperation for UOKiK is undoubtedly the European Competition Network[1035]. It operates based on constant

1035 The European Competition Network is a forum for cooperation and exchange of information between the European Commission and competition authorities in all EU Member States. Its creation was related to the implementation of the Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty, which introduced bases for the operation of a new, decentralised system for the application of Community competition law. The essence of the changes applicable as of 1 May 2004 consist in transfering the European Commission's exclusive competence to apply EU competition law in full scope (Article 101 and 102 of the Treaty on the Functioning of the European Union, OJ C115 of 9 May 2008, former Art 81 and 82 of the TEC) to national competition cooperation and exchange of information between all its members, namely the national competition authorities and the European Commission. It mainly concerns the obligation to inform the Commission on proceedings initiated by national authorities on the basis of the Treaty[1036], forwarding draft decisions for opinions[1037], cooperation within the Advisory Committee[1038] or the possibility to exchange information and use it as evidence in antitrust proceedings conducted by individual members of the ECN[1039]. Cooperation regarding inspections conducted by the European Commission and national authorities at the request of the Commission or within the framework of legal assistance to other members of the ECN[1040] are further instruments important for increasing efficiency of Community competition law's enforcement.

Competition law along with the freedoms[1041] is one of the bases of the EU economic system, that is why its effective application and enforcement is crucial for the proper functioning of the internal market. The cooperation of authorised entities obliged to conduct proceedings on violations of Article 101 and 102 of the Treaty on the Functioning of the European Union within the European Competition Network should help achieve this goal. Regulation No 1/2003 envisages mechanisms for restricting political and bureaucratic barriers in this respect to a minimum, imposing at the same time a legal obligation for all the authorities to cooperate with each other. One of the consequences of the elimination of barriers in the intra-Community trade is a broader field for possible abuses on the part of enterprises which unfairly maximise their profits at the expense of competitors. Constant monitoring of the internal market by the national authorities of the 27 members of the EU and the Commission, coordination of activities linked to undertaking interventions on the market, mutual legal assistance and exchange

authorities of the EU Member States and their national courts. These authorities apply provisions of Article 101 and 102 of the Treaty on the Functioning of the European Union (prohibition of competition restricting practices) by conducting antitrust proceedings in public interest. This competence results from Regulation No 1/2003 (as regards national competition authorities – particularly Article 3 of this Regulation). However, at the same time, Regulation No 1/2003 (Article 6 and Article 15 and 16) indicates a significant role that national courts in the EU Member States play in proper functioning of the new system.

1036 Article 11(3) of the Regulation No 1/2003.

1037 Article 11(4) of the Regulation No 1/2003. According to available data, as of 2009, UOKiK closed seven proceedings with decisions stating a violation of EU competition law provisions, the last one pertaining to a cartel established by seven producers of grey cement (decision No DOK-7/2009, available at: http://www.uokik.gov.pl/decyzje_prezesa_uokik3.php).

1038 Article 14 of the Regulation No 1/2003.

1039 According to rules defined in Article 12 of Regulation No 1/2003.

1040 Article 20-22 of Regulation No 1/2003. As of 2009, UOKiK assisted the European Commission twice during an inspection conducted in Poland's territory, last time in September 2009 in Telekomunikacja Polska S.A.

1041 Free movement of goods, persons, services, capital and payments as well as freedom of establishment are the essence of the functioning of the uniform single market.

of information (free movement of evidence) within the ECN should remedy these threats and at the same time – by achieving the synergy effect – improve the effectiveness of all of the authorities' actions.

The cooperation between competition authorities within the ECN is of a multi-faceted nature. The European Competition Network is also an instrument for maintaining uniformity of antitrust enforcement within the whole EU and optimising the use of resources (prevents duplication of efforts), as well as a discussion forum and a platform for exchanging experiences, knowledge and specific "know-how" among European competition authorities.

The activities of the ECN also favour a characteristic "soft" harmonisation of competition provisions applicable in various EU Member States, including systemic solutions or procedural provisions not covered by the scope of the obligatory harmonisation under Regulation No 1/2003. An example of such activities is the above mentioned ECN Leniency Model Programme, whose assumptions have been implemented also in the Polish law. Apart from an "upgraded" leniency programme, we also owe the ECN new types of decisions which can be issued by the President of UOKiK since 1 May 2004, introduced in our national law copying the instruments of the European Commission. This concerns mainly the so-called commitment decision. Pursuant to Article 12 of the Competition Act, if in the course of antitrust proceedings it becomes evident that anti-competitive practices have been applied and if the enterprise concerned voluntarily undertakes to remedy the abuse, the President of UOKiK may accept these commitments by issuing a relevant decision. In the light of statistics, the Polish competition authority is a leader with 42 commitment decisions issued between 2004-2008, compared with 24 and 18 decisions issued by the authorities from France and Italy, respectively, the first and second runner-up, or 12 decisions issued by the European Commission. However, it is obvious that it is not statistics that matters here. Commitment decisions allow to close a case relatively quickly and eliminate market irregularities without the need to carry out often prolonged investigations (a commitment decision may be issued without the need to gather the extensive evidence normally required – prima facie evidence of violation is sufficient) or appellate procedures (in principle, enterprises do not appeal against commitments which they themselves accepted, although it is not formally impossible). This way, fair competition is immediately restored on the market[1042].

1042 E.g. proceedings on a agreement between P4 and Polkomtel concerning the market for providing domestic roaming services ended with a commitment decision, obliging P4 to buy services on an exclusive basis from Polkomtel, see: http://www.uokik.gov.pl/news.php?news_id=1767.

It is also a favourable solution for the enterprise concerned as such decisions do not impose fines[1043].

Another tool helping achieve better effectiveness of antitrust law enforcement, particularly regarding cases of evident competition violations, are the so-called interim measures. Their objective is to limit further negative effects for competition resulting from the application of anti-competitive practices, even before the antitrust proceedings are formally concluded. Article 89 of the Competition Act envisages the possibility of ordering an enterprise which is party to ongoing antitrust proceedings to cease specific activities which disturb competition, if prima facie evidence proves that further application of the practice could result in serious and difficult to remove threats for competition. Such decisions are issued for a fixed term, however, not longer than until the relevant antitrust proceedings are closed and the practices in question recognised as ant-competitive or not[1044]. This power, however, cannot be used too often due to the rule of law. So far, the Polish competition authority issued such decisions in two cases[1045].

7. CONCLUSION

Efficient systems for protecting competition are based on two basic elements – proper legislation and a structure capable of applying it. Good substantive and procedural rules, without proper institutional system dedicated for their enforcement, just like a well managed structure functioning on its own, without relevant powers and operating tools, will not enable efficient competition policy[1046]. That is why, when searching for the ultimate formula for success, which in our case is effective achievement of the goals laid down in the Act, we should take into account both of these factors. Polish substantive competition provisions are fully aligned with the European legislation, which follows both from the process of harmonising Polish law with *acqius communitaire* on the eve of our access to the EU, as well as from Article 3 of Regulation No 1/2003, which *de facto* introduces the principle of supremacy of European law as regards counteracting

1043 The counterpart of this decision in Community law is a decision issued by the European Commission under Article 9 of Regulation No 1/2003.

1044 The European Commission issues interim measures under Article 8 of Regulation No 1/2003.

1045 These were: 1) decisions ordering Telekomunikacja Polska to withhold price increases for international connections with numbers starting with 0-708-1 (decision No DOK-127/05; 2), decision ordering the publisher of "Przegląd Sportowy" to immediately discontinue actions aimed at eliminating the only competitor from the market – "Sport" newspaper (decision No RKT-3/2006); available at: http://www.uokik.gov.pl/decyzje_prezesa_uokik3.php.

1046 P. Lowe, T*he design of competition policy institutions for the 21st century – the experience of the European Commission and DG Competition*, Competition Policy Newsletter No 3/2008.

competition restricting practices. Also the procedural standards set out in the Act on competition and consumer protection of 2007, although not subject to obligatory harmonisation, envisage a set of procedural rights and investigation instruments corresponding to the standards applicable in modern competition law systems, including the EU legislation.

On the other hand, the construction and status of UOKiK is a specific Polish "patent": the agency has a decentralised structure and is responsible for implementing widely understood competition and consumer protection policy. The activity of UOKiK's branch offices, which in principle implement the full scope of the jurisdictional powers of the Office regarding anti-competitive practices on a micro scale of local or regional markets, is very important for the implementation of the Office's objectives, improving efficiency of its operations and creating competition culture among enterprises and consumers. Quick and effective interventions of UOKiK's branch offices not only enhance the markets' competitive structure by solving problems which are important for the people, but also convince the public that fair competition can bring about actual benefits for them and that competition is more advantageous than monopoly. The Branch offices are UOKiK's specific "competitive advantage" when compared with the agencies in the neighbouring countries, which have no similar field units in their structure. A constant improvement of the branch offices' efficiency of activities, also through their coordination, is an important challenge for the Polish competition authority.

The existing law gives the President of UOKiK a relatively big discretion as regards defining enforcement priorities. To prove the legitimacy of undertaking antitrust intervention the competition authority has to demonstrate that a violation of the public interest has taken place in a particular case. At the same time, the general directions of competition policy implementation, including enforcement priorities, are defined in the strategy accepted by the Council of Ministers. Considering such construction of the current competition regulations in Poland, it is very important from the point of view of achieving competition policy goals that the Office carries out its activities in a foreseeable and transparent manner. Enterprises should have wide access to information on law and antitrust enforcement decisions. This may be achieved with stable, not frequently amended legislation, guidelines prepared by the Office, as well as widespread information policy, which has been particularly important in UOKiK's activities. Results of sociological surveys commissioned regularly by the competition authority are good evidence to that: over the years, the knowledge of competition law among enterprises has been increasing, while UOKiK itself is perceived as a necessary, reliable, independent and effective institution[1047].

The Office's power to influence legislation, including the possibility to present its own pro-competitive proposals and request legislative changes, as well as the authority's international cooperation, especially within the ECN, are another set of "assets" of which a well managed agency should make good use in order to implement competition policy objectives for the benefit of the economy and consumers.

Reflecting on the question on how to create a modern competition policy model, it seems increasingly more obvious that good legislation (both, in terms of substantive provisions, as well as procedural regulations) does not solve the whole problem. A well organised and well managed institutional system, which will implement the tasks and responsibilities prescribed in the law, is equally important for achieving competition policy objectives. In this context, certain standards to be applied in the operations of such a forward-looking institution are emphasised. These are: a) grounding all activities and regulations in a profound knowledge of the law, economics and market, b) striving for cohesion (uniformity) and predictability of actions, which is desired by business circles, c) adjusting priorities of actions to available resources, d) reacting to market problems in the quickest possible way, as well as e) disseminating effective information on the benefits resulting from the competition authority's activities to consumers and enterprises[1048]. Considering these criteria, we can say that the Office of Competition and Consumer Protection, as an institution, and the President of the Office, as an administrative authority equipped with powers by the law, have the organisational and intellectual potential to strive to rise up to these ambitious challenges. It will be for the others to judge if we have passed this test successfully, maybe from the perspective of the next big anniversary.

1047 "Study on knowledge of competition protection law and rules for granting state aid among Polish enterprises. Report for the Office of Competition and Consumer Protection", Warszawa 2009, available at: http://www.uokik.gov.pl/ochrona_konkurencji2.php.

1048 P. Lowe, op cit.

Philip Lowe

MAKING MARKETS WORK FOR CONSUMERS: THE CHALLENGE IN EUROPE

1. INTRODUCTION

The objective of the European Commission's competition policy – in common with antitrust authorities across Europe and, indeed, the world – is to make markets work well for the benefit of businesses and consumers.

The reforms that have been introduced in recent years to the EU competition policy instruments, whether the move towards an effects-based approach or the fundamental modernisation and decentralisation of our system for enforcing the European antitrust rules, have ultimately all had the objective of putting consumers at the heart of our concerns.

I will set out briefly the main lines of these reforms and policy orientations, before moving on to the challenges currently faced by the EU competition policy and the European Commission, particularly in light of the financial and economic crisis.

2. TRENDS IN COMPETITION POLICY

2.1 CARTELS

In recent years the Commission has prioritised the most harmful infringements to consumers, so that we have naturally had a strong focus on horizontal cartels to fix prices and share markets. In relation to cartels, DG Competition has implemented a successful leniency policy[1049] – so that nowadays the majority of the Commission's decisions are the result of applications by parties – and we have a dedicated Cartels Directorate. In 2006 we updated our fining policy,[1050] so as to better reflect the economic harm caused by cartels, and increase the deterrent effect of Commission fines. Furthermore, in 2008, we introduced a settlements policy[1051] – which aims to reduce the administrative burden on DG Competition

1049 Commission Notice on Immunity from fines and reduction of fines in cartel cases, Official Journal [2006] C 298/17.

1050 Guidelines on the method of setting fines imposed pursuant to Article 23(2)(a) of Regulation No 1/2003, OJEC [2006] C 210/2.

1051 Commission Regulation (EC) No 622/2008 of 30 June 2008 amending Regulation (EC) No 773/2004, as regards the conduct of settlement procedures in cartel cases, OJEC [2008] L 171/3; Commission Notice on the conduct of settlement and accelerate the process in cases where the parties do not dispute liability, in return for a reduction of fine imposed on the companies who settle.

2.2 SECTOR INQUIRIES

Sector inquiries have also become one of the Commission's key antitrust tools, enabling to carry out in-depth investigations into markets, which are vital to consumers, but which market information suggests might not be working accordingly. The Commission carried out investigations in retail banking, business insurance, gas and electricity markets, and pharmaceuticals. For example, the energy sector inquiry – which took place between 2005 and 2007 – concluded that after a decade of market liberalisation, there were still barriers to competition which prevented end-users from reaping the full benefits.

In response to the findings of the energy sector inquiry, the Commission devised a dual strategy. First, a package of legislative measures to improve the energy regulatory framework (the Third Energy Package) was adopted in July 2009 and will enter into force in March 2011. This should help achieve effective unbundling of energy networks from their downstream commercial activities, promote European integration of companies and ensure that there is strong and consistent regulation with a cross-border focus.

Secondly, the full spectrum of competition enforcement tools at the Commission's disposal was applied to pursue individual cases that will help remove bottlenecks in the supply chain. Since 2007 no fewer than seven decisions under Articles 81 and 82 of the EC Treaty (Articles 101 and 102 of the Treaty for the Functioning of the European Union, TFEU) in the energy sector have been adopted – including one decision fining the companies substantial sums in respect of market sharing arrangements[1052] and six decisions formalising commitments offered by the parties – and more are under investigation.

2.3 EFFECTS-BASED APPROACH TO ENFORCEMENT

From a substantive point of view the Commission has, over the past few years, consolidated a more economics-focussed and effects-based approach in the EU

procedures in view of the adoption of Decisions pursuant to Article 7 and Article 23 of Council Regulation (EC) No 1/2003 in cartel cases, OJEC [2008] C 167/1.

1052 Case COMP/39.401 – E.ON/GDF, Decision of 8 July 2009.

competition policy across the board: in mergers, anticompetitive agreements and practices other than cartels, abuses of dominance and state aid control. This has helped to establish the actual or potential impact of company behaviour or government measures on the market and on consumers.

The 1997 Guideline on the definition of relevant markets[1053] was one of the first instruments to reflect this economic, effects-based, approach. Then in 1999 and 2000 the Commission completely revised its rules on vertical and horizontal agreements, so that an assessment of a conduct would involve not only examining whether it restricts competition between the parties, but also whether it is likely to negatively affect prices, output, innovation, or the variety or quality of products and services.

In 2002 the European Court of First Instance overruled three merger decisions in quick succession, and criticised the Commission's economic analysis in two of those cases. This acted as a catalyst and a spur for DG Competition to increase its capacity and resources for economic analysis. In 2003, a new Chief Economist post was created and recruitment of economists was accelerated. The amount of resources that Directorate mobilises for economic analysis can now roughly be assessed at one economist for two lawyers. By contrast, in the early 1990s the ratio was 1 to 7.

At that point, the Commission undertook to overhaul EU competition enforcement instruments so as to better align them to current economic thinking – and, in parallel, to provide guidance on how the rules would be applied. It was important that the move towards an effects-based approach should not lead to uncertainty for companies.

In 2004, the substantive assessment for mergers was amended, so as to introduce the "significant impediment to effective competition" test.[1054] This made it clear that the Commission's transactions control powers could be used not only where there was the creation or strengthening of a dominant position – but could also address other unilateral conduct.

1053 Commission notice on the definition of the relevant market for the purposes of Community competition law, OJEC [1997] C 372/5.

1054 Under Article 2 of the revised EC Merger Regulation (Council Regulation 139/2004, OJEC [2004] L24/1), concentrations are prohibited if they would "significantly impede effective competition, in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position".

The horizontal merger guidelines adopted in 2004[1055] helped provide a clear framework for the analysis of such unilateral effects, emphasizing that the Commission would rely less on structural factors (such as market shares, concentration levels) and more on the assessment of whether competitive constraints are eliminated by the transaction, taking into account market characteristics such as product substitutability, capacity limitations, elimination of a significant competitive force, hindrance to expansion by competitors, etc.[1056] It was also foreseen that merger specific, timely and verifiable efficiencies that benefit consumers are taken into account and are a mitigating factor for transactions that might otherwise have adverse effects on competition.

This was followed by the adoption in 2007 of the non-horizontal merger guidelines,[1057] which recognise that the majority of vertical and conglomerate transactions do not raise problems, and can bring about efficiency gains that benefit both businesses and consumers. However, the Commission needs to verify that deals do not lead to competing companies being denied access to an important supplier, or facing increased input prices.

2005-2009 witnessed a major push towards reform with the State Aid Action Plan. The aim was to reform instruments so as to incorporate a refined economic approach that takes better account of the effects of the aid and focuses on those cases that cause the greatest distortions of competition. The aim was also to enable a greater emphasis on key priorities identified in the Lisbon strategy, a reduction in administrative red-tape, and a faster and more predictable decision making process.

The State Aid Action Plan set out a general balancing test as the conceptual framework for analysing cases. In essence, this test asks (i) whether the State aid solves a market failure, or addresses another objective of common interest (equity); (ii) whether the aid is well targeted, which means it provides for an incentive effect (i.e. changes the behaviour of the recipient so that it meets the objective) and is limited to the minimum necessary, and (iii) whether the distortions of competition and trade, resulting from the aid are sufficiently limited, so that the overall

1055 Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, [2004] OJEC C 31/5.

1056 Decisions such as Korsnas/Assidoman Cartonboard and T-Mobile Austria/Tele.ring are good examples of cases involving the analysis of possible impediments on competition even in the absence of dominance.

1057 Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings, OJEC [2008] C 265.

balance is positive. This test has been implemented through instruments such as the Guidelines on risk capital, on research and development and innovation, on regional aid, and on environmental aid, as well as in the General Block Exemption Regulation[1058] adopted in 2008, and a series of individual cases.

The latest milestone in implementing an effects-based approach was the adoption, in December 2008, of the Commission Guidance on its enforcement priorities in applying Article 82 of the Treaty (Article 102 TFEU).[1059] The paper formalises the effects-based approach that has been increasingly applied under Article 82 (Article 102 TFEU), by setting out the Commission's intention to prioritise cases, where the exclusionary conduct of a dominant undertaking is liable to have harmful effects on consumers. The starting point of the Guidance is that dominant companies should freely and fiercely compete on the market, as long as this competition is ultimately for the benefit of end users. Such competition may well mean that competitors who deliver less to consumers have to leave the market. Enforcement under Article 82 (Article 102 TFEU) is not about protecting competitors, but about protecting consumer welfare.

The Intel case is a good example of an investigation under Article 82 (Article 102 TFEU) in which a detailed effects-based analysis has been carried out. [1060] The decision issued by the Commission described how in response to the growing threat which Intel's main rival in the market, AMD, represented, Intel, through the conditions associated with its rebates, prevented its suppliers from offering more computers with pioneering AMD chips. This led to limited choice for consumers and less innovation in the market. This analysis was accompanied by an extensive quantitative study which showed that even a hypothetical competitor as efficient as Intel could not counteract the effect of the conditional rebates in question.

The Commission is currently reviewing the rules governing vertical and horizontal restraints in view of the expiry of the current block exemption regulations in 2010. Regarding vertical restraints, in the summer of 2009 a public consultation was launched on a revised set of rules, which would essentially prolong the existing

1058 Commission Regulation 800/2008 declaring certain categories of aid compatible with the common market in application of Article 87 and 88 of the Treaty (General Block Exemption Regulation). OJEC [2008] L214/3.

1059 Commission Guidance on its enforcement priorities in applying Article 82 of the Treaty, see http://ec.europa.eu/competition/antitrust/art82/guidance_en.pdf.

1060 Case COMP/C-3/37990 – Intel, Decision of 13 May 2009.

regulations, but adapt them to changes in the market place. In particular these changes include increased concentration at retail level and buying power, and a major increase in on-line sales. Regarding horizontal restraints, DG Competition judgment is still at a quite early stage – but its aim is to set out the most appropriate and workable effects-based approach to assess horizontal restraints.

The new European Commissioner for Competition, Joaquin Almunia, will have to determine what direction to take over the coming five years. It is comforting to say, though, that DG Competition is likely to continue the work on reformulating competition legislation and revising its policy guidance, so as to focus on the economic effects of market structures and of undertakings' practices.

3. MODERNISATION OF EU COMPETITION LAW – REGULATION 1/2003

The most profound, structural, change to the enforcement of EU competition law in recent years has been the "modernisation" of the application of Articles 81 and 82 of the EC Treaty (Articles 101 and 102 TFEU) introduced by Regulation 1/2003, which came into force in 2004.

First, Regulation 1/2003 empowered all EU Member States to fully enforce EU competition law, through the National Competition Authorities (NCAs) and the national courts, and set up the European Competition Network (ECN). Secondly, it abolished the system of ex ante notification to the Commission of potentially anticompetitive agreements and practices. Thus, it decentralised enforcement, allowing the best-placed authority to take a case forward. It also freed up resources, allowing the Commission and the NCAs to determine priorities, and to focus on the most serious infringements of the competition rules, where the position of consumers can be significantly improved.

Undoubtedly, the "modernisation" has been a success. The European Competition Network has proved to be a useful and innovative method of cooperating on enforcement and ensuring consistency and coherence in the application of the competition rules across all the Member States.

The Commission's recent report to the Council on the functioning of Regulation 1/2003 emphasizes this success, which is attributable to the dedication, competence and energy of NCAs such as the Office of Competition and Consumer Protection in

Poland. Since the entry into force of Regulation 1/2003, ECN members have been informed of over 1000 cases investigated by public enforcers on the basis of Article 81 or 82 (Article 101 or 102 TFEU), and NCAs have informed the Commission of envisaged decisions in more than 300 cases.

The ECN has adopted the Model Leniency Programme setting out minimum standards, so that there are models now in nearly all of the 27 Member States. ECN working groups on diverse topics, and ECN plenary meetings have proved to be a very useful tool for cooperation and discussion.

These are significant achievements. But the ECN is a long-term investment, and one which will continue to deliver benefits for years to come. When preparing the Commission's report on the functioning of Regulation 1/2003, we took the opportunity to take stock of ECN achievements so far, and to seek areas for further improvements.

One challenge is how to constantly enhance the benefits of cooperation between the European Commission and the NCAs, through the ECN. We could possibly do more to promote the sharing of market intelligence and dialogue between officials at all levels. Explicitly or implicitly this might feed in to prioritisation exercises by NCAs and the Commission.

Stakeholders have also emphasized to the Commission that the exception set out in Article 3 of Regulation 1/2003 allowing stricter national rules on unilateral conduct has resulted in some fairly significant discrepancies between competition regulations enforced by each NCA, and can consequently hinder pan-European marketing strategies. This may merit further consideration.

Of course, differences between national procedures for implementing Articles 81 and 82 (Articles 101 and 102 TFEU) are also significant. A further point is whether the Commission should consider initiatives to help towards convergence in procedures, or whether it is possible to enhance cooperation while maintaining these differences?

Moreover, recent review of the EC Merger Regulation suggests that the 2004 Regulation has worked well both from a procedural and substantive point of view. However, there may also be some room for improvement. In particular, the possibility has been mooted of trying to achieve more convergence between national merger control rules and enhanced cooperation between the 27 national concentration control authorities across the EU, and the European Commission.

Another area in which the ECN has proved its worth is in international cooperation. The ECN has facilitated collaboration with third country agencies through fora such as the ICN, enabling the EU competition authorities to spread our influence and ideas more widely, beyond the borders of the European Union.

4. COMPETITION POLICY AND THE FINANCIAL AND ECONOMIC CRISIS

It is impossible to write about effective competition in Europe without mentioning the current financial and economic crisis. Beyond the antitrust and merger powers which are common to all authorities in the ECN, the Commission has specific powers to control State aid in all sectors of the economy, including banking. At the outset of the financial crisis, there was pressure on the Commission to set aside the EC Treaty rules on competition in order to allow Member States a free hand to adopt the bank rescue measures they saw fit in order to stabilise the industry and notably protect consumers' savings. However, very soon, it proved necessary to enforce the Treaty rules to help maintain a level playing field between financial institutions in the EU – and that the European State aid rules could facilitate minimising the distortions of competition that might otherwise result from large-scale support, prevent disruptions to the Single Market, and prepare the return to normal functioning. More generally, I believe that governments quickly came to realise that a strong competition policy is in fact essential to help all economies out of the crisis. On the other hand, the crisis has shown that it is occasionally inevitable to provide quick responses and show flexibility on procedure.

In order to assist Member States in taking urgent measures to stabilise the economy and to provide legal certainty, the Commission adopted four communications between October 2008 and July 2009 setting out how the State aid rules would be applied to schemes and individual rescue measures, recapitalisation instruments, the treatment of impaired assets and to restructuring aid for financial institutions. At that time the Commission also assessed over 100 national schemes or measures to support financial institutions, under the State aid rules. We have slowly moved from the rescue phase, and are currently reviewing bank restructuring measures proposed by Member States. In essence, the Commission's position is that those banks that have received large amounts of aid and that have unsustainable business models will have to restructure in order to return to long term viability without relying on State support. This is crucial for creating the basis for the competitive sector in Europe.

With regard to the real economy: in December 2008, the Commission adopted the Temporary Framework for State aid. The idea behind this scheme is to allow Member States – on a provisional basis until the end of 2010 – to grant certain types of support to the "real economy" in order to reduce the negative effects of the crisis. Specifically governments needed to be able to facilitate companies' access to finance. Sufficient and affordable access to funding is a pre-condition for investment, growth and job creation by the private sector. In the short term the economic downturn affects the viability of European companies – and in the long term it could delay investments in sustainable growth and other Lisbon Strategy objectives. To date over 65 aid schemes have been approved under the Temporary Framework.[1061]

Naturally, EU antitrust and merger policies have also come under pressure of the crisis. In assessing mergers that occur against the backdrop of the financial and economic downturn, the Commission is very conscious that the priority has to be to maintain effective scrutiny under the competition test laid down in the EC Merger Regulation, in order to preserve competitive market structures in the medium to long term. Where absolutely necessary, the rules allow some flexibility on timing – even though it is very important that DG Competition has sufficient time to carry out an effective and thorough review of the impact of a transaction. As the competition test already allows to take into account rapidly evolving market conditions, the Commission's practice to date has not shown any requirements for adjustments to our substantive review. In the event of a rescue merger, Directorate's policy and practice does also provide for the possibility of taking into account a failing firm defence, although it would have to meet the strict conditions set out in the horizontal merger guidelines.

From the point of view of the antitrust rules, the Commission is aware that in times of crisis companies may face difficulties, including reduced profits and overcapacity. Downturn conditions, however, cannot justify collective or concerted action through so-called "crisis cartels", aiming to reduce capacity

1061 We publish an overview of national measures adopted as a response to the financial/economic crisis, which is regularly updated, on DG Competition's website:
http://ec.europa.eu/competition/sectors/financial_services/financial_crisis_news_en.html.

or production, or agreements to maintain prices. Of course, collective action may take other forms, which may be less harmful, but they would still need to satisfy the conditions laid down in Article 81(3) of the EC Treaty (Article 101(3) TFEU).

5. CONCLUSION

Ultimately, the crisis has helped crystallise the scope and meaning of competition policy. I believe that the focus of the policy in recent years on eliminating consumer harm is putting us in a good position in these difficult economic times. Faced with such hardships, it is important that consumers could make the best possible use of their buying power – companies cannot be allowed to transfer the burden of an economic downturn to consumers, through cartels and abusive practices. Nor should the crisis justify State aid that would sustain uncompetitive businesses at the taxpayer's expense, or mergers that would create uncompetitive market structures. To this end all competition authorities need to pursue a vigorous competition enforcement policy – and to prioritise our enforcement efforts effectively.

Moreover, all agencies need to recognise that sometimes regulatory and legislative change can be a necessary complement to enforcement action, or can help achieve results faster. The crisis – arguably partly brought about by regulatory failures – highlights the need for competition principles to be implemented not only through our direct enforcement action, but also through the regulatory architecture for any given sector of the economy. Competition objectives should be part and parcel of regulating, for instance, the financial sector, the energy sector, or the communications sector.

Monika Tomczak-Górlikowska

CAUGHT IN THE NET – HOW THE INTERNET CHANGED THE APPROACH TO THE APPLICATION OF COMPETITION LAW RULES AND INTELLECTUAL PROPERTY RIGHTS

1. INTRODUCTION

For a long time, the Internet had been advancing independently of any legislations. Created independently and by independent people, it was subject to only a few rules. Currently however, it seems that both intellectual property law and competition law do not want and cannot be indifferent to things happening on the web, since more and more is going on there. This paper will present two areas where regulations regarding competition law and intellectual property law are translated to the language of the Internet and adjusted to its needs. It concerns issues linked with pan-European licensing of creative contents online, such as music, films, books, video games, as well as legal aspects of online distribution in the context of the recently commenced process of reforming regulations on vertical restraints. For obvious reasons, this paper will not raise all legal issues linked with Internet operations, because it is an extremely broad field. We should also emphasise, that both areas described below are currently under transformation and the end of this process is not fully known yet. This is another proof that the Internet is a great challenge for regulations concerning the competition law and intellectual property rights.

2. OPENING THE MARKET OF COLLECTIVE MANAGEMENT IN THE ONLINE ENVIRONMENT

"European consumers want and deserve better online music offerings."

Neelie Kroes, October 2009[1062]

1062 Statement of the European Commissioner for Competition – Neelie Kroes of 20 October 2009, Press release IP/09/1548.

2.1 THE EUROPEAN COMMISSION PROPOSES THE CHANGE OF RULES REGARDING COLLECTIVE MANAGEMENT OF RIGHTS FOR ONLINE SERVICES

It is obvious that musical works are one of the most popular legal assets on the Internet. They are exchanged between users through various online services, promoted and distributed on the web. There is also no doubt that violations of intellectual property rights take place there on a large scale.

Meanwhile, in the real world, use of copyrighted musical works is subject to regulations, which until recently resisted all extraterritoriality. It concerns, in particular, the collective management of copyright in relation to musical works. National collective management organisations granted national licenses and, as a result, online distribution of musical works required obtaining licenses on all territories where the service was available. It should be also emphasised that legislation on operations of collective management organisations, their rules for calculating remuneration for authors, the scope of licenses and the catalogue of creative contents of a given organisation (repertoires) are very complicated and unclear for users.

It should also be added that traditionally, collective management organisations act not only on behalf of authors from a given territory who entrusted their rights to this organisation, but also on behalf of authors from other countries under mutual agreements connecting particular organisations. Collective management organisations also act on behalf of those authors who did not entrust them with their rights under so-called *negoriorum gestor*[1063] theory. Moreover, we should remember that one work may incorporate copyrights of several or several dozens of authors (composers, publishers) and their rights may be managed by several collective management organisations.

It also means that determining the scope of activities of particular organisations is not always easy, as well as that it is difficult to identify the rights' holders. This occurs particularly nowadays, when some authors or right holders do not entrust their rights with so-called traditional collective management organisations, but manage them on their own.

1063 See: *System Prawa Prywatnego*, Vol. 13, *Prawo autorskie*, ed. J. Barty, 2nd edition, C.H. Beck, Warszawa, 2007, §56, p. 589.

Complicated legal status[1064] and the requirement to obtain licenses covering individual EU countries are factors which paralyse the unimpeded development of legal music websites operating in many European countries and significantly increase the cost of such services.

For a long time, collective management organisations effectively defended themselves against any interference from the European Commission or national competition authorities. The steps taken within this scope by the Commission did not generally interfere in the activities of such organisations regarding the offline world, i.e. above all in relation to licensing for mechanical copies.

However, things look different in the online world. The European Commission has been working for several years on cross-border, multi-territorial licensing agreements, which will better suit the needs of the Internet. The Commission has stated that the lack of possibility to conclude such agreements impedes the development of this market.

Already in 2004, the European Commission adopted the Communication on management of copyrights and neighbouring rights on internal market[1065]. A year later, it summarised its considerations in the Recommendation on cross-border collective management of copyrights in relation to online services[1066]. The Commission confirmed that in its opinion it is necessary to establish a multi-territorial licensing system and increase the freedom of authors when conferring rights to a collective management entity[1067]. This freedom would also (or above all) cover the possibility to give licenses for online distribution, even when this field of musical work exploitation was covered by an agreement with the previous collective management organisation[1068].

Moreover, the Commission postulated that the copyright holder could have the possibility to easily transfer it between organisations operating in various Member

1064 For more on online licensing agreements for using musical work and authors' rights, see: M. Grabowski, *Umowa licencyjna online o korzystanie z utworu muzycznego – charakterystyka prawna,* (in:) „Zeszyty Naukowe Uniwersytetu Jagiellońskiego", *Prace z Prawa Własności Intelektualnej,* issue IV 106 (2009), p. 91.

1065 Communication from the Commission to the Council, the European Parliament and the European Economic and Social – Committee The Management of Copyright and Related Rights in the Internal Market (COM (2004) 261 final).

1066 Commission's recommendation of 18 May 2005 on cross-border collective management of copyrights and neighbouring rights in relation to legal online services (Text with EEA relevance 2005.737/EC Dz. U. L 276 p. 54)

1067 Commission's recommendation of 18 May 2005, op. cit. – preamble point (8) and (9).

1068 See also: *System Prawa Prywatnego,* Vol.13, *Prawo autorskie*, op. cit, and point 5) of Commission's recommendation of 18 May 2005.

States. The effect of introducing such principle would be the possibility to bypass a national collective management organisation in favour of a different one located in other Member State. There is no doubt that such solution would contribute to increasing competition between collective management organisations.

The content of Recommendation unequivocally proves that the European Commission is a firm supporter of opening the market for collective management. It would include two areas – first, a cross-border licensing system in order to open the market for online services including licensing of copyrighted works, second – providing authors with greater liberty of choice when entrusting rights to collective management organisations operating in other Member States[1069]. Such changes should lead to a real internal market for copyright management. We can also add that changes postulated within the scope of operations of collective management organisations and assigning rights to them by authors, are not limited only to the online market, but could be applied to operations of these organisations in general.

We should also note that the largest organisations in particular Member States, including *inter alia,* the Association of Polish Authors and Composers (ZAIKS), have achieved a very strong market position and abused it by restricting authors' freedom to entrust their rights[1070]. On the basis of Polish regulations, collective management organisations have been claiming for a long time that they are not even subject to competition law rules, by stating that they are not enterprises. However, such position was finally rejected by the Polish Supreme Court[1071], which confirmed that there is no basis for excluding these entities from the scope of the competition law.

Despite that in the Recommendation of 2005 the European Commission appealed to the Member States for taking necessary steps for opening the collective

1069 Point 3) of the Commission's recommendation of 18 May 2005, op. cit.

1070 See, *inter alia,* decision of the President of the Office of Competition and Consumer Protection of 21 July 2009 (RWA–10/2009) concerning the five-year period of entrusting rights without the possibility of earlier change; decision of the President of the Office of Competition and Consumer Protection of 16 July 2004 RWA–21/2004 (decision in the Brathanki case) (final decision); decision of the President of the Office of Competition and Consumer Protection of 10 June 2009 (RWA–6/2009) concerning the SAWP Polish Musical Performing Artists' Society; all available at: http://www.uokik.gov.pl/pl/orzecznictwo_prezesa_uokik/decyzje_prezesa/.

1071 Judgment of the Supreme Court of 6 December 2007, case file III SK 16/07 (OSNP 2009/1-2/31) – the Supreme Court dismissed the cassation complaint lodged by the Association of Polish Authors and Composers, confirming that collective management organisations carry out economic activity and are therefore enterprises, which corresponds to the established position of the Court of Justice of the European Union in this respect, expressed *inter alia* in cases 1127/83 SABAM and 395/87 Ministere Public versus Tournier (Rec. 1989, p. 2521).

management market and supporting the market of legal online services, the changes postulated in relevant regulations were not implemented. At the same time, the "side effect" of the Recommendation of 2005 was that some music publishers decided to depart from the system of entrusting rights to national collective management organisations in favour of pan-European, direct licensing of their repertoire in cooperation with selected organisations.

EMI Music Publishing was the first one to do so. Despite the resistance of some collective management organisations, it implemented pan-European licensing of its repertoire through the CELAS initiative[1072]. EMI emphasised that its initiative is a proof that even in the current legal situation it is possible to introduce an effective licensing mechanism at the EU level.

However, due to the fact that the Recommendation of 2005 did not result in the implementation of systemic changes in the manner of licensing on the common market, the Commission continued its work and in January 2008 published a Communication on creative content online in the single market[1073]. The communication was based on a survey and public consultations conducted at the request of the Commission. The Commission observed therein, that multi-territorial approvals for creative content online are still one of the challenges preventing their distribution on the web and that it requires actions at the Community level. The Commission noted again that territoriality of copyrights requires obtaining approval for distributing content in every Member State[1074]. This statement is reflected in practice – many websites distributing creative content online limit access to them to users from particular Member States. One of the examples is the online music store iTunes, which conducts activities in such Member States as the United Kingdom and the Netherlands but which cannot be used by consumers from many Member States, including Poland. Another example is the popular website Amazon.com, which also limits the possibility to purchase music in the form of downloadable files depending on where the transaction is initiated (e.g. users from Poland currently cannot download music from amazon.co.uk). The

1072 CELAS is a joint venture of the German collective management organisation GEMA and the English organisations MCPS-PRS, which grants licenses to the English and American repertoire of EMI Music Publishing. Currently, CELAS hold an exclusive right to license this repertoire for online distribution in 41 European countries (it also operates through agents). More information on CELAS can be found at its website www.celas.eu.

1073 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions on Creative Content Online in the Single Market, COM (2007) 836, final version.

1074 Communication of the Commission on creative content online, op. cit., point 2.2.

obstacles observed by the Commission concern not only music files but also other copyrighted material, e.g. audiovisual works, in particular video-on-demand. Rights holders often give approvals covering only defined territories and not the whole area of the internal market.

2.2 CONTENT ONLINE PLATFORM

Due to this situation, the European Commission decided to set up the Content Online Platform with the objective to create a forum for discussing the future development of creative content distribution at the Community level[1075]. These discussions were concluded with the Final Report on the Content Online Platform published in May 2009[1076].

In relation to multi-territorial licensing, the report stated that in the music sector, the above Recommendation of the Commission of 2005 on cross-border collective management of copyrights was not accepted by all stakeholders. At the same time, in the audiovisual sector cross-border licenses are issued only at regional level (e.g. Scandinavia, the Baltic countries). What is important, during discussions within the Platform, the necessity for creating a European database containing a list of European creative content was emphasised in order to identify right holders and manage rights at the Community level. Identification of the right holder and the possibility to give him or her proper remuneration is a key element of collective management.

In view of such statements the Commission decided to commission a survey on legal, cultural and economic aspects of multi-territorial licenses for distributing content through the Internet. The study will also present the structure of the online distribution sector and the main obstacles to granting pan-European licenses. According to the statements made in the report, the study will be created in early 2010. Surely it will be an interesting report examining reasons why solutions recommended by the Commission were not put into practice, despite the fact that they seemed to be advantageous for all interested parties.

Moreover, on 22 October 2009 the Commission published a document containing further observations regarding the challenge of creating a uniform digital

1075 Communication of the Commission on creative content online, op. cit., point 3.

1076 "Final Report on the Content Online Platform", available at: http://ec.europa.eu/avpolicy/docs/other_actions/col_platform_report.pdf.

market for creative content such as books, music, films or video games[1077]. The document once again states that digital distribution of cultural goods is still facing regulation and territorial difficulties, which can be an obstacle for creativity and innovativeness. The Commission invited all interested parties, i.e. copyright holders, consumers and commercial users, as well as all other interested parties to participate in the debate (until 5 January 2010).

2.3 ROUNDTABLE MEETINGS

At the same time, debates on music distribution on the Internet were conducted within so-called roundtables, presided over by the European Commissioner for Competition – Neelie Kroes. The meetings gathered representatives of the interested parties, namely publishers, collective management organisations, consumer organisations. They were even honoured by Sir Mick Jagger and Steve Jobs.

As a result of these meetings, a very interesting report was published presenting opportunities and barriers for development of online music sales[1078]. The report clearly states that currently there is no single EU market for downloading music files[1079]. In the opinion of the roundtable participants this results from several factors. First, EU countries have complicated rules on collective management of copyright, which significantly differ from each other. Second, the main factor which impedes the development of the online market is the necessity to conclude license agreements with many entities – not only due to the territorial scope of copyrights, but also because one work can incorporate rights of many authors and these rights may be entrusted to different collective management organisations. This way, small enterprises, which would like to start business activity concerning online distribution of music outside the territory where they are located cannot overcome the challenge of obtaining a license from entitled entities operating on other territories due to organisational and financial reasons.

Creating innovative services combining not only downloading music files but also the distribution of video clips, lyrics, etc. is also hindered because of legal complexities. Such service combines many rights, only part of which could be

1077 Press release of 22 October 2009 No IP/09/1563 "European Commission launches reflection on a Digital Single Market for Creative Content Online", available at: http://europa.eu/rapid/pressReleasesAction.do?reference=IP/09/1563&format=HTML&aged=0&language=EN&guiLanguage=en.

1078 There were four meetings of so-called "online commerce roundtable" starting from September 2008. The report entitled "Online Commerce Roundtable Report on Opportunities and barriers to online retailing" is available at: http://ec.europa.eu/competition/consultations/2009_online_commerce/roundtable_report_en.pdf.

1079 The above-mentioned report, p. 1.

assigned to collective management, whereas part of them may require direct approval from the rights' holders.

On the other hand, representatives of collective management organisations (French organisation SACEM) emphasised that from their perspective, the main problem is the identification of the rights' holders, as well as violations of copyrights still occurring on the Internet. Moreover, due to the Internet's extraterritoriality, collective management organisations are faced with great difficulties when enforcing rights. SACEM also argued that some users are against the introduction of a direct licensing model and multi-territorial licenses. It emphasised that some organisations managing smaller repertoires are against multi-territorial licenses because such system may result in the marginalisation of their repertoire, which in turn is a threat to Europe's cultural diversity.

Representatives of consumer organisations emphasised that not using the potential of the Internet for distributing creative content results in the internal market being divided by various real barriers. This allows for price discrimination with respect to consumers from individual EU countries. To support this argument, the British consumer organisation Which? used the example of Apple, which offered higher prices for downloading music files to users from the UK than from other areas. Although Apple agreed to lower its prices, users from one territory still cannot download files from a website addressed to consumers from other EU country.

Noting the above arguments presented during the roundtable meeting seems useful for understanding the reality in which both the service providers and customers operate. The challenges still occurring in relation to the operations of this sector were clearly formulated in the roundtable report and this is the value that the report adds to the previously repeated position of the European Commission indicating the necessity of granting multi-territorial licenses. Moreover, the document shows the discrepant views of the individual interested entities and concludes that finding a formula which would satisfy all will be extremely difficult. However, reaching an agreement by individual players of this sector seems to be necessary in light of the expectations of European consumers, frustrated by their transactions being rejected by websites only because they come from a "second class" territory.

During the roundtable meetings, individual participants also voiced opinions on the possible solutions to the problem of licensing online distribution of music. Interestingly enough, we can distinguish certain differences of opinion between such rights' users as Apple, publishers like EMI, or organisations like SACEM. Apple voiced the farthest reaching, but currently not realistic, proposal for establishing pan-European copyrights, which would replace the present national copyrights[1080]. Such proposal does not seem at present feasible because it would require serious intervention into individual national copyrights regimes.

Moreover, representatives of rights' users emphasised that publishers should not refuse licensing their rights to collective management organisations, which in turn should have the right to grant further sublicenses to users. This proves that some users fear that powerful publishers would tend to granting direct licenses. Moreover, Apple emphasised (similarly to the representatives of collective management organisations) that there is a significant deficit of information concerning right holders for a particular musical work. Moreover, there is no single format for providing information on rights incorporated in particular musical works – and this is a vital issue from the perspective of distributing remuneration to authors as well as reporting downloads made by consumers.

EMI, one of the music publishers from the "majors" group [1081], emphasised that there should be a greater exchange of opinions and identification of needs between rights holders and potential licensees, so that it would be possible to introduce alternative business models, different from the traditional model of rights management. Such position is not surprising since EMI has been advocating pan-European model of licensing (through the CELAS initiative described above).

On the opposite side, there is the opinion of collective management organisations regarding the proper model for the development of online distribution of musical works. In their opinion, pan-European licenses are the cure for problems connected with the operation of the Internet. The most important issue for these organisations is the possibility to effectively enforce the rights of the entitled entities. According to French SACEM, the system of national licenses ensures that authors have the chance to seek due remuneration.

1080 Report on roundtable activities, op. cit., p. 11 point (42) and subsequent.

1081 The Polish market for music publishing is dominated by four big entities that are affiliates of the international music publishing corporations – referred to as "majors" – Universal Music, EMI Music, Sony BMG Music, and Warner Music Poland. For more on the structure of the Polish market of musical records, see: Report on competition on national market of production and distribution of musical records prepared by the Department of Market Analyses of the Office of Competition and Consumer Protection, August 2007, available at: www.uokik.gov.pl.

During subsequent roundtable meetings representatives of publishers also emphasised that it is necessary to implement rules proposed by the Commission in 2005 regarding the improvement of transparency of operations of collective management organisations, particularly concerning competition among them. Despite the content of the above Recommendation of the Commission, it is unlikely that organisations will change their rules of operation. On the contrary, it follows from the decision of the European Commission on CISAC[1082] that in the context of changing market conditions, collective management organisations "closed ranks" and came to an understanding regarding the issue of mutual licensing of relevant repertoires by signing mutual representation agreements including clauses which strengthened territorial restrictions along national borders.

Although the decision of the Commission on CISAC does not concern only online licensing but is mainly connected to offline licensing, it shows the methods employed by organisations, which for decades enjoyed a specific immunity from competition law and now have to face a new state-of-play. In the new situation they have the same rights (and duties) as other market participants, thus, they cannot freely use their monopoly or quasi-monopoly and conclude competition-restricting agreements.

It should be emphasised that collective management organisations enjoy such a wide range of rights because in many EU jurisdictions the manner of determining the level of remuneration for using copyrights is regulated to some degree. In principle, such regulations aim to protect users against discrimination on the part of collective management organisations and provide equal access to licensed rights. However, it seems that these mechanisms impede determining the level of remuneration depending on the actual use of the works in the repertoire of a given organisation, thus solidifying their position on the market and their manner of operation.

As practical experience shows, apart from direct and multi-territorial licenses, service providers who intend to distribute music files online in a given territory still communicate with local collective management organisations in order to obtain licenses for using their repertoire. As such service providers claim, the

1082 Decision of the Commission of 16 July 2008 in the case COMP/C-2/38.698 – CISAC. The decision was issued under Article 7(1) of the Regulation (EC) No 1/2003 and is addressed to twenty four collective management organisations from the EEA, which are CISAC (International Association of Collecting Societies of Authors and Composers) members. The decision concerns the conditions on which the collective management organisations grant licenses to perform musical works in public and on which they manage these rights. The European Commission also questioned certain clauses of mutual representation agreements, particularly the exclusivity clause, membership clause and agreements on territorial restrictions along national borders. Currently, the decision is appealed against in the Court of First Instance.

main asset of websites which enable legal downloads of music files is offering a very wide range of protected musical works, possibly of niche character.

Despite the discrepancies described above regarding the perception of challenges and market needs for licensing creative content online, the roundtable meetings ended with partial success, as on 19 October 2009 their participants signed a joint statement which included general principles of music distribution on the Internet[1083]. Commissioner Neelie Kroes expressed her satisfaction that through these meeting the access to music for the consumers on the Internet should improve. Indeed, for the first time, some participants of this market, including iTunes, Amazon, Nokia, and what is more, collective management organisations decided to undertake certain obligations aimed at the implementation of new licensing platforms covering the whole area of the European Union.

First, all participants agreed that multi-territorial licenses are needed in the online world. Both, EMI (through CELAS) and SACEM decided to grant pan-European licenses. SACEM indicated also that it is prepared to entrust giving such licenses to collective management organisations in Europe. In turn, EMI stated that it will appoint additional entities managing its repertoire, which will be authorised to give licenses at the level of the whole EEA.

All participants also acknowledged that it is necessary to improve the exchange of information between right holders and users (e.g. regarding the type of information that is conveyed), emphasising, however, that it should not lead to creating of a monopoly as regards databases or making such information available. In light of such positive developments, iTunes stated that it will try to distribute its services to more areas than currently, within the capacities it possesses.

Despite the fact that the above declarations do not introduce revolutionary legal changes to the existing situation, they indicate that the Internet forced all the interested entities to depart from the traditional model of territorial licensing which has been applied in the EU for decades. The above declarations, although limited, indicate that sooner or later it will be necessary to implement an effective pan-European licensing system, because such solution corresponds to the needs of the Internet and its users.

1083 Press release of 20 October 2009 IP/09/1548.

There is also no reason why divisions stronger than physical borders, which were abolished by the Schengen Agreement, should remain in the EU internal market, where the principle of free movement of goods applies and where the principle of admissibility of parallel importation has been undisputed for many years.

It also seems that the Internet will finally force collective management organisations to change their manner of their operations and adjust to a competitive and open market. Since the Commission indicates that such a need exists in reference to the online world then there is no reason why this should not apply to the offline world as well where users' needs are equally important.

3. WHAT WE CANNOT BUY ON THE INTERNET - SELECTIVE DISTRIBUTION ON THE WEB

3.1 MODERNISATION OF VERTICAL RESTRAINTS SYSTEM

"The review launched today aims to ensure that the assessment of supply and distribution agreements under the competition rules takes account of recent market developments, namely further increased market power at the level of buyers and new forms of distribution including the opportunities brought by the Internet".[1084]

In July 2009 the European Commission started a process leading to the amendment of the Regulation on vertical restraints[1085] by presenting for public consultation a proposal for amended Regulation on vertical restraints and Guidelines on agreements concerning supplies and distribution. The Commission emphasised that main modifications proposed regard, *inter alia,* online commerce, because its development is one of the two main changes which occurred since the current Regulation on vertical restraints was adopted. The process of public consultation ended on 28 September 2009 and the submitted comments are available on Commission's website[1086].

1084 Statement of the European Commissioner for Competition – Neelie Kroes on the review of competition rules in distribution sector of 28 July 2009 IP/09/ 1197. The draft regulation on vertical restraints (C(2009) 5365/2) is available at the Commission's website at: http://ec.europa.eu/competition/consultations/2009_vertical_agreements/draft_regulation_pl.pdf.
The draft guidelines are available at the Commission's website at: http://ec.europa.eu/competition/consultations/2009_vertical_agreements/draft_notice_pl.pdf. Restrictions related to online commerce were discussed in points (51)-(54).

1085 Commission Regulation (EC) No 2790/1999 of 22 December 1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices (OJ L 336/21)), currently in force, expires in May 2010.

1086 The comments were provided by competition authorities from EU countries, individual persons, and above all by the entities concerned. They are available online at: http://ec.europa.eu/competition/consultations/2009_vertical_agreements/index.html.

Generally speaking, in relation to online sales, two groups of interest are clashing – on the one hand there are those who support selling everything to everyone (the best such example is eBay), on the other – those who enviously protect the reputation of their brands and do not want to devalue them by using online commerce, which has numerous traps lurking for consumers and where stores do not shine with a well-known trademark. Surely everyone was faced with a situation where a certain good or service cannot be bought on the Internet or is reserved only for selected people from other territories. There is also no doubt that the scale of violations of trademark rights and other industrial property rights is still great on the Internet and with only a few clicks it is possible to find Internet stores offering fake goods.

For several years already there has been an animated debate on whether and to what extent it is possible, in the context of selective distribution systems, to impose restrictions regarding online commerce, as well as whether it is possible to establish an absolute prohibition on selling goods on the Internet[1087].

The European Commission has to manoeuvre between these extremes. When announcing the above mentioned drafts it stated that its objective is to protect consumer rights to make „advantageous purchases abroad" through the Internet. On the other hand, the Commission indicated that it must respect certain restrictions imposed on distributors, to prevent online sellers from drawing benefits from promotions of a given brand made by other distributors, who invested in traditional outlets (so-called "free ride" argument)[1088]. In this context the doctrine emphasises that an online store which does not need to invest in a traditional outlet, personnel training and provision of additional services, incurs lower costs, which can be reflected in offering lower prices to consumers. Thus, consumers can benefit from the advice and services offered by traditional stores and then make a purchase in the Internet store.[1089]

The new approach postulated by the Commission introduces more detailed solutions in terms of online sale and restrictions permitted under the block exemption,

1087 An interesting summary of problems concerning the economic assessment of "free ride" arguments can be found in P. Marsden and P. Whelan, *Selective Distribution in the Age of Online Retail*, European Competition Law Review, Vol. 21 2010. The authors claim that protecting distributors from free ride practices does not sufficiently justify an absolute prohibition of online commerce; see also F. Carlin, K. Haegeman, *Europe's competition rules on online sales: a plea for regulatory restraint,* PLC Competition Law, August 2009.

1088 Press release of the European Commission of 28 July 2009 IP/09/1197.

1089 A. Font Galarza and C. Gissler, *Selective Distribution of Branded and Luxury Products and the Conjuncture of Online and Offline Commerce in the light of the European Commission 's Revision of the Vertical Restraints Regime*, Global Competition Policy, March 2009.

in comparison with the current regulations. In relation to online commerce, the Commission wants to introduce a distinction between sales made as a result of promotion activities and sales based on consumer's initiative (i.e. between active and passive sales). The Commission indicated that, in its opinion, a general Internet advertisement can potentially reach customers from other areas, but mainly it is directed at customers within a given territory and is considered a form of passive sales. It also formulated a rather controversial argument that language options on websites should also be considered a form of passive sales. We have to note that such a distinction is important from the perspective of admissibility of imposing such restrictions on distributors, because, in principle, imposing restrictions concerning passive sales results in the loss of the block exemption benefit.

Moreover, the Commission stated that requiring distributors to redirect transactions initiated by customers from another territory or automatically ending a transaction if the credit card indicates that the address is outside a given area, is the most serious restriction of passive sales (so-called hard-core restriction). There is no doubt that such proposal is favourable from the point of view of integrating the internal market with respect to online commerce.

According to the Commission's proposal, imposing requirements regarding the quantity of goods which can be sold on the Internet is also a restriction of passive sales. However, it is possible to oblige a distributor to complete a specific percentage of its sales offline in order to ensure effective operations of its traditional store[1090]. Moreover, the required level of offline sales may be similar for all buyers or is defined individually for each one of them based on objective criteria, such as the size of the buyer's enterprise within a chain or its geographical location[1091].

According to published drafts, the Commission intends to treat the imposition of different prices on distributors as one of the most serious restrictions, depending on whether the products are intended for online or offline sale. However, this does not exclude the application of fixed payments in order to support distributors in conducting online and offline sales.

1090 So-called "brick & click" rule – see comments of LVMH, producer and distributor of luxury products, available on the above mentioned website, footnote 26. eBay, which is the greatest advocate of opening online market, has a completely different position.

1091 Footnote 29 to point (52) of draft guidelines, op. cit.

Nevertheless, the Commission acknowledges that an absolute prohibition on Internet sales may be exceptionally justified by the need to protect health and security. It seems, however, that such exception may be applied only in very specific circumstances. Restrictions may also be justified by introducing a new product which can be linked with additional investments.

It follows from the comments presented to the Commission during the public consultation that, above all, market participants would like to receive more detailed clarifications on the proposed hardcore violations regarding online sales, because they are linked with negative effects for enterprises and may serve as bases for legal proceedings.

3.2 INTERNET SALES AND LEGAL PROCEEDINGS

The Court of Justice of the European Union has not been directly[1092] engaged in the online sales issue yet. However, in October 2009, the Court received a request for preliminary ruling, which regarded a question asked by French Cour d'Appel[1093] on whether a general and absolute ban on selling goods to end-users on the Internet imposed in the context of a selective distribution network is a competition restriction due to its subject matter within the meaning of Article 81(1) of the TEC which may potentially be eligible for an individual exemption under Article 81(3) EC. A reply to this question will be interesting not only for the parties to the proceedings but also for the whole sector of selective distribution.

It should also be emphasised that in many EU countries there are proceedings going on regarding online sales and restrictions imposed on distributors in this respect[1094]. It proves that online sales cannot remain outside the scope of the competition law.

1092 However, the judgement of the Court of Justice of the European Union in case C-59/08 COPAD S.A. versus Christina Dior and Sil is significant for selective distribution (and online commerce) – the Court stated there that "the proprietor of a trade mark can invoke the rights conferred by that trade mark against a licensee who contravenes a provision in a licence agreement prohibiting, on grounds of the trade mark's prestige, sales to discount stores such as the ones at issue in the main proceedings, provided it has been established that that contravention, by reason of the situation in the main proceedings, damages the allure and prestigious image which bestows on them an aura of luxury".

1093 Decision of the Cour d'Appel de Paris in case Pierre Fabre versus Président de l`Autorité de la Concurrence (ref. 2008/23812). In this case, the European Commission presented its comments as *amicus curiae*.

1094 Particular attention should be paid to the following German cases: Lancaster Group GmbH v Beaty Net AG (Bunderskartellamt before Bundesgerichtchof) ; CIBA Vision B3 (Bundeskartellamt) ; as well as the French Hi-Fi equipment case – decision of the Conseil de la Concurrence No. 06-D-28.

Tomasz Wardyński

COMPETITION ADVOCACY AS A TOOL SUPPORTING COMPETITION LAW

1. INTRODUCTION

Twenty years have passed since inception in the Polish legal system of a specialised authority to safeguard free competition. This is a good opportunity to draw public attention to the important role played by this institution in ensuring the rule of law.

Polish society is increasingly aware of the benefits of free competition and anti-trust legislation. This is due to many factors. Surely significant here is the close media coverage of cases in which the competition authority identified and severely punished price collusion or abusive practices of dominant companies. Information on raids and high fines imposed by the Competition and Consumer Protection Office (UOKiK) has caught public attention. Some of the Office's decisions prohibiting company mergers were also widely publicised. Implementation of the leniency programme by the competition authority also sparked considerable interest, particularly among entrepreneurs.

Nevertheless, the majority of Polish society still does not negatively view anti-competitive activities from a moral standpoint. This is largely due to Polish history and a lack of awareness of the essence of competition as a legally protected interest. To remedy this competition authorities promote principles of free competition in addition to enforcing competition law. Activity of this type is described as competition advocacy. It is directed at government agencies and society as a whole and constitutes an important pillar of competition protection policy.

2. DEFINITION OF COMPETITION ADVOCACY

The term "competition advocacy" refers to the activities of competition authorities aimed at protecting competition through measures other than enforcing the prohibition on anti-competitive agreements, abuses of a dominant position, or prohibitions on mergers that restrict market competition. According to the definition adopted by the International Competition Network, competition advocacy rests on the creation of competitive conditions for business activity, mainly by influencing other state bodies and promulgating public awareness of competition-related benefits.[1095]

In other words, competition advocacy consists of activities undertaken by competition authorities resting on participation in the law-making and application process without exercise of public authority for the purpose of propagating competition rules. It is this sphere of activity in which they act as "competition advocates" in relation to other authorities and society as a whole.

The need for actions of this type stems from the fact that "*competition may be significantly limited by various official actions. Indeed, private restrictive business practices are often facilitated by various government interventions in the marketplace. Thus, the mandate of the competition office extends beyond merely enforcing competition law. (…). It must assume the role of competition advocate and be proactive in influencing government policies that lower entry barriers, promote deregulation and otherwise minimize unnecessary government intervention in the marketplace.*"[1096]

The legal framework for any activities undertaken by the Polish competition authority acting as a "competition advocate" is Article 31 of the Competition and Consumer Protection Act of 16 February. According to this provision, the tasks of the Chairman of the Competition and Consumer Protection Office include:

– studies on the level of concentration in the economy and the market behaviour of entrepreneurs;
– preparation of draft government programmes for competition development and draft consumer protection policy;
– preparation and presentation to the Council of Ministers of legislative proposals concerning competition and consumer protection;
– presentation to the Council of Ministers of periodic reports on the implementation of government programmes for competition development and consumer policy.

The previous Competition Protection Act of 15 December 2000 (Article 26) and its predecessor dated 24 February 1990 (Article 19) contained a similar provision.

1095 Advocacy Working Group, International Competition Network Advocacy and Competition Policy Report 25 (2002), http://www.internationalcompetitionnetwork.org/OutreachToolkit/media/assets/resources/advocacy_report.pdf.

1096 World Bank, OECD: A Framework for the Design and Implementation of Competition Law and Policy, Chapter 6, p. 93, 1998, (in:) "Competition Advocacy: Challenges for Developing Countries" – extract from a publication by OECD: http://www.oecd.org/dataoecd/52/42/32033710.pdf.

3. SIGNIFICANCE OF COMPETITION ADVOCACY

It is first necessary to define competition before establishing the significance of competition advocacy. However, defining competition nevertheless proves to be problematic. Neither legal commentary nor adjudication provide us a coherent and commonly accepted definition of competition as a legally protected interest.

This term evades strict legal definition to the extent that various public objectives that are frequently contradictory are undertaken under the banner of competition protection. Competition law has evolved from its ordoliberal roots to its current regulation favouring economic efficiency and primary defence of consumer interests. Exceptionally, this has occurred despite its key provisions not having changed at all. Their interpretation and the subject of protection have, however, radically changed.

The problem with defining competition stems from the fact that the definition must not only specify competition as such, but also its desired results if it is to serve any practical purpose from the standpoint of applying competition law. In enforcing competition law, competition authorities act in the context of real or potential competition restrictions. In determining whether any practice has an anti-competitive nature, authorities must compare its actual or potential consequences to the situation of no such limitation on competition. Hence the natural tendency to define the subject of competition law protection through attempts to determine the consequences of unrestricted competition, so that it is upheld with adequate administrative orders and prohibitions.

However, the value of competition stems from inability to predict its results or replicate them through arbitrary decisions. Competition elicits particular effects without state coercion. It is thus assumed that the effects of unrestricted competition are indeed fair specifically because they are achieved in a somewhat diffuse manner free of authoritative arbitrary decisions. According to F. Hayek, the superiority of competition not only stems from the fact that it is one of the most efficient methods of attaining our goals, but also, or even more so, from the fact that it is the only method owing to which our actions can mutually adapt to each other without coercion from the state or its arbitrary intervention[1097].

1097 F. Hayek, *The Road to Serfdom*, London 1979, p. 27. R. Gwiazdowski, *O zaletach konkurencji i potrzebie jej efektywnej ochrony*, (in:) *Ochrona Konkurencji i Konsumentów w Polsce i Unii Europejskiej (Studia prawno-ekonomiczne)*, C. Banasiński (ed.), Urząd Ochrony Konkurencji i Konsumentów, 2005.

Defined this way, competition is more than just an order of things that maximises economic efficiency and leads to material well-being. It is a value that is part of the axiology of a democratic state of law and a civic society respecting individual liberty and dignity.

An economic system based on the principle of free competition is an expression of respect for the premise that citizens who are free and aware of their rights are able to independently establish better and fairer mutual relations than through state coercion. Protecting competition, as understood in the above manner, is therefore an element of protecting basic constitutional values such as the freedom of citizens from unjustified state coercion and its resulting civic society and democratic state founded on the rule of law.

4. THE OBJECTIVES OF COMPETITION AUTHORITIES

The above manner of perceiving competition as a legally protected interest, allows us to properly define the sort of tasks facing competition authorities. These institutions are authorities responsible for protection of the law and constitute an important element of a system founded on the rule of law. Indeed, their role is to safeguard the liberty of individuals. The human right to freedom like any other human right, requires protection against the activity of private entities abusing the rights accorded to them, as well as against unjustified and excessive state intervention.

In protecting competition, antitrust bodies safeguard citizens' liberty in both of those areas. By enforcing competition laws, they prevent private entities from abusing their right to economic freedom in order to abuse the rights of others. By acting as "competition advocates" towards other state authorities, competition authorities counteract unjustified or excessive restrictions of individual liberty on the part of the state. In this manner, the activities of competition authorities in both areas are complementary.

5. COMPETITION ADVOCACY – KEY AREAS OF ACTIVITY

In an attempt to safeguard competition, competition authorities very closely observe all activities of the state that may result in excessive state intervention in the economy.

The important role that competition authorities can play in the process of state enterprise privatisation in developing countries is emphasized. State monopolies are turned into private monopolies far too frequently[1098]. This is usually due to the open desire to ensure a solid market position for a privatised enterprise, which influences its value and consequently results only in short-term benefits from privatisation. Unfortunately, competition authorities frequently do not possess a sufficiently solid position when a socio-economic system is undergoing transformation to draw attention to long-term threats to competition arising from irregularities in the privatisation process and thereby effectively protect free competition principles against limitations.

It seems that the main area of competition authority′ activity as a "competition advocate" is engagement in the process of legislation and influence on its application. The review of draft laws or identification of restrictions upon competition from legal provisions in force are areas of particular relevance to competition authorities. Of equal importance is their analysis and investigation of how other administrative authorities exercise their powers from the standpoint of affecting competition. Competition law provides competition authorities instruments allowing them to identify legal and institutional barriers to economic activity. An important element of their activity is also the drafting of reports on the state of competition in particular sectors of the economy and communicating all threats resulting from poor law or administrative practice in these sectors.

Many legal systems, including the Polish one, have appropriate procedures enabling competition authorities to assess and review proposed laws in order to establish whether they constitute a threat to competition. Activity of this type is an important element of competition authority activity. According to a report on the Polish authority′s activity in 2008[1099], its experts reviewed over 2,000 draft acts of law and other documents submitted to the Office as part of inter-ministerial arrangements. This was done in order to evaluate their impact on competition in the market. These included, among others, laws concerning such sensitive markets from the standpoint of competition as energy, aviation, pharmacy and telecommunications.

1098 Robert Gwiazdowski provides an example of negligence in ensuring competition protection in the privatisation of the telecommunications sector, see R. Gwiazdowski, op. cit.

1099 http://www.uokik.gov.pl/pl/o_urzedzie/informacje_ogolne/sprawozdania_z_dzialalnosci_urze/.

A task facing competition authorities within the framework of competition advocacy is development of a competition culture in society. This takes places through public promotion of the advantages derived from competition and the importance of competition law, as well as through keeping the public informed of the activities of competition authorities. To this end, collections of issued decisions are published, guidelines are developed and interpretations of the law, studies, articles and educational materials are prepared. Another important area of competition advocacy is cooperation with the media, members of academia, competition law practitioners and business representatives, whereby experts take part in various conferences, seminars and training.

6. COMPETITION ADVOCACY AND COMPETITION LAW ENFORCEMENT

Implementing competition protection policy is a complex, multi-level process. Mere enforcement of administrative prohibitions in competition law will not ensure effective protection of competition. Competition advocacy is an essential complement of competition authority enforcement actions.

In many cases, anti-competitive behaviour of private entities would not have been possible if not for unnecessary state intervention in the economy that only encouraged it. Proper legal or institutional solutions could in large part limit the need for intervention by competition authorities and thereby facilitate and increase effectiveness of such intervention when needed[1100]. Activities of competition authorities aimed at increasing public legal awareness undoubtedly contribute to increased effectiveness of competition law. Ensuring respect for competition rules in the legislative and law enforcement process, as well as in privatisation or public procurement may limit the risk of monopolisation and market abuse. In other words, competition authorities are able to significantly limit enforcement activities by promoting competition.

The role of competition authorities should, therefore, not only be to enforce competition law, but also to enhance public knowledge of the law and ensure that

1100 The taxi service sector can serve as an example here. Legal barriers in access to this profession resulted in anti-competitive agreements in this industry (see: decisions of the competition authority of 25 August No. RPZ 23/2006 or the decision of 9 June 2006 No. RWR 23/2006). The opening of the market to allow the presence of entrepreneurs providing transport of persons will (understandably) cause protests by those entrepreneurs who have made efforts and incurred costs in order to meet restrictive legal requirements. The above mentioned problem could have been avoided if *a priori* analysis of the rationale for introducing restrictions had been carried out.

government authorities respect the principle of fundamental state obligation in relation to competition protection of refraining from any activities that encourage anti-competitive behaviour[1101].

Even though competition and human liberty are pillars of a liberal state founded on the rule of law, these are not absolute values. Law-makers at times restrict competition in order to protect other socially relevant values. The role of competition authorities is to ensure that these restrictions are justified and proportionate. Utilising specialist knowledge and relevant legal instruments, competition authorities investigate potentially negative effects of proposed legal solutions and communicate them to the public and law-makers. At the same time, these authorities cannot remain indifferent toward values that may be placed at risk by competition restriction. In order to ensure proportionality and balance to these restrictions, it is essential to consider the importance of all conflicting interests in an objective and profound manner.

Competition authorities, acting as advocates of competition, should especially ensure that there are no competition restrictions arising from the negligence of law-makers, poor quality of the law or its inadequate implementation, lack of due respect for competition as a value, or activities of state authorities undertaken in bad faith or being simply unfair. All state authorities act as a single entity from a public standpoint, thus their actions with respect to citizens should be coherent, if ever the state is to enjoy citizens' trust. This trust is, in turn, necessary for a state to call itself democratic and founded on the rule of law.

Citizen confidence in the state is placed at risk when, on one hand, the state does not respect competition as a value in its own activities and, on the other hand, it severely punishes private entities disregarding this value. Such a discrepancy can even undermine the legitimacy of competition law and erode public approval for this authority to enforce this law. In extreme cases, competition law may merely serve to increase executive powers while encumbering private entities with heavy liability for errors made by the state[1102]. The problem of competition law'

1101 Long before the establishment of the modern, competition law, Adam Smith explained that this is in deed the basic obligation of the state in the area of competition protection – A. Smith – "Inquiry Into the Nature and Causes of the Wealth of Nations", PWN 2007, p. 152.

1102 This is an argument against competition law raised by the American philosopher, Ayn Rand, who states the following in "Voice of Reason": "Antitrust laws were the classic example of a moral inversion prevalent in history: an example of the victims, the businessmen, taking the blame for evils caused by government, and the government using its own guilt as a justification for acquiring wider powers on the pretext of "correcting" the evils".

legitimacy is particularly relevant today when there is ongoing debate in Europe on the criminalisation of gross anti-competitive practices.

It should also be recalled that competition authorities themselves employ administrative coercion. Competition enforced by means of administrative orders and sanctions is not a method with which actions of citizens *"can adapt to each other, without coercion of the state or its arbitrary intervention"*.

Free competition cannot exist without competition law based on state coercion just as personal freedom cannot exist without law supported by coercive power that protects such freedom against abuse by others. Undoubtedly, however, administrative intervention by competition authorities in economic freedom should be restricted to a minimum. Poor and overly restrictive competition law may constitute unjustified restriction of economic activity[1103]. European competition law system prior to its updating may serve as an example here[1104]. However, also a system based on direct application of competition law and lack of need to obtain individual exemptions overly complicated executive regulations as well as incoherent and excessively restrictive decisions of competition authorities and courts in issues related to competition law, together with severe sanctions, can also lead to legal uncertainty and result in disproportionate restriction of economic freedom.[1105]

1103 This is the threat to which Milton Friedman draws our attention by paradoxically concluding that competition law can do more harm than good to competition. M. Friedman, *The Business Community's Suicidal Impulse*, Cato Policy Report, March/April 1999 Vol. 21, No. 2.

1104 One of the aims of Community competition law reform introduced by means of Regulation 1/2003 was to reduce the number of obstacles and restrictions to enterprise caused by the system of individual notifications, rendering entrepreneurs unable to benefit from any general exemptions. See: R. Whish, *Competition Law,* 5th edition Reed Elsevier (UK) Ltd 2003, p. 246 and literature cited therein. Prior to its update, European competition law to some extent included a presumption that agreements between entrepreneurs were illegal. This presumption was exceptionally set aside in cases of general and individual exemptions. This must have cast doubts from the standpoint of respecting fundamental freedoms.

1105 It is still, for instance, difficult to reject the allegation that competition authorities often achieve certain non-economic goals in an arbitrary manner under the cover of competition protection policy. Making integration of the European market a reality by means of appropriate application of competition law is a widely discussed problem. Some decisions of the European Commission may raise doubts as to the importance of aspects such as environmental protection in the analysis of agreements between entrepreneurs in terms of their anti-competitive nature (cf. Decision of the European Commission on CECED (OJ [2000] L187/47, [2000] 5 CMLR 635). The problem is even more obvious in activities of competition authorities related to ensuring public aid legal compliance, whereby the influence of non-economic political factors can be particularly strong. Complications resulting from incoherent application of competition law are particularly obvious in global contracts and transactions assessed from the standpoint of threats to competition in various legal systems. A most recent example is the takeover of Sun Microsystems by Oracle Corporation. The transaction was almost immediately approved in the USA, whereas in Europe it encountered serious problems due to the fact it had to be reported to the European Commission (European Commission press release No. IP/09/1271).

It therefore seems that the most important element of competition advocacy should be the activity of competition authorities consisting of a critical analysis of their own actions and review of competition legislation from the standpoint of its efficiency, together with the proportionality of restrictions of economic freedom that it entails. The task of these institution is also ensure that competition law is applied reasonably and that it is not applied in areas where competition may occur in a natural manner free of any state intervention or pressure.

7. CONCLUSION

Competition advocacy is an important pillar of competition protection policy. Competition law could not be effective without it. The promotion of competition by competition authorities renders the process of competition law enforcement easier, increases the effectiveness of its outcomes and strengthens the legitimacy of competition authorities in exercising public authority.

Competition protection contributes to the development of a civic society and a state founded on the rule of law. It is, in fact, aimed at safeguarding the right of citizens to freedom and the shaping of mutual relations without state coercion. This right is protected at two levels: against abuse by private entities and against excessive intervention of the state. Competition authorities take relevant courses of action in each area. They exercise public authority to counter abuses on the part of private entities. In order to prevent excessive state intervention, competition authorities participate in the legislative process and law enforcement by other state agencies without recourse to public authority and seek to ensure that their exercise own power is not out of proportion.

BIOGRAPHIC NOTES

Virág Balogh

Virág Balogh is the head of Consumer Protection Section of the Hungarian Competition Authority (GVH). She completed her studies in law at the Eötvös Loránd University in Budapest, and is currently finishing her Master studies at the Budapest University of Economic Sciences. In 2008, she participated in the US Federal Trade Commission's International Fellowship Program, and spent three months at the FTC's Bureau of Economics.

Jan Krzysztof Bielecki

Jan Krzysztof Bielecki is a graduate of the University of Gdańsk. In 1973-1981 he worked at the University, teaching economics. He was one of the participants of the historic strike at the Gdańsk shipyard. In 1981 Mr Bielecki was removed from the University on account of his active participation in the activities of NSZZ "Solidarność". From 1985 to 1990 he chaired the Cooperative "Doradca", established by the members of "Solidarność". There he assisted the Trade Union in its opposition activities. In 1990 President Lech Wałęsa appointed Jan K. Bielecki Prime Minister. Mr Bielecki performed the function from January to December 1991. In 1992-1993 he acted as the Chairman of the Liberal-Democratic Congress (KLD), participated in the Parliamentary Committee on Foreign Affairs and was the Polish Delegate to the European Parliament and the Minister for European Integration in the cabinet of Hanna Suchocka. From December 1993 to October 2003 Jan K. Bielecki was an Executive Director of the European Bank for Reconstruction and Development. From 2003 to 2010 he acted as the President of Bank Pekao. On 5 March 2009 Jan Krzysztof Bielecki was awarded the title of the Financier of the Year 2008 by the newspaper "Gazeta Finansowa". The editorial team appreciated the fact that Mr Bielecki as one of the first among Poland's leading economists predicted the future economic downturn.

Henryka Bochniarz

Henryka Bochniarz has a PhD in economics and is a certified management consultant. She acted as the Minister of Industry and Trade in the cabinet of Jan Krzysztof Bielecki in 1991. She is the President of Boeing Central and Eastern Europe, the founder and President of the Polish Confederation of Private Employers Lewiatan and the Deputy President of BUSINESSEUROPE – the biggest organization of employers in Europe. Ms Bochniarz is also the Deputy President of the Tripartite Commission for Socio-Economic Affairs and the Committee of Good Practices. She won the Kisiel Award and the Andrzej Bączkowski Award for her special contribution to the development of social dialogue in Poland and undertaking activities spanning beyond political disparities. She was honoured with the Commander's Cross of the Order of Polonia Restituta.

Jacques Bourgeois

Jacques Bourgeois is Professor at the College of Europe, Bruges and a Consultant with WilmerHale, Brussels. A former senior official with the European Commission, Mr Bourgeois is, among other activities, currently the Chairman of the Competition Commission advising the Belgian government and the President of the Global Competition Law Centre (GCLC).

Barbara Brandtner

Barbara Brandtner was born in Vienna. She studied law at the University of Vienna and the College of Europe and has an LL.M. from University of Michigan Law School (Ann Arbor). Following activities in the national administration and private practice, she joined the Commission's Legal Service in 1996, and held a range of positions in several Cabinets, including as Deputy Head of Cabinet of Competition Commissioner Neelie Kroes. She took up her current position as Head of Unit "Enforcement and Procedural Reform" in DG Competition in April 2008.

Ayesha Budd

Ayesha Budd is an international lawyer who has been affiliated with the NMa since 2006. Ms Budd currently works in the Strategy and Communication Department as a Senior International Policy Advisor. Initially, she was case handler in the Merger Control Department and subsequently the Competition Department of the NMa. At that time, Ayesha was also responsible for the coordination of the NMa's involvement in the ECN. Prior to working for the NMa, Ayesha worked as a junior case handler for the European Commission, DG Competition and as a lawyer for Cleary Gottlieb, Cologne, and Clayton Utz, Sydney.

Gergely Csorba

Gergely Csorba is the chief economist of the Hungarian Competition Authority (GVH) and also research fellow at the Institute of Economics (Hungarian Academy of Sciences). He completed Master studies in Economics at the Budapest University of Economic Sciences and at the University of Toulouse, and received his PhD degree in Economics from the Central European University. He published on industrial organizations and competition policy in various journals such as the Journal of Industrial Economics, International Journal of Industrial Organization and Information Economics and Policy.

Claudia Dörr

Claudia Dörr is a qualified lawyer. She began her professional career in the Federal Ministry of Economics in 1989; since then, she has always worked in positions related to the EU and other international issues: initially as deputy head of division for EU and OECD relations in the context of the state export credit insurance systems; from 1995-1998 head of section in charge of trade policy, transatlantic relations, relations with Latin America, Asia and Central and Eastern Europe in the economic department of the Permanent Mission of the Federal Republic of Germany to the EU in

Brussels, latterly as deputy head of the economic department. From the end of 1998 until March 2001, Ms Dörr headed the division responsible for trade policy (EU, WTO) in the Federal Ministry of Economics and Technology (BMWi) and from April 2001 to February 2006 she was Deputy Director-General responsible for "European policy" in the BMWi/BMWA (Federal Ministry of Economics and Labour).

Since February 2006, Ms Dörr has been Director-General responsible for "European policy" in the BMWi.

Anna Fornalczyk

Anna Fornalczyk is the member of the Board of Directors of the Polish-American Freedom Foundation, as well as the Governing Board of the European Policy Centre in Brussels and the Center for Application of Modern Technologies in Warsaw. She is also a professor at the Faculty of Organisation and Management at the Technical University of Łódź. She has lectured at the Central European University in Budapest.

In 1990-1995 Ms Fornalczyk was the President of the Antimonopoly Office. In 1991 she took part in the negotiations between Poland and the European Union concerning the Association Agreement. She was responsible for the negotiations on competition and State aid. From the very beginning of Poland's integration with the EU she was involved in the process of harmonising the Polish law on competition and State aid with the Community standards.

Her publications focus primarily on the issue of competition in the context of restructuring, privatisation, de-monopolisation and State aid both in Poland and the European Union. She is a partner at Comper, Fornalczyk i Wspólnicy, which provides consultancy services related to competition protection policy, mergers and acquisitions, State aid and determining companies' market position. She authored many publications, including a paper on competition law and policy and a book *Biznes a ochrona konkurencji*, published in 2007.

Peter Freeman

Peter Freeman is the Chairman of the UK Competition Commission. He was appointed Chairman in 2006, having been a member since May 2003 and a Deputy Chairman since September 2003. Prior to joining the Competition Commission, he was head of the EC and Competition Law Group of the international law firm Simmons & Simmons. He was co-founder of and, until 2007, Chairman of the Regulatory Policy Institute, is a Consulting Editor of Butterworths' Competition Law, and is a member of the Advisory Boards of the Competition Law Journal, the International Competition Law Forum and the ESRC Research Centre for Competition Policy.

David Gerber

David J. Gerber is University Distinguished Professor of Law at Chicago-Kent College of Law, Illinois Institute of Technology. He received his B.A. from Trinity College (Conn.), his M.A. from Yale and his J.D. from the University of Chicago. He has been a visiting professor at the law schools of the University of Pennsylvania, Northwestern University and Washington University in the United States as well as on the law faculties in Munich and Freiburg in Germany, Stockholm and Uppsala in Sweden, and Meiji University in Japan. He has also been a visiting fellow at the Woodrow Wilson School of Public and International Affairs at Princeton University and the Max Planck Institute for Research on Collective Goods in Bonn, Germany. Before beginning his teaching career, Professor Gerber practiced law in New York and in Europe. He writes and teaches primarily in the areas of comparative law, international and comparative competition law, international economic law (esp., competition law and business regulation) and European Union law. He is a member of the International Academy of Comparative Law, the executive editorial board of the American Journal of Comparative Law and the editorial boards of the Journal of International Economic Law and Concurrences (France). His most recent book is *Global Competition: Law, Competition and Global Markets* (Oxford U. Press., 2010).

Stanisław Gronowski

Stanisław Gronowski graduated from the Faculty of Law and Administration at the Adam Mickiewicz University in Poznań in 1969, where he subsequently obtained a PhD in law in 1979. After graduating from law school, he worked with the State Economic Arbitration as an arbitrator of the Central Arbitration Committee. As of 1 September 1989 he was appointed judge at the Voivodeship Court (now District Court) in Warsaw. From April 1990 to June 2000 he was the President of the Antimonopoly Court, now the Court of Competition and Consumer Protection. On 1 July 2000 he took up the post of a judge at the Supreme Administrative Court, which he holds until now. He is an author of many publications related, *inter alia*, to competition and consumer protection law, energy law and industrial property rights.

Scott Hammond

Scott Hammond is the Antitrust Division's Deputy Assistant Attorney General for Criminal Enforcement. He is responsible for the Division's criminal investigations and litigation nationwide. Since joining the Division in 1988, Mr Hammond has also served as the Director of Criminal Enforcement, Senior Counsel for Criminal Enforcement to the Assistant Attorney General, and as a trial attorney in one of the Division's litigation sections.

Leigh Hancher

Leigh Hancher is Professor of European Law at the University of Tilburg, the Neterhlands, and Of Counsel to Allen & Overy, Amsterdam. She is co-author of EU State Aid Law – now in its 3rd edition and of numerous articles on state aid. She is a member of the editorial board of the European State Aid Law Quarterly.

Alberto Heimler

Alberto Heimler is professor of economics at the Scuola Superiore della pubblica amministrazione (the Italian School of Government) and advisor of the Italian Competition Authority on international matters. He is the Chairman of the Working Party on Competition and Regulation of the Competition Committee of the Organization of Economic Cooperation and Development (OECD). Until 2008 he was in charge of research and international affairs at the Italian Competition Authority and until 2009 he was member of the Steering Group of the International Competition Network (ICN) and co-chair of the Working Group on the Operational Framework. He has published extensively on antitrust and regulatory issues in leading academic journals.

David Henry

David Henry graduated from the LLB with European Legal Studies programme at King's College, London. He also obtained an LLM in European Community Law from the College of Europe, Bruges. Mr Henry has worked as a research fellow at the Institute for European Legal Studies, University of Liege and completed the Bar Vocational Course at the Inns of Court School of Law, London where he was a Diplock scholar of the Honourable Society of the Middle Temple. He is an EU inter-institutional competition laureate and, having completed a period of pupillage at a leading set of commercial chambers in London, he now works as an associate at Howrey LLP, Brussels. Mr Henry is involved in cases pertaining to Articles 101 and 102 TFEU and merger control. His experience spans a wide range of industries including air transport, chemicals, electronics and semi-conductor products. He has also published a number of articles in various fields of EU competition law.

Hanna Jahns

Hanna Jahns holds a degree from the Poznań University of Economics, where she studied at the Faculty of International Business and Economics in the Department of European Studies. In 2002 she obtained a PhD in economics from the Collegium of World Economy at the Warsaw School of Economics. She was awarded a scholarship as part of the European Studies programme: Economic and political integration in the EU (European Union TEMPUS programme). Under the programme in 1997 she studied at the Aalborg University in Denmark. In 1998-2006 she worked as an assistant professor at the Institute of Business Cycles and Prices in Foreign Trade. Hanna Jahns has gained her professional experience working with the Ministry of Regional Development and Construction, the Permanent Representation of the Republic of Poland to the European Union, and from March 2007 in the Directorate General for Regional Policy, where she managed the Budget Team. From December 2007 to February 2010 she was Secretary of State at the Ministry of Regional Development. She has authored and co-authored several academic publications and articles.

René Jansen

René Jansen has been involved in the NMa since its inception in 1998. Mr Jansen has served not only as a member of the Board of Directors (since July 2005), but also as Director to both the Merger Control Department and the Antitrust Department and as Acting Director General for a substantial part of 2003 (in the years before the NMa became an independent administrative body). He is a former member of the Board of Directors of the Netherlands Competition Authority (from July 2005 through October 2009 he served as a member of the Board of Directors).

Knut Eggum Johansen

Knut Eggum Johansen is Director General of the Norwegian Competition Authority since 1999, and has been appointed for a second six year term until April 2011. Before joining the Norwegian Competition Authority, he held various leader positions at the Norwegian Ministry of Finance, in particular in the Department of Administrative Affairs, the Department of Customs and Indirect taxation, the Economic Policy Department and the Planning Department. From 1986 to 1988, he was a Counsellor of Embassy at Norway's Permanent Delegation to the OECD in Paris. In the early eighties he also worked at the Institute of Applied Social Research (Oslo) in the framework of a research exchange programme. He graduated from the University of Oslo (Master of Sciences in Economics) in 1970, and has spent one year doing postgraduate studies at the Department of Economics at the University of Minnesota (1975/76). He has also attended the Norwegian School of Business Administration (AFF Leadership Development Programme).

Krzysztof Kanton

Krzysztof Kanton is a partner at the Antitrust and Competition Department of the Sołtysiński & Szlęzak law firm. He holds a degree in law from Warsaw University. He is a legal advisor and a member of the Warsaw Association of Legal Advisers. As regards competition law he advises in investigations and antitrust proceedings carried out by the President of the Office of Competition and Consumer Protection, as well as in court proceedings concerning competition restricting practices. He took part in several antitrust proceedings on merger clearances, including large international transactions such as Exxon/Mobil, AOL/TimeWarner and Sony/Bertelsmann, and transactions resulting in a significant concentration of market shares in Poland. He also provides ad hoc counsel on broadly understood antitrust law issues, for example, by verifying distribution contracts with respect to their compliance with the competition law.

Magdalena Kąkol

Magdalena Kąkol obtained her degrees in economics and law at the Maria Curie-Skłodowska University in Lublin. At the moment, she is working as an assistant professor at the University's Faculty of Economics, in the Chair of World Economy and European Integration. She took part in a scholarship programme at the University of Kent in Canterbury. She also completed scientific traineeships at the University of Regensburg and in the European University Institute in Florence. She authored over 40 publications; approximately half of them concern competition policy.

Peter Klocker

Peter Klocker is Vice President of the Bundeskartellamt (German Federal Cartel Office). After a 20-year career with the Federal Ministry of Economics, Mr Klocker joined the Bundeskartellamt in 2000, first as Head of Department (General Competition Law Issues) and since 2005 as Vice President. He started his career in the Federal Ministry of Economics in the field of education policy. In 1984 he was posted to the German Permanent Mission to the United Nations in Geneva, where his field of activity was the UNCTAD. In 1985 Mr Klocker returned to the Federal Ministry of Economics where he worked in the "Competition Policy" Section. In 1992 he became head of the "Social Policy" Section and in 1998 head of the "Telecommunications Policy" Section. Mr Klocker holds a doctorate degree in law from the University of Münster, where he also took his First State Examination in Law. Before taking the Second State Examination he completed the required practical training in law at several courts and administrative bodies in Bremen and Hamburg.

William E. Kovacic

William E. Kovacic has served on the Federal Trade Commission since January 2006, and served as Chairman from March 2008 until March 2009. Mr Kovacic was the agency's General Counsel from 2001 through 2004, and he worked for the Commission from 1979 until 1983, initially in the Bureau of Competition's Planning Office and later as an attorney advisor to former Commissioner George W. Douglas. Before he became a Commissioner, Kovacic was the E.K. Gubin Professor of Government Contracts Law at George Washington University Law School, where he began teaching in 1999. He had taught at the George Mason University School of Law since 1986, after practicing antitrust and government contracts law for three years at Bryan Cave's Washington, DC, office. Earlier in his career, Mr Kovacic spent one year on the majority staff of the U.S. Senate Judiciary Committee's Antitrust and Monopoly Subcommittee. Since 1992, Mr Kovacic has been an adviser on antitrust and consumer protection issues to the governments of Armenia, Benin, Egypt, El Salvador, Georgia, Guyana, Indonesia, Kazakhstan, Mongolia, Morocco, Nepal, Panama, Russia, Ukraine, Vietnam, and Zimbabwe. Mr Kovacic received a bachelor degree from Princeton University in 1974 and a law degree from Columbia University in 1978. He and his wife, Kathryn Fenton, reside in Virginia.

Małgorzata Krasnodębska-Tomkiel

Małgorzata Krasnodębska-Tomkiel holds a PhD in law. She was appointed the President of the Office of Competition and Consumer Protection on 4 June 2008. Earlier, since 21 June 2007 she acted as the Office's Vice-President and was responsible for the operations of the Department of Competition Protection, Department of Legal Affairs and European Jurisprudence and Department of Market Surveillance. She has been working for the Office since 1998. Ms Krasnodębska-Tomkiel is a lecturer of Community and antitrust law at the Warsaw School of Economics and the Higher School of Public Administration in Ostrołęka. She also cooperates with Collegium Civitas and the Pultusk Academy of Humanities. Ms Krasnodębska-Tomkiel is the author of several publications related to Polish and Community competition protection law, including academic publications, glosses to the decisions of the Polish Supreme Court and press articles.

Bruno Lasserre

Bruno Lasserre has been, since March 2009, the President of the French Autorité de la concurrence (Competition Authority). He was born in 1954. He is a graduate of the French National School of Administration (ENA), after which he joined the Conseil d'Etat (Supreme Administrative Court). He now has the rank of Conseiller d'Etat. After eight years spent at the Conseil d'Etat, he joined the French Ministry of Posts and Telecommunications, where he ultimately became Director General. During his eight years' tenure, he was the main architect of a comprehensive overhaul of the telecommunications sector, culminating in its full opening to competition, in the creation of an independant regulator and in the privatisation of the historic incumbent. He then returned to the Conseil d'Etat, where he became Deputy-Chairman for litigation. In parallel, he served as Member (1998-2004) and then as President (2004-2009) of the French Competition Council. He is the author of a number of reports commissionned by the French Prime Minister. He was also a member of the Commission for the Liberation of French Growth. He is Officer of the Légion d'honneur.

Philip Lowe

Philip Lowe was born in Leeds in 1947. He read Politics, Philosophy and Economics at St John's College, Oxford and has an M. Sc. from London Business School. Following a period in the manufacturing industry, he joined the European Commission in 1973, and held a range of senior posts as Chef de Cabinet and Director in the fields of regional development, agriculture, transport and administration, before becoming Director General of the Development DG in 1997. From September 2002 to February 2010 he was Director General of the DG Competition and currently is Director General of the Energy DG.

Grzegorz Materna

Grzegorz Materna has been working for the Office of Competition and Consumer Protection since 2001. In 2005 he was appointed the Deputy Director of the Branch Office in Warsaw and since November 2009 he has acted as the Director of the Department of Competition Protection. He has a PhD in law and he graduated from the Faculty of Law and Administration at the Warsaw University. He is an assistant professor in the Institute of Legal Studies of the Polish Academy of Sciences. Mr Materna has authored a range of publications on competition law and antitrust policy, and co-authored the commentary to the Act on competition and consumer protection edited by T. Skoczny, A. Jurkowski and D. Miąsik.

Elżbieta Modzelewska-Wąchal

Elżbieta Modzelewska-Wąchal is a legal advisor at the law firm Centrum Prawa Konkurencji. She has been practising competition law continuously since 1987. In 1990-2001 she worked with the Antimonopoly Office (now the Office of Competition and Consumer Protection), first as the Director of the Department of Jurisprudence and from February 1996 until the end of 2001, as a Vice-President of the Office responsible for competition, including State aid. In 1992-1993 she worked as an expert on de-monopolisation and competition for the competition authorities in Ukraine and

Belarus. From 1998 until the end of 2001 she was a member of the Polish EU accession negotiating team responsible for competition policy (covering antitrust and State aid issues) and consumer protection and health. Ms Modzelewska-Wąchal lectures in several higher education institutions and she is an expert for the Sejm (lower chamber of the Polish parliament). She is a co-author of the Act on competition and consumer protection, as well as author of several publications devoted to competition, including *Ustawa o ochronie konkurencji i konsumentów. Komentarz*, Twigger, Warsaw 2002; *Pomoc publiczna dla przedsiębiorców. Komentarz*, Wydawnictwo Prawnicze „LexisNexis" 2003; *Spółka akcyjna w praktyce*, Verlag Dashofer 1997-2003. She cooperates with several market leaders and public administration agencies. She is ranked as one of the leading competition lawyers in such rankings as Global Counsel 3000 Highly Recommended Competition/Antitrust Practitioner in Poland, the *Rzeczpospolita* daily in 2007 and *Forbes* magazine in 2008 and 2009 – most recommended lawyer in the field of competition law in Poland.

Ann O'Brien

Ann O'Brien is Senior Counsel to the Deputy Assistant Attorney General for Criminal Enforcement in the U.S. Department of Justice's Antitrust Division. Her responsibilities include reviewing domestic and international cartel case recommendations, handling criminal enforcement policy matters, and advising foreign governments in the development and implementation of their cartel enforcement programs. Since joining the Division in 2000, Ms O'Brien has also served as a Special Assistant to the Directors of Enforcement and as an attorney in the Division's Cleveland Field Office.

Cormac O'Daly

Cormac O'Daly is an Irish and English-qualified Solicitor and has worked with WilmerHale since 2004. He is a Counsel in the firm's Brussels office. Mr O'Daly specializes in antitrust work including merger control, cartels, vertical and horizontal agreements and abuses of dominant positions. Before joining WilmerHale, Mr O'Daly was an associate in the competition department of a UK law firm and he has also been a stagiaire and référendaire to Advocate General Fennelly at the European Court of Justice.

Balázs Pálvölgyi

Balázs Pálvölgyi has been working as an economic expert at the Hungarian Competition Authority (GVH) since 2002. He received his Master degree in Economics from the Budapest University of Economic Sciences. He was also working as an expert at the OECD in 2005- 2006. His main expertise lies in competition advocacy and building of competition culture.

Soultana Paschalidou

Soultana Paschalidou studied law at the University of Heidelberg and is a graduate of the European Legal Studies Department of the College of Europe (Bruges). She trained with WilmerHale in Berlin and Brussels and qualified in Berlin in 2005. Ms Paschalidou joined the European Commission in the same year. She first worked for DG Employment and Social Affairs, where she was responsible for labour law. In April 2009, Ms Paschalidou joined DG Competition where she was dealing with the enforcement of state aid rules. Ms Paschalidou became a member of the Cabinet of Maria Damanaki, European Commissioner for Maritime Affairs and Fisheries, in February 2010.

Mercedes Pedraz Calvo

Mercedes Pedraz Calvo studied law in Salamanca University (Spain) and got an EEC law degree at the College of Europe (Brugge Belgium). She worked as a lawyer and university professor (University of Salamanca Law School, International Law Department) until March 1987 when she became a judge, working first in criminal and civil law courts and since January 1992 at the Audiencia Nacional, in Madrid. That Tribunal is in charge of reviewing the Spanish Competition Authorities decisions. She is the author of several books on competition law and other legal issues.

Nicolas Petit

Nicolas Petit is a full-time Lecturer ("Chargé de cours") in competition law and economics at the University of Liege School of Law (ULg) and co-director of its Institute for European Legal Studies (IEJE, www.ieje.net). He holds a PhD (thesis on Oligopolies and tacit collusion in EU competition law, April 2007), a LL.M in European Law with Highest Honors (College of Europe, Bruges – 2001-2002) and a DESS in European Business Law (University Paris II, Panthéon Assas 2000-2001). From 2005 to 2009, Nicolas Petit was an associate at Howrey LLP, Brussels. In 2008, he was awarded the Jacques Lassier Prize by the International League of Competition Law and the second PhD prize of the *Concurrences* review. In addition to this, over the past years Mr Petit has served as the Executive Secretary of the Global Competition Law Centre (GCLC) of the College of Europe. Nicolas Petit's main research interests cover Abuse of Dominance, Economics of Competition Law, Network Industries and Enforcement issues in EU, Belgian and French competition law.

Marta Sendrowicz

Marta Sendrowicz has a PhD in law. She is an assistant professor at the Department of European Law at the Faculty of Law and Administration of Warsaw University. Ms Sendrowicz is a legal advisor at the Allen & Overy, A. Pędzich law firm in Warsaw. She represents clients in different types of proceedings taking place before the Polish and European competition authorities, as well as in court proceedings.She is a member of the Management Board of the Competition Law Association. Her major interest is competition law; in particular she studies its functioning in the pharmaceutical, telecommunications, banking, construction and FMCG sectors.

Stanisław Sołtysiński

Stanisław Sołtysiński is the co-founder and now also partner at the Sołtysiński & Szlęzak law firm. He specialises in company law, intellectual property rights and competition law. He participated in the development of the first Polish competition act. He also took part in the drafting of the International Antitrust Code (1993), where he was a member of an international expert group chaired by Professor W. Fikentscher.

Jarosław Sroczyński

Jarosław Sroczyński is a lawyer and economist. He was also the founder of UOKiK's Branch Office in Kraków and its first director. He participated in the legislative works concerning competition and consumer law, acting, *inter alia*, as UOKiK's legal expert on the implementation of the Directive on combating unfair commercial practices. He also advised the Ukrainian Antitrust Committee as an EU expert. Mr Sroczyński has been a legal advisor specialising in competition law for several years now, currently he is a partner at the Markiewicz&Sroczyński law firm.

Mikołaj Stasiak

Mikołaj Stasiak is an expert on State aid, working with the Office of Competition and Consumer Protection for several years now. In 2004-2008 he worked for the Permanent Representation of the Republic of Poland to the European Union and in the European Commission's Directorate General for Energy and Transport. He authored several publications devoted to State aid issues. At present, he runs his own consultancy firm Easy State Aid Mikołaj Stasiak, which provides expert advice to administrative agencies and businesse, both with respect to State aid admissibility, as well as the procedures before the European Commission.

Walter A. Stoffel

Walter A. Stoffel (Dr. iur. University of Fribourg/Switzerland, 1979; LL.M. Yale Law School, 1976; admitted at the Zurich Bar, 1979) is President of the Swiss Competition Commission (since 1st January 2003) and Member of the Swiss Council of Science and Technology (since 1st April 2003). Formerly Dean of the Faculty of Law, he continues to be Professor for Company Law, Bankruptcy Law and Private International Law at the University of Fribourg. From 1995-2001 he was Scientific Director of the International Association of Legal Science (IALS) and Member of the Board of the European Association of Law Faculties (ELFA; 1998-2001). He also was a Foreign Expert Member of the Belgian National Research Foundation and a Foreign Legal Expert for the German *Gesellschaft fuer technische Zusammenarbeit* on Small and Medium Sized Enterprises in China. He continues to hold membership in numerous national and international professional associations and lectures, frequently or occasionally in universities in Italy, Canada, Australia, the United States, France and Turkey, as well as in Israel, Spain, Germany, Denmark, China, Serbia and Taiwan.

Kjell J. Sunnevåg

Kjell J. Sunnevåg is working as a research manager and economist at the support staff of the Norwegian Competition Authority. He graduated from the University of Bergen (M. Sc. in Economics from 1987). He has worked as a research economist since 1987, his last position being as a research manager at the Foundation for Research in Economics and Business Administration (SNF), where his research extended to energy economics, environmental economics, petroleum tax policy as well as public policy and economics. From 2000 to 2001 he spent a year as a visiting scholar at the Department of Economics at the University of California, Santa Barbara. In the last few years, he has worked as a senior advisor and research manager at the Norwegian Competition Authority, i.a. leading the work on the two recent joint reports by the Nordic competition authorities. He has recently coauthored the Palgrave Macmillan book "Making Essential Choices with Scant Information: Front-end Decision Making in Major Projects" with Terry Williams and Knut Samset; the book which was published in 2009.

Małgorzata Szwaj

Małgorzata Szwaj is a legal advisor and an expert in competition law and European law. She has authored a range of topical publications and lectures at the National School of Public Administration. Ms Szwaj chairs the team of lawyers dealing with competition and EU law at Linklaters' Warsaw office. She was recognised as a leading expert in competition law in Poland by *PLC Which lawyer? Yearbook 2008*, *An International Who's Who of Competition Lawyers*, *Guide to the World's Leading Competition and Antitrust Lawyers*, the *Rzeczpospolita* daily and *Forbes* magazine.

Wojciech Szymczak

Wojciech Szymczak is the Director of the Department of Market Analyses at the Office of Competition and Consumer Protection. He deals with economic and market aspects of settlement proceedings undertaken by the Office as regards competition protection, as well as for market studies and economic analyses performed in the Office. He graduated from the Faculty of Economic Sciences and Management at the Nicolas Copernicus University in Toruń; he has a PhD in economics. He completed a post-doctoral European Programme at the Sussex European Institute, University of Sussex in Brighton, as well as a methodological course related to case study application in economic sciences – the International Faculty Program in IESE Business School, University of Navarra in Barcelona.

Monika Tomczak-Górlikowska

Monika Tomczak-Górlikowska is an attorney and senior associate at the Miller, Canfield, W. Babicki, A. Chełchowski and Wspólnicy law firm. After graduating from the Faculty of Law and Administration at the University of Gdańsk, she studied Community law at the University of Lyon and at the Faculty of Law at the College of Europe in Belgium, where she obtained her Master of European Law (LLM) *cum laude*. She has been specialising in competition law and intellectual property rights for several years. In 2002-2003 she worked at the Legal Service of the General Secretariat of the Council of the European Union in Brussels, drafting the Treaty of Accession of Poland and other European Union candidate countries, as well as working on the Polish wording of the Community law. She is often a speaker during conferences devoted to competition law, as well as intellectual property rights. She has also authored publications on the above issues. Moreover, Ms Tomczak-Górlikowska is a consultant of the Legal Department of the European Central Bank.

Tomasz Wardyński

Tomasz Wardyński is an attorney, partner and a co-founder of the Wardyński i Wspólnicy law firm. He was one of the first attorneys in Poland to specialise in Community law and competition law. He is a member of the Competition Law Association. He graduated from the Faculty of Law at Warsaw University (1970), and went on to study at the College of Europe in Bruges and the Institute of European Studies at the University of Strasbourg. Mr Wardyński has been practicing law since 1979. In 2001 he was appointed the Honorary Commander of the British Empire. He is an arbitrator of the Court of Arbitration operating by the Polish Chamber of Commerce, the Court of Arbitration operating by the Polish Confederation of Private Employers "Lewiatan", as well as at the International Arbitral Centre of the Austrian Federal Economic Chamber (VIAC) in Vienna. He is a member of the Bar Association in Warsaw. Mr Wardyński is an active member of the International Bar Association (IBA) and the European Circuit of the Bar of England and Wales.

Stanley Wong

Dr Stanley Wong was appointed Member of the Competition Authority of Ireland by the Government of Ireland in October 2005. He commenced his five-year term in February 2006. The five Members with one Member as Chairman serve as the executive and the board of the Authority. The Authority enforces Irish and EU competition law in Ireland. He is currently the Member responsible for the Mergers Division, serving as its Director. From 2006 to 2008, he served as Director of the Monopolies Division. Dr Wong has represented the Authority on various projects of the European Competition Network and in consultations of Member States by the European Commission on major cases and policy initiatives such as Article 82 guidance and private damages actions and in the work of the Competition Committee and Working Party No. 3 of the Organisation for Economic Co-operation and Development (OECD) and Unilateral Conduct and Mergers Working Groups of the International Competition Network (ICN). He currently serves as co-chair of the ICN Mergers Working Group. He frequently writes and speaks about competition law and policy at many international forums. Prior to joining the Competition Authority he was a Partner and head of the competition law practice in the Canadian law firm Davis & Company LLP (now Davis LLP). His practice included appearing as trial and appellate counsel before the Competition Tribunal (Canada) and courts as well as providing advice on the application of competition law to business practices and mergers and acquisitions. He has served as Chair of the National Competition Law Section of the Canadian Bar Association. Dr Wong is qualified as an economist and a lawyer. He holds two degrees in economics (B.A. Simon Fraser University and Ph.D. University of Cambridge, King's College) and a law degree (LL.B., University of Toronto). He is qualified to practice law as a barrister and solicitor in Canada (Ontario and British Columbia) and as a solicitor in England and Wales (non-practicing). In private practice, he was recognized internationally as a leading competition lawyer. Prior to entering the practice of law, he was Associate Professor of Economics at Carleton University (Ottawa).

Bohdan Wyżnikiewicz

Bohdan Wyżnikiewicz holds a PhD in economics (Warsaw University) and is the Vice-President of the Gdańsk Institute for Market Economics. He completed econometric studies at the Main School of Planning and Statistics (now: Warsaw School of Economics). In 1991-1992 he acted as the President of the Central Statistical Office. He also worked at the United Nations Economic Commission for Europe, the Institute of Science Policy and the Institute of Economic Sciences of the Polish Academy of Sciences. He is an expert of the Sejm (lower chamber of the Polish parliament), Warsaw Stock Exchange, Polish Confederation of Private Employers "Lewiatan", the Conference Board Europe and Oxford Analytica. He is also an arbitrator of the Court of Arbitration operating by the Polish Financial Supervision Authority. He is a guest lecturer in many higher education institutions, e.g. Warsaw School of Economics and Warsaw University. He is an expert in applied economics, macro-economic analyses and market and sector studies. He wrote over one hundred reports, studies and academic papers; he is also a business columnist.

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Office of Competition
and Consumer Protection
Plac Powstańców Warszawy 1
00-950 Warsaw, Poland
tel. +48 22 55 60 800
e-mail: uokik@uokik.gov.pl
www.uokik.gov.pl