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ROUNDTABLE ON FAILING FIRM DEFENCE

-- Note by the Delegation of Poland --

This note is submitted by the delegation of Poland to the Competition Committee FOR DISCUSSION at its forthcoming meeting to be held on 21 - 22 October 2009.

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FAILING FIRM DEFENCE

-- Note by Poland --

1. The *failing firm defence* concept (hereinafter also referred to as "FFD") has not been directly regulated in the Polish antimonopoly law. In consequence neither Polish antimonopoly authority nor courts has presented their opinions on the subject. It does not mean, however, that when conducting merger investigations the problem of companies at risk with bankruptcy has not been discussed. Despite the fact that Polish law lacks regulation directly referring to the *failing firm defence* concept, it is possible to find in the Polish law some provisions which indirectly refer to the concept in question. Two provisions should paid particular attention:

1. Article 14.4 of the Antimonopoly Act, which excludes the obligation to notify the concentration of entrepreneurs if the concentration takes place in the course of bankruptcy proceedings.

2. Article 20.2 of the Antimonopoly Act introducing as an additional concentration assessment test, a public interest test, which gives the possibility of accounting for the *failing firm defence* concept when using the test to assess concentration.

1. Excluding obligation to notify concentration of entrepreneurs if concentration takes place in the course of bankruptcy proceedings.

2. In the Polish antimonopoly law entrepreneurs are obliged to notify their intent of concentration when turnover criteria are met (Article 13.1 of the Antimonopoly Act) and when a transaction is considered to be a form of concentration, specified in the Act (Article 13.2 of the Antimonopoly Act)[1]. However, Article 14 of the Antimonopoly Act specifies situations in which entrepreneurs are not obliged to notify their intent of concentration. Pursuant to Article 14.4 of the Antimonopoly Act, there is no obligation to notify the intent of concentration if this concentration takes place in the course of bankruptcy proceedings, providing that the entrepreneur which intends to take over the control is not a competitor or does not belong to a capital group composed of competitors of an entrepreneur which has been acquired. The basis for this provision is the observation that concentrations taking place in conditions specified in this norm do not have any negative impact on the market and thus, do not have to be subject to assessment performed by an antimonopoly authority. Thus, the aim of this regulation is to reduce charges and limit transaction costs borne by entrepreneurs, as well as a better allocation of powers and funds of an antimonopoly authority.

3. The analysis of Article 14.4 leads to the conclusion that the article will be applied providing that two premises are met simultaneously:

1. Concentration takes place in the course of bankruptcy proceedings;

[1] Polish Antimonopoly Act does not include a definition of concentration, it only provides the information on what types of transactions are considered to be concentrations.

2. An entrepreneur taking over the control is neither a competitor nor is a member of a capital group composed of competitors of an entrepreneur which has been acquired.

4. When analyzing the first premise, it is important to note that it refers to a situation in which bankruptcy proceedings are in progress or when a sale transaction of an entrepreneur is a direct result of such proceedings. Further resale of an acquired bankrupt enterprise will be subject to notification. Additionally, it refers to a situation in which bankruptcy proceedings are conducted in Poland, in a Polish court and based on Polish legal regulations. Thus, the regulation in question does not apply to situations in which bankruptcy proceedings take place abroad. The second important premise is that an entrepreneur taking over the control is neither a competitor nor is a member of a capital group composed of competitors of an entrepreneur which has been acquired. According to the definition provided in the Polish Antimonopoly Act, a competitor is an entrepreneur who simultaneously introduces or may introduce, purchase or may purchase goods on a relevant market (Article 4.11 of the Antimonopoly Act). In practical terms it means that the provision in question is used by banks and investment funds.

2. Failing firm defence as an important circumstance taken into account when applying public interest test.

5. A basic merger test in Polish law is SIEC test. However, a public interest test is an additional merger test, which can be applied in certain situations. Pursuant to Article 20.2, Polish antimonopoly authority gives its consent for concentration, which will result in a significant impediment to competition, particularly by creating or by strengthening dominant position, providing that there exist overriding public interest and particularly if:

1. concentration will contribute to economic development or to technical progress; or

2. concentration may have positive impact on the national economy.

6. Analyzing above premises it may be said that especially the second provision may be used for the purposes of applying FFD. Bankruptcy of inefficient companies may result in significant negative social effects, i.e. unemployment. This argument was raised several times during the debate on rescuing Polish shipyards. Threat of unemployment may be exemplified by two decisions of Polish antimonopoly authority which concerned the establishment of two energy groups, i.e. Polska Grupa Energetyczna[2] and Grupa Tauron[3]. When justifying approval for these anticompetitive mergers between energy producers Polish antimonopoly authority referred to the analysis of Polish needs in the area of energy, namely obsolete and too small capacity as far as energy in Poland is concerned. What is important, the OCCP indicated also that concentrations in question would contribute to the Polish energy security and would result in saving of workplaces.

7. It is also important to take account of procedural consequences of such a construction of the provisions in question. If SIEC test constitutes a basic merger test and a public interest test is an exception, it determines the distribution of burden of proof. In case of a SIEC test, it is an antimonopoly authority which shall prove that a notified concentration leads to significant impediment to competition. Whereas if we resign from applying this basic merger test, it is the party to the proceedings which shall prove that an intended transaction will contribute to economic development or to technical progress, or that it can have a positive impact on the national economy. It is an entrepreneur who, as a professional, has complete knowledge about the market on which he or she conducts business activities, as well as about consequences that a notified concentration can have. Consequently, it is an entrepreneur who shall prove

2 Decision of the OCCP President of December 22, 2006, No. DOK 163/06, not published.

3 Decision of the OCCP President of March 8, 2007, No. DOK 29/07, not published.

that his or her personal benefits which result from a given transaction translate into general social benefits accessible to all market participants. The role of an antimonopoly authority in the proceedings is to verify the above mentioned assertions in the hearing of evidence in order to balance values protected by law and to make a final decision.

8. Another aspect of the discussed regulation, related to the proceedings, is an exceptionally high standard of burden of proof which rests on a given party. Evidence proceedings, based on Article 20.2, is rather complicated. It results from the fact that every concentration may have both positive and negative impact on the market. Generally, positive and negative effects appear simultaneously, and as a result, after producing evidence, Polish antimonopoly authority has to balance all anti-competition and pro-competition effects of concentration. It is important to note that if Article 20.2 is applied, the nature of pro-competition effects of concentration should be exceptional, since benefits resulting from a transaction will have to concern as many entities as possible, if not all consumers. The same applies when party tries to rely on FFD considerations.

- Harmonisation and evolution.

9. As stated above there is no explicit regulation of FFD in Polish law. Neither there has been any discussion on this subject. It may be result of rather insignificant number of cases when parties are invoking FFD considerations. Existing legal framework responds to those considerations and sees to work fine. Therefore we see no need for harmonization of national approaches to the FFD, for jurisdictions where the FFD concept is absent. However, it may be a case for those national jurisdictions which regulated FFD.

- Market context.

10. When analyzing market context one should bear in mind particularities of Polish economic transformation. During the last decade of XX century Poland was confronted with several declining industries. Polish antimonopoly authority had to deal with this issue in numerous of cases. However, it has never been accepted that declining industries should be treated in a special, more lenient way. The only exceptions were situations when overriding public interest came into play.

- Should the FFD Analysis Be Changed During Economic Crises?

11. Despite the economic crisis, Polish antimonopoly authority has not noticed in the examined cases the multiplication of arguments referring to the crisis, including arguments raising the issue of the FFD. Because of the lack of direct regulation of the FFD in the Polish law, it is difficult to say whether the attitude towards the FFD should be liberalized. However, it seems that a possible increase in the number of cases where the FFD would be analyzed does not have to mean that the FFD would be justified in every case. It is also difficult to accept the situation in which we depart from fundamental rules governing the process of choosing potential purchasers because of the crisis. We should try to investigate every case in order to see whether the lack of potential purchasers is objectively justified or whether there are other factors which may come into play. One should remember that the crisis is a part of the market economy and the fact that it has started means that one day it will probably finish, whereas, giving its consent to concentration or accepting a purchaser who raises serious doubts will be permanent and will prevail even after the crisis finishes.

- Mergers between Financial Institutions.

12. The issue of the FFD has not been raised in any concentrations between financial institutions supervised by Polish antimonopoly authority. It is also worth mentioning that in the period of the economic

crisis, Polish government has not undertaken any actions aiming at saving inefficient financial institutions. From the point of view of Polish antimonopoly authority, we do not consider it necessary to undertake such actions or to change merger assessment rules for the needs of financial institutions.

- Interplay with other policy instruments.

13. According to the Polish antimonopoly authority, one should very carefully approach the possibility of employing the FFD in the assessment of agreements concluded between different entrepreneurs. The crisis may create incentive and sometimes an excuse to undertake various anti-competition initiatives, for instance in the form of crisis cartels.

14. However, it is difficult to find any justification for the practice of applying the FFD concept to analyses concerning state aid. The state aid law elaborated, in a comprehensive way, the methodology of the assessment of companies which are in a difficult financial situation or companies which are in bankruptcy. Balance test for the assessment of new state aid projects, introduced by the Commission, constitutes a new comprehensive instrument for the economic assessment of state aid. This test also creates the possibility of assessing the financial situation of potential beneficiaries of state aid projects and of creating adequate state aid funds.