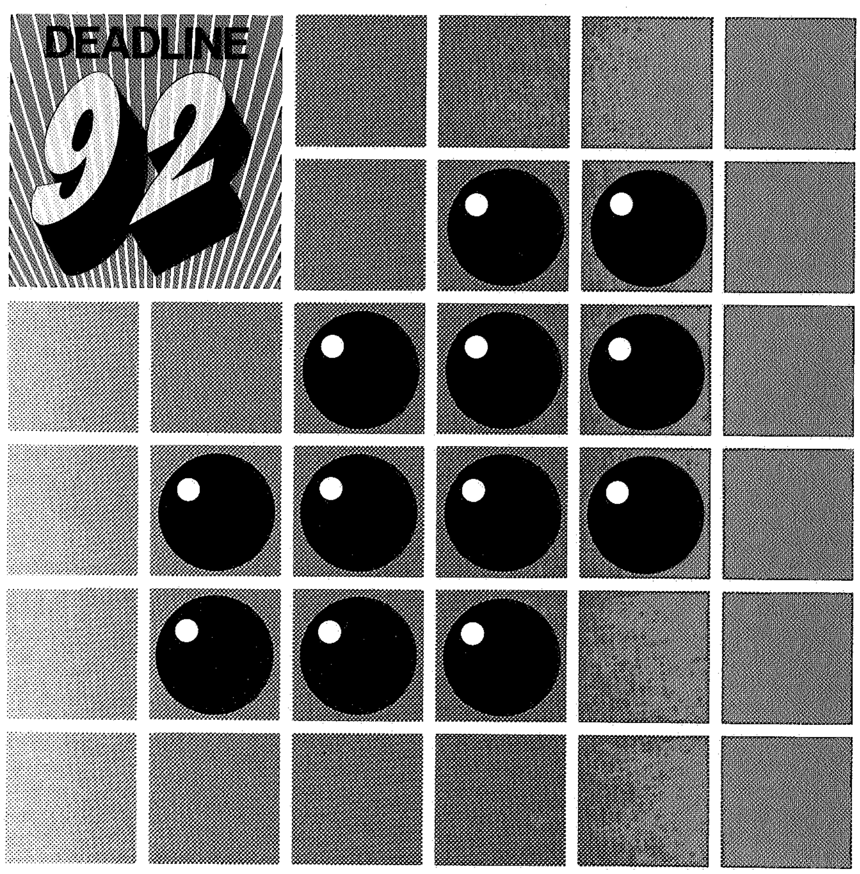
Periodical 1/1989

EEC COMPETITION POLICY IN THE SINGLE MARKET



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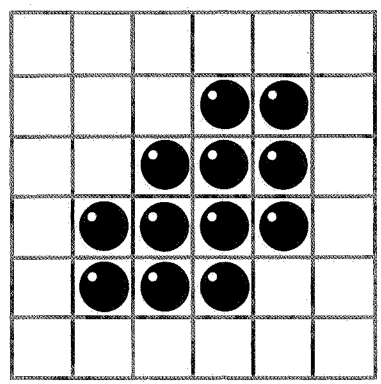
Maintenance of undistorted competition is one of the fundamental principles of the free-market economy on which the European Community is based.



The competition rules which have been established in this context are aimed at ensuring that a healthy competitive environment exists throughout a unified European market, for the benefit of all — producers, traders, consumers and the economy in general.

With the creation of a unified internal market among the 12 Member States of the European Community by 1992, there is even greater need for an effective policy to ensure fair competition throughout the Community.

This brochure explains the objectives and rules of European competition policy, and it shows how they work. It not only applies to big companies which are already preparing for an enlarged European market: it is as relevant to small and medium-sized enterprises, showing how they may benefit from cooperation with other firms and take full advantage of a unified European market.

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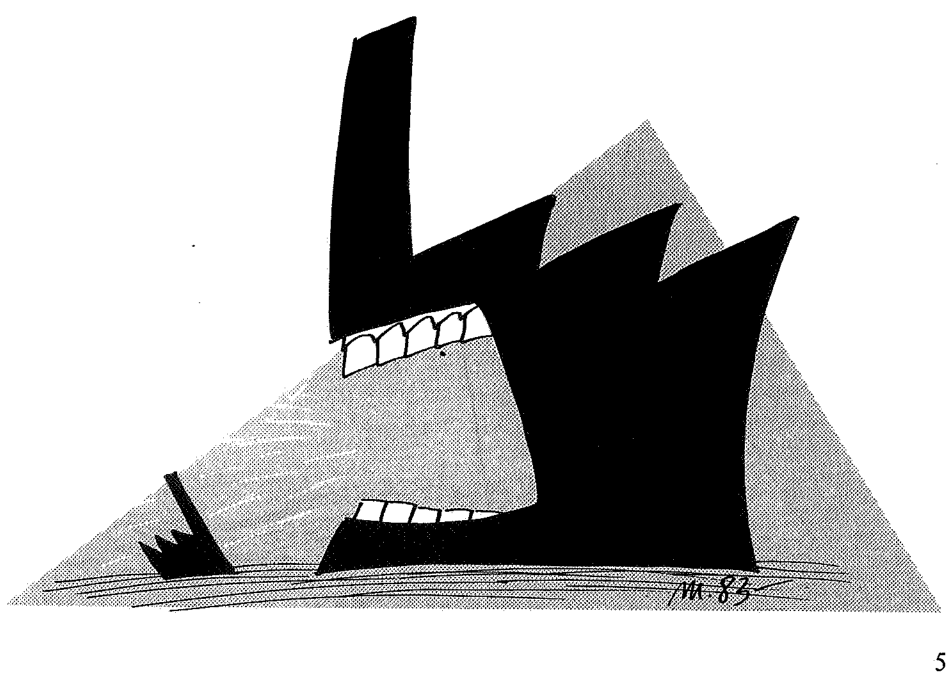
Introduction

The purpose of the European Community is to lay the foundations of an ever-closer union among the peoples of Europe and to ensure economic and social progress in its member countries by common action aimed at eliminating the barriers which divide Europe. Over the years, the Community has progressively dismantled many obstructions to trade including customs duties, quotas, and charges or measures which have an equivalent effect. It has been recognized, however, that genuine economic integration requires more extensive action in a number of fields. In accepting the Commission's proposals for completing the internal market the European Council pledged the Community in 1985 to a strategy which would lead to the realization of this objective.

If one considers the historical, cultural and economic diversity of the Member States, the idea of creating a common market is clearly an ambitious undertaking. Enlargement has provided the Community with further challenges. From a group of six countries with

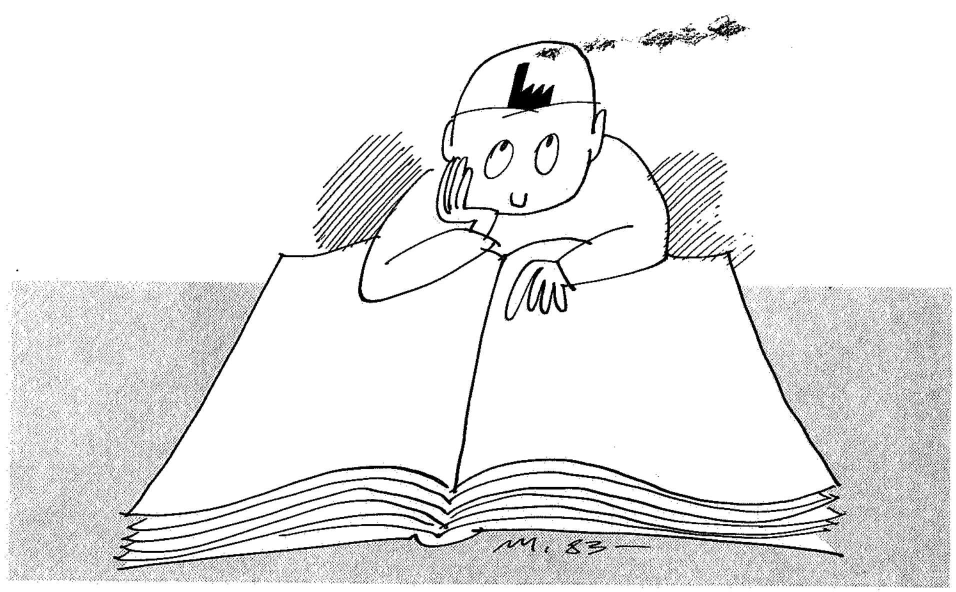


a relatively homogeneous economic structure, the Community now has 12 members, some 320 million inhabitants and an economy which shows marked regional disparities. All the Communities' efforts are now being applied to strengthening the cohesion of this unit and to removing the remaining obstacles which stand in the way of the Community's development.

Community businesses are also increasingly recognizing that a strengthening of the European dimension is indispensable in order to maximize commercial opportunities. There is a growing awareness that the creation of the single market can help to provide stability to European industry by placing it on a more equal economic footing with its major world competitors.

An efficient competition policy has a key role to play since it leads to the optimal allocation of resources and helps to create the best possible climate for fostering innovation and technical progress in the unified market. The Cecchini Report recognizes that the expected benefits of the single market, including increased productivity, lower prices and greater employment opportunities, will not be realized unless free and fair competition is fully maintained in the post-1992 Community.

The policy must ensure that new protectionist barriers are not erected, whether as a result of restrictive business practices or through measures by Member States in favour of national enterprises.



The existing Community rules for dealing with restrictive agreements, concerted practices and abuses of a dominant position are already making an important contribution to the integration process, to the extent that they prevent market partitioning cartels, restrictive vertical agreements and abuses of monopoly power. These rules will continue to have an essential function in creating and consolidating the single market. The Commission is also seeking the adoption of a Community system of merger control, in order to put in place the more complete legal framework which is necessary, if the benefits of the integrated market are to be maximized.

In the context of 1992 the control of State aids also has considerable significance. Government assistance to enterprises could be used as a protectionist tool, thus undermining the wider strategy, which rests on the philosophy that the single market must be free and competitive. The consistent application of the Community's State aid rules is therefore an essential element in the creation and maintenance of a unified market.

As the pace towards the realization of the single market accelerates, the significance of competition policy increases. This brochure has been prepared by the Commission in recognition of this, and it sets out, for the benefit of companies and individuals who will be operating in the single market, the essential provisions of the Community competition rules, in so far as they affect undertakings.

I — What is the EEC?

Definition and aims of the EEC

The European Economic Community (EEC) was established in 1957 by France, Italy, the Federal Republic of Germany, Belgium, Luxembourg and the Netherlands, for the purpose of creating a union of European States, bound together by common economic goals. In 1973, Denmark, Ireland and the United Kingdom joined and since 1981 Greece has been a member. The entry of Spain and Portugal in 1986 brought the total membership to 12.

By creating a single 'common market' the Member States strive together to achieve the harmonious development of economic activities, continuous economic expansion and a faster rise in the standard of living. With these goals in mind, the activities of the EEC include:

(a) the elimination of customs duties between the Member States;
(b) the creation of a common commercial policy towards third countries;
(c) the creation of common policies in a number of specific sectors, such as agriculture and transportation;
(d) the removal of obstacles to the free movement of persons, services and capital throughout the Community;
(e) the creation of common funds to promote social and regional development;
(f) the approximation, or 'harmonization' as it is often referred to, of national laws;
(g) the establishment of a system which ensures that competition is not distorted.

Many of the most important barriers affecting trade between the Member States have already been removed, and the Community's programme for the completion of the single European market by 1992 is aimed at eliminating those which remain. Thus, undertakings in the Community are increasingly able to reap the benefits of operating in a large unified market of 320 million consumers.

Next to this general economic community which exists between the Member States a common market has also been established in the coal and steel sector (ECSC, the European Coal and Steel Community) and in the field of nuclear energy (Euratom, the European Atomic Energy Community). Together, the three Communities are commonly referred to as the European Community (EC).

The institutions

The responsibility for achieving the aims of the European Community lies with four institutions:

(i) The European Parliament, which has 518 members, is elected directly by the citizens of the Member States. The parliamentarians are not organized in national sections, but in Community-level political groups. The Parliament must be consulted on the more important Commission proposals to the Council and has far-reaching powers in the budgetary field, among others the power to reject the Community budget as a whole. Also, the Parliament can compel the Commission to resign as a body by passing a motion of censure.

(ii) The Court of Justice, composed of 13 judges, assisted by six Advocates-General, ensures that implementation of the Treaties is in accordance with the rule of law. It plays an essential role in the interpretation of European law, frequently at the request of national courts. The Court also deals with disputes on Community matters between Member States, between Member States and the Community institutions, or between the latter and individuals, including firms.

In the field of competition policy, the Court has issued important decisions which give valuable guidance to undertakings as to the meaning of the competition rules.

(iii) The Council consists of representatives of the governments of the 12 Member States. Although the 'main' representative for each is its Foreign Minister, membership of the Council varies with the subjects down for discussion. Meetings are thus often attended by the Ministers for Agriculture, Transport, etc.

Under the EEC and Euratom Treaties, any measure of general application or of a certain level of importance must be enacted by the Council, which can, however, only in rare cases proceed without a proposal from the Commission.

(iv) The Commission is a collegiate body consisting of 17 Members, appointed by agreement between the member governments. Throughout their four-year term of office, Members must remain independent of the governments and of the Council. The Commission has a wide range of duties:

(a) it is the guardian of the Treaties;
(b) it is the executive arm of the Communities;
(c) it is the initiator of Community policy and exponent of the Community interest in the Council.

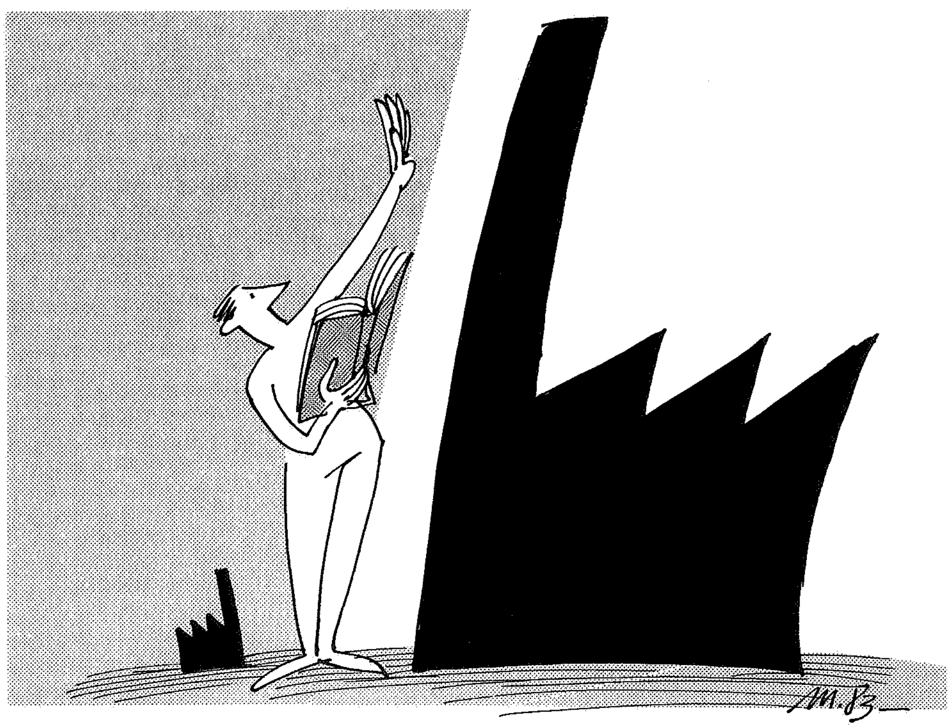
Other Community organs include the Economic and Social Committee, the European Investment Bank and the Court of Auditors.

Legislation in the EEC

The EEC Treaty mentions four instruments which the competent Community institutions can use to establish law or policy:

(i) regulations, which are laws directly applicable and binding in the Member States;

(ii) directives, which are addressed to Member States and which lay down the results to be achieved, but leave the Member States free to choose form and methods;



(iii) decisions, which are binding on those to whom they are addressed, whether a Member State, a legal entity or a private person. In the competition field, decisions issued by the Commission can have a far-reaching impact on the behaviour of undertakings;

(iv) recommendations and opinions, which have no binding force.

This list of Community acts is not exhaustive: use is also made, for example, of communications, memoranda, guidelines and general programmes.

In the competition area, the Commission has issued several notices which, although not binding, can none the less be useful for undertakings as general guidance.

Community law is a factor which all those operating in the common market must be aware of and take into account. Not only do the EEC rules — including the rules of competition — apply, often directly, in all the Member States but, in cases of conflict with national laws, Community law prevails.

II — The EEC competition rules which apply to undertakings

The creation of a single European market requires, among other things, the elimination of economic barriers such as customs duties, quantitative restrictions, and other charges and measures having an equivalent effect, which exist between the Member States. Accordingly, where national legislation impedes, for example, the free movement of goods across Member State frontiers, it is the national authorities who will come under attack for violating the Treaty.

Private arrangements, however, may also interfere with cross-border trade by creating divisions within the European market. For instance, companies may agree to keep out of each others' national markets and in such cases, it is the companies themselves who may face legal action under the competition rules.

The EEC Treaty provides for the establishment of a system to ensure that competition in the common market is not distorted. The objective of market integration is as important as the traditional role which competition plays in free market economies, ensuring efficient allocation of resources, stimulating enterprises to make the best use of their know-how and skills and encouraging them to develop new research techniques and products.

The rules of competition are contained in Articles 85 to 94 of the EEC Treaty.

Articles 85 and 86 relate to anti-competitive behaviour by enterprises which has an effect on trade between Member States. These are the rules which undertakings must be aware of and must comply with in all their commercial dealings.

Both Articles are aimed at preserving and enhancing competition rules by different means. Article 85 is directed at agreements or concerted practices between two or more enterprises, whereas Article 86 is aimed at abusive behaviour by monopolies or firms with very considerable power.

Competition can, of course, also be distorted when national governments favour certain undertakings, by granting them aids in whatever form, such as outright grants or special tax advantages. This aspect of competition policy, which is dealt with in Articles 92 to 94 of the Treaty, is of indirect importance to enterprises in the sense that if the Commission finds a certain State aid to be illegal, it will intervene against the national government concerned and not against the company to whom the aid is given. However, in view of the fact that companies might be obliged to reimburse any aids illegally received, it is obviously also of direct relevance for them. A brief outline of the rules in this area is given in Chapter V.

Note: The ECSC Treaty imposes special competition rules on undertakings operating in the coal or steel industry.

Article 85

Basic principle — the prohibition of Article 85 (1)

Article 85 of the Treaty relates to anti-competitive behaviour by two or more undertakings or decisions by their associations and it prohibits agreements or other practices which distort competition and which are liable to affect trade between Member States. Examples of such prohibited activities are price fixing between competitors, agreements on market shares or production quotas, or tie-in clauses. The acquisition of shares in competing companies, and other agreements leading to economic concentrations may also fall within the scope of Article 85 (1). The prohibition of Article 85 applies both to so-called horizontal agreements, meaning agreements between undertakings at the same level of commercial activity (competitors), and to vertical agreements, such as agreements between manufacturers and the distributors of their goods.

The following checklist can be used in considering whether a particular commercial activity will be caught by the prohibition of Article 85 (1):

(i) there must be an agreement (in writing or oral), or a decision by an association of undertakings (for example a trade association) or a so-called concerted practice, which covers positive action falling short of an actual agreement, to align undertakings' activities (hereinafter, the term 'agreement' will be used to cover all three types of activities);

(ii) there must be more than one undertaking involved; the term 'undertaking' must be viewed in the broadest sense, covering any entity engaged in economic or commercial activities such as production, distribution or the supply of services and ranging from small shops run by one individual to large industrial companies;

(iii) there must be a noticeable restraint upon competition involved; this applies not only where the actual object but also where the effect is such a restraint;

(iv) the agreement must have a perceptible effect, actual or potential, on trade between Member States. Agreements which have no effect on trade at all, for example agreements relating to warning labels on dangerous products, and agreements which have an impact only on internal trade within one Member State or on trade outside the EC will not be caught. It should be emphasized that the fact that all parties to an agreement are located in one Member State, and operate only on that market, does not necessarily mean that there is no effect on inter-State trade. If the effects of the agreement are not entirely confined to that Member State — for example, by having an impact on exporters in other Member States — there *is* an effect on trade.

Activities outside the scope of Article 85 (1)

The administrative practice of the Commission provides for a procedure enabling parties to an agreement to seek a declaration from the Commission that their activities do not come within the scope of the competition rules and are therefore 'safe'.

Such 'negative clearances', as these declarations are called, can be given in individual cases, provided the parties have notified their agreement to the Commission; this procedure is dealt with in Chapter IV.

Furthermore, a number of 'block' negative clearances exist for certain activities which, because of either the size of the undertakings involved, the relationship between those undertakings or the nature of the activity, are not deemed to be an infringement of the competition rules. For certain of these activities, the Commission has issued notices to provide guidance to business people as to what course of action they may pursue without falling out of the competition rules.

When doubt remains as to whether an agreement falls within one of the following categories, parties can of course apply for individual negative clearance.

Agreements of minor importance (the de minimis *rule)*

Small and medium-sized firms should be aware of the fact that many of the agreements they conclude will not be considered as violating the competition rules because the economic effect involved is not significant enough. This can be measured by market share and turnover.

As a guideline, the Commission has issued a notice (Notice concerning agreements, decisions and concerted practices of minor importance which do not fall under Article 85 (1) of the Treaty establishing the EEC) indicating that normally agreements will not be caught by Article 85 (1) if two conditions are met:

(i) market share: the goods or services which are the subject of the agreement and other goods or services of the participating undertakings, considered by consumers to be similar by reason of their characteristics, price or use, must not represent more than 5% of the total market in the area of the Community where the agreement has effect;

(ii) turnover: the aggregate annual turnover of the participating undertakings must not exceed ECU 200 million.

Such so-called *de minimis* agreements are normally safe, even though they involve certain restrictions. A caveat must be added: the criteria indicated by the Commission are by way of guidance only.

Relations between undertakings to which the competition rules do not apply

Commercial agents

In interpreting the EEC competition rules, the Commission stated in a notice issued in 1962 (Notice on exclusive dealing contracts with commercial agents) that a contract made with a commercial agent transacting business on behalf of a principal did not fall under Article 85 (1). A trader would only be considered to be a commercial agent, however, if he did not bear any responsibility for the financial risks involved in the business transactions (except for the normal *del credere* guarantee, by which the agent undertakes to indemnify the principal against failures to pay by customers) and was in fact, no more than a mere intermediary of the principal. Where a distributor maintains a considerable stock of the goods in question as his own property, where he provides at his own expense substantial free customer services, or where he determines the prices at which he sells or other terms of business, he will be deemed to be an independent trader, in which case, Article 85 must be taken into account.

Since 1962, legal developments have suggested a limiting of this approach. The Court and the Commission have indicated that, in deciding whether a genuine agency relationship exists, they would consider the economic reality as more important than the legal form.

The decisive question is whether the agent is, or is not, economically integrated with the principal. This is at least questionable where the agent is a very large firm and the principal a small one, or where the agent is transacting business on behalf of several competing principals.

Networks of agency contracts should be considered differently from individual contracts.

The Commission is currently preparing an updated notice in this area.

Parent companies/subsidiaries

Article 85(1) can only apply where the competition which exists between undertakings is capable of being restricted. Agreements between parent companies and their subsidiaries, or between subsidiaries amongst themselves — in other words, undertakings, forming one economic unit — will not be caught by Article 85(1), where:

(i) the subsidiary does not have any real freedom to determine its course of action on the market; one criterion here is how large the parent company's shareholding is;

(ii) the agreement relates merely to the allocation of tasks within the concern.

Activities which by their nature are not anti-competitive

The Commission has stated, again by way of notices, that certain forms of cooperation between undertakings and certain types of subcontracting agreements do not pose any problem under the competition rules. The size of the undertakings involved is generally not relevant in this context.

Cooperation agreements

In its 'Notice concerning agreements, decisions and concerted practices in the field of cooperation between enterprises', the Commission indicates that 18 types of agreement are deemed not to restrict competition where their object is one of the following forms of cooperation:

(a) an exchange of opinion or experience;

(b) joint comparative studies of enterprises or industries;

(c) joint preparation of statistics and calculation models;

(d) joint market research;

(e) cooperation in accounting matters;

(f) joint provision of credit guarantees;

(g) joint debt-collecting association;

(h) joint business or tax consultant agencies;

(i) joint implementation of research and development contracts;

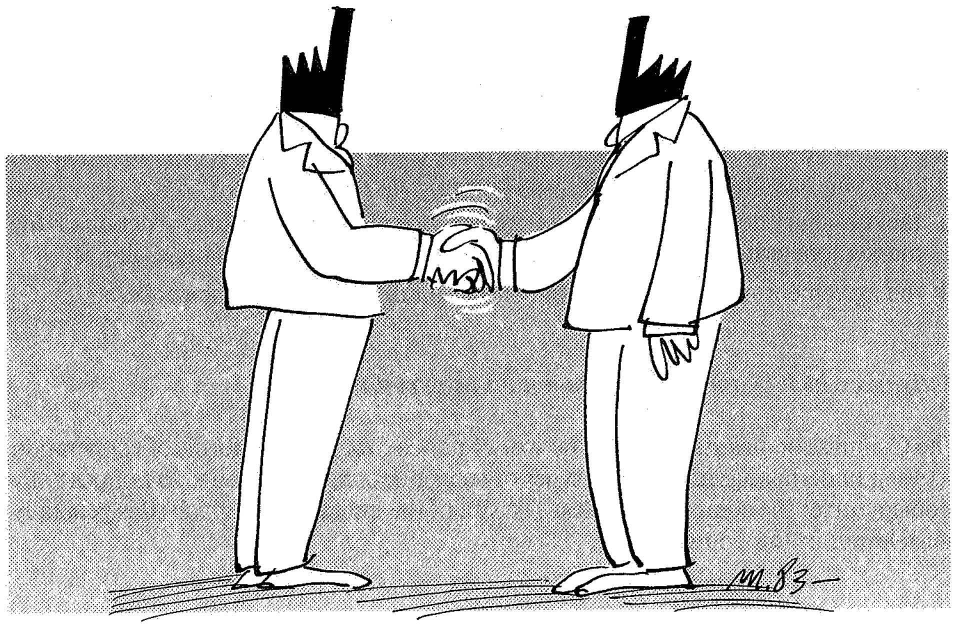
(j) joint implementation of research and development projects;

(k) joint placing of research and development contracts;

(l) sharing out of research and development projects, among participating enterprises;

(m) joint use of production, storage and transport equipment;

(n) joint execution of orders (but only when the participants do not compete with each other as regards the work to be done);



(o) joint selling arrangements by non-competing firms;

(p) joint after-sales and repairs services when the participants are non-competing firms, or, even if they are competitors, when these services are provided by an undertaking independent of them;

(q) joint advertising (but no restriction is allowed on the participants also to advertise independently);

(r) joint quality marks (but only where the label is available to all competitors on the same conditions).

Subcontracting

A subcontracting agreement is a form of work distribution whereby one firm — the subcontractor — supplies goods, work or services for another firm — the contractor — in accordance with the latter's specifications. This distinguishes it from an ordinary sale of goods or supply of services.

The provision of the contractor's technology or equipment to the subcontractor may justify the obligation to supply solely to the contractor, the items manufactured or the work done with the help of the technology or equipment. This is the case, not only when the technology or equipment is protected by the contractor's industrial property rights or rights over secret know-how, but also when it can be used to manufacture a distinctive product or to supply a service which is not available from other undertakings in the same industry. Otherwise, the subcontractor must remain free to meet orders from other customers.

Exemptions — Article 85 (3)

The general rule is that restrictive practices which affect inter-State trade are not allowed, and undertakings engaged in such activities will be ordered to stop doing so as well as running the risk of being fined by the Commission. However, there is an important exception to this general rule. The prohibition of Article 85 can be declared inapplicable by the Commission (and not by national courts) if the harmful effects of a restrictive agreement or practice are sufficiently counterbalanced by a number of beneficial elements. Article 85 (3) lists four conditions which must all be met before such a so-called exemption can be granted by the Commission:

(i) the agreement must contribute to an improvement in production or distribution, or economic progress. In other words, there must be clear objective advantages involved, such as a reduction of costs or an increase of production capacity;

(ii) a fair share of the resulting benefits must be allowed to consumers (and this includes not only ultimate consumers but also trade purchasers), for example, in the form of lower prices or an improvement in the quality of the goods or services concerned;

(iii) only restrictions of competition which are indispensable in order to achieve the beneficial results will be allowed;

(iv) competition in respect of a substantial part of the goods or services in question.

Where an agreement meets these four requirements, an exemption can be granted, either on an individual basis or by way of a group exemption.

(a) For the Commission to be able to grant an exemption in an individual case, the parties must normally first have notified their agreement, to the Commission, on a special form. Chapter IV deals with this procedure in greater detail. One important consequence of notification should be noted. As a general rule, no fines may be imposed for the period from the moment of notification until the Commission reaches a decision;

(b) agreements need not be notified and will none the less benefit from exemption if they fulfil the requirements contained in so-called group-exemption regulations which exist with respect to certain categories of agreements. At present, group exemptions are in force with respect to the following types of agreements:

- specialization agreements,
- exclusive distribution agreements,
- exclusive purchasing agreements,
- patent licensing agreements,
- research and development agreements,
- distribution agreements in the automobile sector,

- franchising agreements,
- know-how licensing agreements.

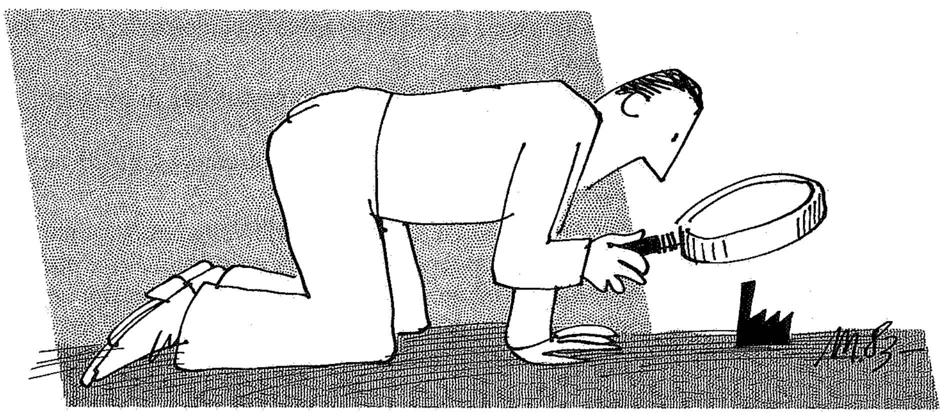
These group exemptions are dealt with in more detail in Chapter III.

Consequences — Article 85 (2)

If an agreement falls within the prohibition of Article 85(1), the following consequences apply.

(i) It is null and void from the outset. An agreement can be declared void, and thus unenforceable, by a national court, if the parties are involved in a lawsuit about the agreement. The Commission can also order parties to put an end to such a prohibited agreement.

(ii) The Commission has the power to order the parties to terminate the illegal conduct and it may impose fines of up to ECU 1 million,[1] or a larger sum up to 10% of the annual turnover of the undertakings concerned. Fines are paid to the Commission, not to any parties injured by the anti-competitive behaviour. The latter, however, may seek damages in national courts.



Article 86

Article 85 relates to restrictive practices between undertakings. As long as there is an appreciable restraint upon competition and an effect on inter-State trade, such agreements are prohibited, regardless of the size of the undertakings concerned.

[1] The ecu (European currency unit) was equal, on 30 June 1988, to BFR/LFR 43.48 (convertible) or 47.74 (financial), DKR 7.89, DM 2.08, DR 166.20, FF 7.00, HFL 2.34, IRL 0.77, LIT 1 539.79, UKL 0.67.

Article 86 is directed at a different problem, namely the behaviour of undertakings which are in a dominant position. Having a dominant position is not in itself prohibited.

The elements necessary for application of Article 86 are:

(a) The undertaking must be in a dominant position. Although market share is the major element in assessing dominance (as a rule a share below 40% precludes a finding that the undertaking is dominant), it is by no means the only factor. An undertaking can be deemed to be dominant if, because of various factors, such as ready access to raw materials or capital, it has the power to act independently, without having seriously to take into account its competitors, purchasers or suppliers.

(b) The dominant position must be in the common market or a substantial part of it. Whether a particular geographical area — for example a portion of a Member State — can be deemed to be a 'substantial part' depends on a number of factors, including the nature of the product market involved. In one case, the southern part of Germany was held to be 'substantial' in this context; in another case, Belgium.

(c) There must be an abuse of the dominant position, in the sense that advantage is taken of the dominant position which causes injury to third parties. Examples are:

   (i) charging unfair purchase or selling prices. Prices which are unfairly high will be to the detriment of consumers, while those which are unfairly low (below cost) may be aimed at eliminating weaker competitors, who do not have the power to match such prices for any length of time;

   (ii) discriminatory prices, e.g. charging customer A more than customer B for exactly the same transaction, thereby placing customer A at a competitive disadvantage;

   (iii) refusal to sell to a customer without valid, objective reasons;

   (iv) attempts to hold on to customers, for example by granting fidelity rebates;

   (v) acquisitions of competing undertakings, thereby affecting the competitive structure within the common market.

It should be noted that economic concentrations brought about by merger or acquisition may fall within the scope of Article 86 where the acquiring company already occupies a dominant position in the relevant market.

Merger trends in the Community, 1984-88

The following chart highlights the recent growth in the number of mergers and acquisitions of majority holdings within the Community (including international operations between Community and non-Community enterprises)[1]

	Total mergers and acquisitions of majority holdings involving at least one of the 1 000 largest firms in the Community			Mergers and acquisitions of majority holdings where the combined turnover of the firms involved exceeded ECU 1 000 million		
Sector[2] / Year	1985-86	1986-87	1987-88	1985-86	1986-87	1987-88
1. Food	34	52	51	17	35	40
2. Chem.	57	71	85	33	51	57
3. Elec.	13	41	36	9	12	23
4. Mech.	29	31	38	17	20	26
5. Comp.	1	2	3	0	1	3
6. Meta.	17	19	40	4	11	32
7. Trans.	10	21	15	3	11	14
8. Pap.	27	25	34	5	8	18
9. Extra.	10	9	12	7	4	9
10. Text.	9	6	14	2	2	4
11. Cons.	14	19	33	8	11	29
12. Other	6	7	22	3	5	13
Total	227	303	383	108	171	268

1 *Source:* Data gathered by the Commission in the specialist press.

2 *Key*

Food: Food and drink
Chem.: Chemicals, fibres, glass, ceramic wares, rubber
Elec.: Electrical and electronic engineering, office machinery
Mech.: Mechanical and instrument engineering, machine tools
Comp.: Computers and data-processing equipment (in 1983/84, included under mechanical engineering)
Meta.: Production and preliminary processing of metals, metallic goods
Trans.: Vehicles and transport equipment
Pap.: Wood, furniture and paper
Extra.: Extractive industries
Text.: Textiles, clothing, leather and footwear
Cons.: Construction
Other: Other manufacturing industry

III — How the competition rules affect agreements and other business dealings of undertakings

Introduction

In the previous chapter, a general description was given of the meaning of Article 85(1) of the EEC Treaty with regard to restrictive agreements, concerted practices or decisions of associations of undertakings.

Having thus established the principles involved in the application of this Article, we now turn to its relevance with regard to specific types of agreements.

Article 85 itself lists, by way of example, several types of agreements which may prevent, restrict or distort competition.

For the sake of clarity, we will make a distinction between *horizontal agreements* (agreements between competitors or potential competitors) and *vertical agreements* (agreements between undertakings in different stages of the process through which a product or service passes from the manufacturer to the final consumer).

The *de minimis* rule

As indicated in Chapter II, agreements which, because of the market share and the turnover of the undertakings involved are deemed to have a negligible effect on competition and inter-State trade pose no problems under the competition rules.

This so-called *de minimis* rule applies to agreements between companies which meet the criteria as to market share and turnover, laid down in the Notice concerning agreements of minor importance. Whatever the nature of the agreement in question, if the two criteria are applicable, the undertakings concerned normally need not worry about the possible applicability of Article 85(1) and can therefore refrain from notifying the Commission.

In borderline cases, of course, undertakings are well-advised to consider whether their agreement falls under any of the headings indicated below.

Horizontal agreements

Horizontal agreements which pose no problems under the competition rules

When undertakings have established that a particular agreement does not satisfy the *de minimis* rule, the next step is to check whether the agreement is one which by its nature is not deemed to pose a problem under Article 85(1).

For this purpose, the Notices on, respectively, cooperation agreements and subcontracting agreements offer guidance. These are dealt with in Chapter II.

Horizontal agreements which benefit from a group exemption

Specialization (Commission Regulation 417/85)

Specialization agreements are one of the forms of horizontal agreement now exempted as a group under Article 85(3). This means that although Article 85(1) is normally applicable (again, the *de minimis* rule must first be considered), agreements which fall under the criteria of the group exemption issued by the Commission are deemed to meet the requirements of exemption under Article 85(3) without the need of prior notification.

For the purpose of the group exemption, specialization agreements are agreements by which parties undertake a reciprocal obligation:

(i) not to manufacture certain products or to have them manufactured, but to leave it to other parties to manufacture the products or have them manufactured; or

(ii) to manufacture certain products or to have them only manufactured jointly.

By giving up the manufacture of certain products, the participating undertakings can each concentrate — or, in other words, 'specialize in' — the manufacture of those products remaining in their respective production lines. Competition is restricted because the parties give up the possibility of independently manufacturing certain items.

The group exemption was created in order to allow small and medium-sized firms to improve their production processes and thereby strengthen their competitive position *vis-à-vis* larger firms.

In order to fall under the group exemption, specialization agreements must fulfil the following conditions.

(1) The agreement must be between small and medium-sized undertakings, measured on the basis of market share and turnover, in this case:

(a) the market share with respect to the specialized products may not exceed in a substantial part of the common market, 20% of the market for all such products;

(b) the total annual turnover of the participating undertakings must not exceed ECU 500 million. If the turnover exceeds this limit, the parties can still benefit from the group exemption but they must notify their agreement to the Commission.

The group exemption is basically aimed at individual small and medium-sized firms: if a small firm is in fact part of a larger concern, the market share and turnover of the whole concern must be taken into account, with the result that the thresholds would probably be exceeded and the exemption thus inapplicable.

(2) The commitment to specialize must be reciprocal, which means that an obligation on only one of the parties to refrain from production of a certain item would not qualify for group exemption.

(3) The commitment must refer only to the nature of the products, so that any quantitative limitation of production does not fall within the group exemption.

(4) Certain additional clauses may be agreed which are essential to implement the commitment to specialize:

(a) a non-competition clause;

(b) exclusive purchasing and distribution commitments with respect to the specialized products, in order to enable the participants to continue dealing in the whole range of products;

(c) obligations concerning minimum stocks, replacement parts, and customers and after-sales services.

(5) Commitments with regard to prices are not allowed in the context of the group exemption.

Research and development (Commission Regulation No 418/85)

The Commission has always shown a favourable attitude towards R&D cooperation, provided that competition is maintained by the existence of different independent poles of research.

The block exemption regulation on R&D agreements covers three types of agreements concerning:

(i) joint research and development of products or processes with joint exploitation of the results of that R&D;

(ii) joint research and development of products or processes without joint exploitation of the results (if, exceptionally, such 'pure' R&D agreements fall within Article 85(1));

(iii) joint exploitation of the results of prior R&D agreements between the same undertakings.

The notion of 'joint exploitation' includes joint manufacturing and joint licensing to third parties, but *not* joint distribution and selling.

Under the regulation, joint R&D must be carried out in the framework of a defined programme and joint exploitation is only allowed where the know-how resulting from the common R&D contributes substantially to technical or economic progress and constitutes a decisive element for the manufacturing of the new or improved products. Furthermore, the block exemption is only applicable:

(i) if all the parties have access to the results;

(ii) if, where there is no joint exploitation, each party is free to exploit independently the results and any pre-existing technical knowledge necessary therefor;

(iii) if, in the case of specialization in the manufacturing of the new or improved products, each party has the right to distribute those products.

In order to ensure the possibility of several independent poles of research in the Community and, in general, to maintain effective competition on the markets concerned, the block exemption sets out different conditions according to the competitive position of the parties:

(i) where at the time the agreement is entered into, any of the parties are competitors for products which may be improved or replaced by the results of R&D, the exemption applies only if their combined production of such products does not exceed 20% of the market;

(ii) where no two or more of the parties are competitors at the time the agreement is entered into, the exemption applies irrespective of market shares;

(iii) after five years of joint exploitation, the exemption continues to apply, whether the parties were initially competitors or not, *only* if their combined production for the new product does not exceed 20% of the market.

The regulation contains a detailed list of permitted restrictions and obligations, such as those aimed at reinforcing the cooperation between the parties in the field of R&D, and provisions relating to the field of use of the new technology or granting limited territorial protection to the parties. Also listed in detail are the provisions which may under no circumstances be included in agreements if the parties want to benefit from the block exemption (the 'black list'). An opposition procedure is included whereby agreements containing restrictions not expressly exempted or prohibited by the regulation can be notified to the Commission and will be deemed to be covered by the block exemption unless the Commission opposes exemption within six months.

Horizontal agreements which are not allowed

Assuming the *de minimis* rule, the Notices on cooperation and subcontracting and the specialization and R&D block exemptions are all not applicable in a particular case, (competing) undertakings must refrain from engaging in the following activities:

(a) Price fixing (other trading conditions). Prohibited are all agreements, directly or indirectly fixing buying and/or selling prices. The term 'indirectly' covers the situation where undertakings agree in general as to their pricing policies. Also prohibited are any agreements by which undertakings restrict themselves as to the trading conditions they apply in their business dealings, such as on what basis discounts are granted, credit terms, etc.

(b) Market or production sharing. Agreements between (potential) competitors to keep out of each others' markets or to allocate certain territories or sources of supply amongst themselves are prohibited. Arrangements to control production itself, such as limitations imposed by quotas, as well as long-term plans regarding production are normally not allowed.

(c) Agreements to discriminate. Agreements between undertakings to fix discriminatory terms in their dealings with third parties who are in competition with each other are not allowed. For example when A and B agree to apply more advantageous conditions to buyer C than to buyer D, for transactions which are the same, buyer D will be placed at a competitive disadvantage. It should be noted that this type of behaviour is only prohibited where there is an agreement between A and B to discriminate. In the absence of a dominant position, A, acting individually, is as a general rule free to apply the terms he wants in his various business dealings.

(d) Collective boycotts. Agreements between undertakings aimed at forcing a (potential) competitor out of the market or preventing market entry by others are not allowed.

(e) Tie-ins. Agreements are not allowed by which undertakings impose 'tying arrangements', for example, obliging a buyer of one product or service also to buy another product or service which is not connected to the first by nature of its commercial usage.

This list of prohibited agreements is not exhaustive, but illustrates the types of agreement which have restrictive effects on competition.

Horizontal agreements which may pose problems

Again, assuming the *de minimis* rule does not apply, certain agreements may possibly violate Article 85(1):

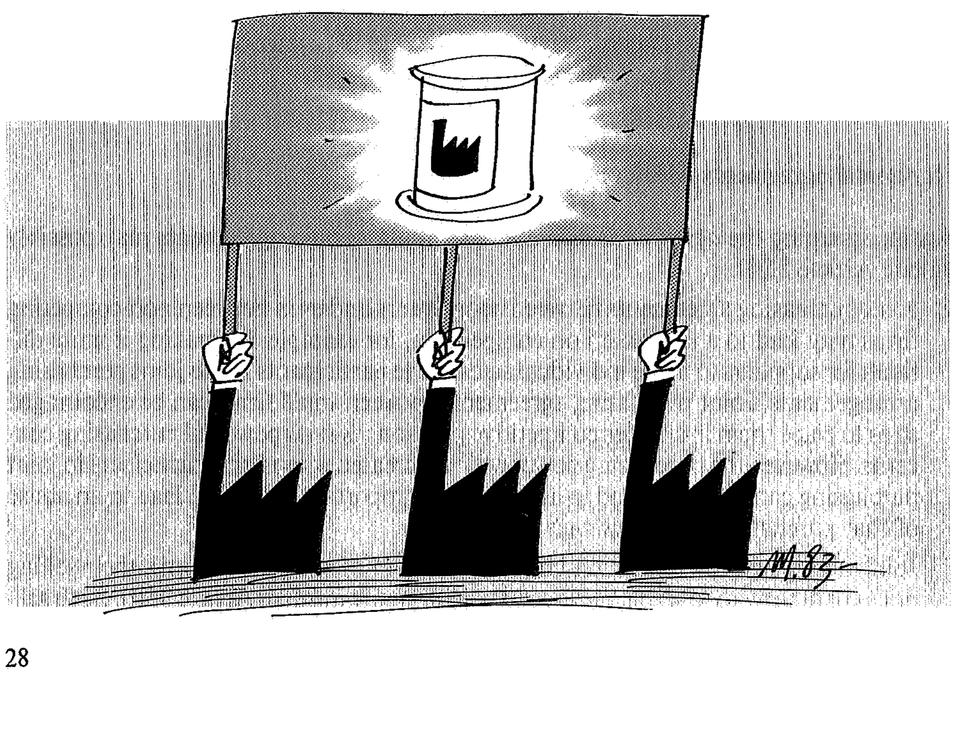
(i) Joint purchasing agreements between competitors and even between non-competing firms may lead to a restriction on competition, for example, by making it more difficult for suppliers to make individual sales to the participants in the joint purchasing arrangements. Joint purchasing agreements between small firms can be encouraged so as to place them in a better competitive position *vis-à-vis* powerful purchasing concerns. However, the purchasing power which is created when firms participate in joint purchasing cannot be allowed to assume such proportions as would lead to an abuse of that purchasing power *vis-à-vis* suppliers.

(ii) Joint selling agreements which limit the freedom of the parties to fix their selling prices or otherwise to sell as they see fit will normally infringe Article 85(1). Such selling arrangements can for example be organized in the context of a trade association or through jointly owned marketing subsidiaries.

Joint selling arrangements between non-competing firms (actual or potential) will normally not be held to violate Article 85(1), nor is it likely that joint selling to countries outside the EEC will be deemed to be an infringement provided trade between Member States is not affected.

(iii) Sales promotion. Three types of sales promotion may be relevant under the competition rules: trade fairs, joint advertising and the use of a common quality-control label.

- Trade associations which organize trade fairs may impose certain restrictions on the members as to their participation in trade fairs other than those organized by the association. These restrictions may be anti-competitive at two levels, in that they limit the possibilities of other organizers of trade fairs to acquire participants and furthermore limit the freedom of participating producers to promote their goods elsewhere. Certain restrictions may, however, be exemptable because of the advantages which result from an orderly organization of trade fairs.
- Joint advertising may be used to promote the products of a particular industry or a common brand. Such joint publicity normally poses no problems, as long as the participants remain free also to promote their products independently.
- The use of a common quality-control label or trademark in joint promotional activities is allowed when use of the label is open to all manufacturers whose products meet the relevant quality standards. If further restrictions are involved, such as an obligation on the participants not to manufacture other products not covered by the common label, the agreement may pose problems under Article 85(1).



(iv) Exchange of information. Undertakings may arrange to exchange information, for example, through a central agency, on quantities, prices, discounts and other terms of business, or on suppliers and customers. Such exchange of information can lead to an alignment of the participants' business conduct.

The legality of such information arrangements will depend on, in the first place, the type of information involved. Exchange of purely statistical information, for example on production and sales figures for a particular industry, without identifying the individual firms concerned, is not objectionable.

In general, information arrangements become dangerous from the competition point of view where they are likely to lead to collusion: Cooperation which jeopardizes the independent determination of business policies by the participants must be avoided.

(v) Trade associations/market foreclosure. Undertakings in a particular sector may validly pursue common interests by creating a trade association. Among the possible problems which must be considered in this context are:

- activities within the trade association which tend to deprive members of their freedom to determine their individual business policies;
- market foreclosure *vis-à-vis* potential competitors who want to enter a particular market, where all or nearly all of the undertakings in that sector are organized in such an association.

Both of these may give rise to problems under the competition rules.

(vi) Non-competition clauses in connection with the sale of an undertaking. When the ownership of an undertaking changes hands, the new owner (the purchaser) will normally want to be protected from competition by the previous owner (the seller), who may at least initially be in a stronger competitive position due to his knowledge of the market, etc.

Agreements relating to the sale of undertakings therefore often contain so-called non-competition clauses, obliging the seller to refrain from competing in the market in question.

Whether such a clause is a forbidden restriction of competition depends on a number of factors:

- if the sale involves merely the transfer of material assets, a non-competition clause is normally not necessary and therefore in violation of Article 85(1);
- if the sale involves the transfer of good-will and know-how, protection from competition by the seller will normally be acceptable under Article 85(1), under two conditions:
  (1) the duration of the clause must not exceed the period required for an active, competitive purchaser to build up his position to equal that of the previous owner's at the time of the transfer; the length of this period depends on the specific facts of each case;

(2) the scope of the clause may not be excessively wide; the obligation not to compete must be limited to the market in which the undertaking was active before its sale.

Vertical agreements

General

The horizontal agreements dealt with in the previous chapter involve situations in which competition is diminished due to arrangements by competitors restricting their independent business behaviour.

Vertical agreements relate to the passage of a product from the factory to the end-user. In the EC, such agreements are particularly relevant to the creation of one European market, in that distribution arrangements across Member State borders can promote market unification.

In this chapter, the problem of distribution will be dealt with in the context of Article 85(1); in other words only situations in which agreements have been concluded relating to distribution will be considered. For the application of Article 86 (abuse of a dominant position) no distinction need be made between horizontal and vertical activities; the same concepts apply regardless of whether a dominant firm abuses its position *vis-à-vis* its competitors (horizontal) or in the distribution of its products (vertical).

Whether or not vertical agreements come under Article 85(1) depends on the extent to which the parties, i.e. the supplier and his intermediary/distributor, agree to restrict their commercial freedom. The following concepts are relevant with respect to distribution agreements:

(i) 'simple' distribution agreements: where neither the supplier nor the distributor is bound to any restrictive obligations, such as exclusivity of purchase and/or supply, territorial restrictions, non-competition clauses, or minimum purchase requirements, the agreement will not fall within the scope of Article 85(1);

(ii) exclusive distribution agreements: the supplier agrees to supply only one distributor in a determined territory. Here, Article 85(1) is relevant: there is a restriction on competition in that the supplier is no longer free to supply other distributors or, in some cases, even end users directly, in that territory. In return for the exclusivity, the exclusive distributor may in turn accept certain restrictions, for example, he may also agree not to act as the distributor for the supplier's competitors;

(iii) exclusive purchasing agreements: the distributor agrees to purchase all of his requirements of a particular product only from one supplier. The distributor is thus restricted in his source of supply and other suppliers of the same type of goods have lost a sales outlet;

(iv) selective distribution: a supplier may wish to limit the sale of his products to only those sales outlets that meet certain standards. For example, in the case of highly technical products, the supplier may require that all dealers possess a minimum degree of technical knowledge.

In the following sections, the applicability of Article 85(1) and the possibilities of exemption are considered.

Distribution agreements which pose no problems under Article 85(1)

For application of Article 85(1), there must be an agreement between independent undertakings. Thus, the following cases do not fall under the prohibition:

(a) distribution by the manufacturer himself;

(b) distribution through a branch office in a given territory; although a position of exclusivity is present, the branch is seen as part of the manufacturer himself;

(c) likewise, true agency agreements, where the commercial agent is merely an auxiliary of the supplier, do not fall under Article 85(1) — see Chapter II; and

(d) where a local subsidiary company is entrusted with the distribution of the supplier's goods, Article 85(1) will not apply if that subsidiary has no autonomous commercial freedom (see Chapter II).

The *de minimis* rule (see Chapter II) also applies to vertical arrangements.

However, a caveat must be added: The underlying principle of the *de minimis* rule is, that for Article 85(1) to apply, the restriction on inter-State trade and of competition must be appreciable. If a supplier concludes only one distribution agreement with a particular distributor, there will normally be no problem if the criteria as to market share and turnover are fulfilled. However, if that supplier has set up a vast network of agreements with a large number of distributors, the whole effect of that network may be relevant, and not just the individual agreements between the supplier and each distributor.

Exclusive distribution agreements (Commission Regulation No 1983/83)

General

Although exclusive distribution agreements as described above have detrimental effects as far as competition is concerned, such agreements may at the same time be beneficial, not only in improving the efficiency of distribution but, in general, by contributing to market unification. For example, contacts with one (exclusive) distributor only in a particular area may make it easier for a supplier entering a new market to deal with linguistic and legal differences.

The underlying principle of the group exemption is that while certain restrictions will be allowed in the interest of improving distribution, those restrictions may not go too far, and must notably never result in absolute market insulation. In this context, the concept of parallel imports is very important. 'Parallel imports' exist where in addition to the 'official' route by which the goods are imported by the exclusive distributor into a given territory, there is also a second 'parallel' route, by which another trader in the territory imports the goods, which he has obtained from a third party outside the territory. In other words, that 'parallel importer' is a source of competition for the exclusive distributor. Any attempts to hinder such parallel imports render the group exemption inapplicable.

Specific provisions

The exemption may apply where (i) A (the supplier) agrees with B (the reseller or distributor, to supply only to B certain goods for resale within a defined area in the common market, or (ii) B (the reseller) agrees with A (the supplier) to purchase only from A certain goods for resale or (iii) A agrees to supply exclusively to B and at the same time B agrees to purchase exclusively from A.

The main conditions of the group exemption are:

(1) the agreement must involve two parties only. These need not necessarily be established within the common market;

(2) the products must be supplied for resale. Thus for example the exemption does not apply when the distributor uses the products to manufacture another end-product;

(3) the sales area must be either a defined part of the common market, or the entire territory of the common market;

(4) the only permitted restriction on the supplier is the obligation not to sell to other resellers in the sales area allocated to the exclusive distributor;

(5) the supplier may not be required to guarantee absolute territorial protection for the distributor, for example, by barring parallel imports into the sales area;

(6) the supplier may, however, agree not to make direct sales himself to customers within the distributor's territory;

(7) the distributor may agree to purchase all his requirements from the supplier. Aside from this, the following obligations on the distributor are also permitted under the group exemption:

   (a) not to manufacture or sell competing goods;

   (b) to concentrate his sales efforts in his sales territory; this means that he can be obliged to refrain from actively seeking customers elsewhere. He must, however, always remain free to sell outside his sales territory, even in areas allocated by the same supplier to other exclusive distributors;

(c) to purchase minimum quantities;

(d) to sell under the trademark, etc. indicated by the supplier;

(e) to carry out after-sales service.

No restrictions may be imposed on the distributor as to his prices and other terms of resale, such as the choice of his customers. Where these exist, the benefit of the group exemption is lost;

(8) the agreement must not involve competing manufacturers, since this could lead to (horizontal) market sharing. However, where one or both of the parties have a total annual turnover of less than ECU 100 million, non-reciprocal distribution agreements are allowed between competing manufacturers;

(9) there must be no effort by the parties to create absolute territorial protection for the distributor, including the improper use of a patent or trademark for that purpose. In other words, parallel imports of the contract goods must remain possible.

Agreements which satisfy these conditions are automatically exempted, without the need for the parties to notify the agreement to the Commission. The Commission does, however, retain the right to withdraw the benefit of the group exemption in certain cases, for example if the distributor is abusing the exemption by charging unreasonably high prices.

Agreements which contain restrictions going beyond the conditions of the group exemption can, of course, be notified to the Commission in order to obtain an individual exemption.

Exclusive purchasing agreements (Commission Regulation No 1984/83)

Agreements by which a reseller is obliged to buy his supplies exclusively from a stated manufacturer or other supplier (e.g. wholesaler), without, however, being allotted an exclusive sales territory, present different problems than exclusive distribution agreements. Where a supplier has succeeded in tying the most numerous or the largest sales outlets in a given area to himself, his competitors may find it very difficult to sell their goods in that area. The longer the duration of the exclusive purchasing obligation and the wider the range of products involved, the more serious is this barrier to market entry for competitors.

Also, such arrangements limit the commercial freedom of the resellers, who may often be smaller firms.

With these considerations in mind, the group exemption on exclusive purchasing, which parties must take into account for all exclusive purchasing agreements entering into force after 1 January 1984, provides that:

(i) the maximum duration of the exclusive purchasing obligation must be limited to five years (renewable);

(ii) the range of products covered by the obligation must be limited to products which either by their nature or by commercial usage are connected to each other.

Aside from these provisions as to the duration and the range of the obligation, the same provisions found in the group exemptions (both old and new) for exclusive distribution agreements apply.

Beer and petrol

Special provisions are included in the new group exemptions for exclusive purchasing agreements relating to beer (and other drinks) sold for consumption on the spot (in cafés, for example) and to petrol sold in service stations.

Normally, such agreements entail considerable financial involvement on the part of suppliers, which may thus justify binding the reseller for a longer period of time than in other sectors.

The following special provisions were therefore deemed appropriate for such beer supply or service-station agreements:

(1) the maximum duration of an exclusive tie for beer alone or for petrol is 10 years;

(2) in beer-supply agreements, if the obligation relates to beer *and* other drinks, the maximum duration is five years;

(3) for both beer-supply and service-station agreements, if the premises where the products are sold are subject to a tenancy agreement between the reseller and the supplier, the duration of the exclusive purchasing obligation can be as long as the duration of the tenancy (even if it is longer than 10 years);

(4) as to the range of products covered, for beer supply agreements, no other products may be included in the tie except other drinks (i.e. not crisps, fruit machines, etc.). For service-station agreements, the tie can relate only to petroleum-based motor vehicle fuels and, in some cases to lubricants to be used in a lubrication bay (i.e. not maps, car-accessories, etc.);

(5) special transitional rules apply to such agreements.

Those interested in detailed information on the rules governing beer supply and service-station agreements are advised to consult the relevant 'Guidelines' published in the *Official Journal of the European Communities.*

Selective distribution

Certain manufacturers may want their products to be sold only by qualified, 'approved' dealers. This is particularly true for technically sophisticated products such as electronic equipment, watches or automobiles.

In such cases, so-called selective distribution systems can be created in which only 'selected' dealers are authorized to distribute the goods concerned.

The selection of the dealers allowed into the system sometimes takes place on the basis of purely qualitative criteria which are entirely justified, given the nature of the product in question. For example, dealers may need a minimum amount of technical knowledge, or skilled personnel, or suitable premises in order to be able to sell the products in an appropriate way. If all dealers who fulfil these justified quality standards are allowed without discrimination into the system, there will be no objections as far as the EEC competition rules are concerned.

It also happens, however, that manufacturers go beyond applying purely qualitative criteria when appointing dealers. They may, for example, accept only dealers who are willing to carry out sales promotion for the manufacturer's products, or to stock his other products.

Dealers who are technically qualified to sell the products concerned but who are unwilling to accept these additional obligations, are thus excluded from the system; this is clearly a restriction.

Even more restrictive is a selection system in which the manufacturer applies quantitative criteria, for example, limiting the number of dealers in an area to the presumed purchasing power of the population there. In these cases, dealers who are qualified and moreover willing to accept additional obligations may nevertheless be excluded.

Aside from the need to have qualified dealers for certain products, all the above restrictions may seriously harm competition. Such closed distribution systems may be particularly damaging for potential dealers who may be excluded without any objective reasons. Also, the dealers who are a part of such a network may be seriously hampered in their commercial freedom, for example they may be obliged to sell only to other approved dealers.

These distribution systems can in any event not benefit from the group exemption for exclusive distribution agreements (see above), because the restrictions go beyond those allowed.

They may however be exempted on an individual basis if they manifestly improve distribution and fulfil all the other conditions for exemption under Article 85(3). It must in these circumstances be clear that the beneficial results cannot be achieved through other, less restrictive means.

Any indication that a selective distribution system is being used artificially to maintain prices, or to exclude in a discriminatory way certain types of retail outlets (for example, discount shops or supermarkets who are qualified to sell the products), or any attempts to hinder parallel imports through the system, will make exemption highly unlikely, and such distribution systems thus remain illegal. Action can then be called for by national courts or by the Commission.

Automobiles

Selective distribution systems are more common in certain sectors than in others, often depending on the nature of the products concerned.

One example is the motor vehicle sector, where manufacturers tend to set up distribution networks in which, at all stages, access is reserved only for selected dealers.

In view of the special circumstances in the motor trade, a number of restrictions of competition that appear in dealership and servicing agreements fulfil the conditions for exemption laid down by Article 85(3) of the Treaty. Distribution arrangements of a selective and exclusive nature are usually indispensable measures of rationalization in this sector. Also, motor vehicles are consumer durables that at both regular and irregular intervals require expert maintenance and repair, not always in the same place. The cooperation between the manufacturer or his importer and a number of selected dealers and repairers guarantees the provision of specialized servicing for the product. Finally, competition in the motor trade tends to focus on inter-brand competition between rival distribution networks. A certain degree of restriction of intra-brand competition between dealers and repairers in the same network and for the same goods can thus be tolerated.

A block exemption regulation (Commission Regulation No 123/85) exempts, in principle, the following types of restrictions on the motor dealer:

(i) not to sell the new vehicles of another manufacturer nor parts which do not match the quality of those supplied by the manufacturer to whom he is linked;

(ii) not actively to seek customers outside his allotted territory;

(iii) not to subcontract distribution or servicing and repairs to other dealers or repairers without the consent of the manufacturer or his importer;

(iv) not to sell new vehicles or replacement parts obtained from the manufacturer to dealers outside the distribution network.

Also exempted is a restriction on the manufacturer's freedom to appoint other dealers or to supply end-users direct in the allotted territory.

Certain conditions are attached to the exemption in order to safeguard effective competition and unrestricted freedom for consumers to buy new cars in the common market wherever prices and conditions are most favourable. The regulation, in particular, ensures that:

(a) consumers can have servicing or repairs done under the manufacturer's warranty anywhere in the common market;

(b) dealers are not made over-dependent on the manufacturer or importer; thus, the agreements must run for at least four years and specify at least one year's notice for termination;

(c) consumers can order new passenger cars with the specifications required at the place where they are to be registered from official dealers in other Member States who are willing to sell the vehicles to them, if the manufacturer or his importer sells the model concerned through the official distribution network at both places. This condition stops manufacturers or importers from trying to prevent or hinder sales of right-hand-drive versions of their cars on the Continent.

The Commission has always stressed that it has neither the desire nor the power to take interventionist measures to harmonize car prices across the common market. It cannot satisfy demands to abolish price differentials between Member States which are in fact partly a reflection of the particular play of supply and demand in the regions concerned. However, where price differentials are substantial, there may be reason to suspect that national measures or private restrictive measures are behind them and very large, long-lasting price-differentials between Member States can thus result in withdrawal of the benefit of the block exemption in individual cases.

Franchising

Franchising agreements have developed considerably in the Community during recent years as a new form of distribution. They consist essentially of licences of industrial or intellectual property rights (trademarks or names or know-how) to be exploited for the purpose of selling goods or providing services to end-users in premises of uniform appearance and with the same business methods.

Franchise agreements have generally a positive effect on competition. They improve distribution as they give franchisors the possibility of establishing a uniform distribution network without the need for major investments, which may assist the entry of new competitors on the market, particularly in the case of small and medium-sized undertakings, thus increasing inter-brand competition. They also allow independent traders to set up outlets more rapidly and with a higher chance of success than if they had to do so without the franchisor's experience and assistance. They therefore have the possibility of competing efficiently with large distribution undertakings. Finally, they allow consumers and other end-users a fair share of the resulting benefit, as they combine the advantage of a uniform distribution network with the existence of traders personally interested in the efficient operation of their business.

With these considerations in mind, the Commission enacted, in 1988, a block exemption regulation in the field of franchising agreements (Commission Regulation No 4087/88, OJ L 359, 1988). The Regulation is based on the principle that the exemption should apply to all economic sectors, including those where specific block exemptions have been adopted (motor vehicles, beer, service-stations). This is because franchise agreements are considered to be different in nature from selective distribution or exclusive purchasing agreements. The Regulation however formally excludes the possibility of combining different block exemptions. The block exemption covers distribution and service franchises but does not include manufacturing franchises, which consist normally of patent, know-how and/or trademark licences.

Main provisions of the Regulation

The Regulation exempts the territorial protection granted by the franchisor to the franchisee or to the master franchisee, the location clause imposed on the franchisee and the obligation on the latter not to deal in goods competing with those manufactured by the franchisor or bearing its trademark.

A list is included of the obligations which are normally not to be restrictive of competition. Exclusive purchase is admitted only for products for which it is not possible to formulate objective quality specifications. A non-competition obligation is also considered as non-restrictive, including for a period up to one year after termination of the contract. To take account of the possibility that some of the obligations listed such as the non-competition clause or the obligation to keep minimal stocks, might in practice be restrictive of competition, the Regulation states that in such a case they are also covered by the exemption. This technique mirrors that which has been adopted in the patent licensing and motor-vehicle distribution regulations.

The exemption applies only where certain conditions are fulfilled such as the possibility of inter-franchisee sales and Community-wide guarantee.

The Regulation contains a 'black list' of restrictions which prevent the application of the exemption. This applies in particular to market sharing between competing manufacturers, clauses unduly restricting the franchisee's choice of suppliers or customers, and to cases where the franchisee is restricted in determining its prices.

Provision is also made for an 'opposition procedure' pursuant to which the exemption may be extended to agreements containing restrictions of competition which are not expressly mentioned in the Regulation. Such agreements must be notified to the Commission which then has six months in which to oppose the exemption. An agreement which has not been opposed within this period is automatically exempted under the Regulation.

The possibility of the withdrawal of the exemption is provided, in particular, in cases where access to, or competition within, a specific market is substantially restricted.

Industrial property

Industrial property rights include patents, copyrights, trademarks, performing rights, registered designs and models. 'Know-how' is not actually an industrial property right, but it is sometimes treated analogously.

At present, how these rights can be obtained and used is determined by the national laws of each Member State.

The existence of these national systems is in itself perfectly legitimate, but a problem arises where the national rules are used to partition the common market along national boundaries. This is a matter relating to the free movement of goods within the Community. A second problem relates to how the owner of an industrial property right uses that right or allows others to use it. Here, the competition rules may be relevant. Both of these problems have taken on an added significance in the light of the single market strategy.

The following general rules are important to bear in mind when dealing with industrial property rights:

(i) The principle of the free movement of goods. Once goods protected by industrial property rights have been legitimately marketed in Member State A, by the owner or someone authorized by him to do so (for example, a licensee), the importation of those goods into Member State B cannot be prevented on the basis of the parallel property rights existing under the national legislation of Member State B. For example, a manufacturer registers a trademark for his products in each Member State where the products are sold, for example France and Germany. Once the goods in question have been marketed in Germany, the importation of those goods into France cannot be stopped by invoking the same trademark it is registered under in France.

Of course, where a third party unlawfully uses a registered trademark, the manufacturer can take the necessary steps, but this is a normal case of trademark infringement, not a matter of illegally partitioning the common market.

(ii) If an undertaking is in a dominant position in the common market or a substantial part thereof, the improper exploitation of an industrial property right may be in violation of Article 86 (abuse of a dominant position). There must, of course, be an actual or potential effect on trade between Member States.

(iii) The owner of an industrial property right may decide to confer upon an enterprise the benefit of that right; for example, he may let another firm use his registered trademark, or if he is the owner of a patent, he may confer a licence to manufacture and sell the goods to another. In return, the other party will normally be asked to pay a royalty. In itself, such authorization of a third party to exploit the patent or any other industrial property right is not caught by Article 85(1). Problems may, however, arise when the authorization is accompanied by clauses which restrict competition without being justified in that they protect the industrial property right.

In general, the tests for application of Article 85(1) or exemption under Article 85(3) are the same in the area of industrial property rights as in other areas.

Patent licensing (Commission Regulation No 2349/84)

Patent licensing agreements may present problems in view of the territorial restriction they impose, which can lead to the isolation of national markets, and the exclusivity they confer on the licensee to manufacture and/or sell the products covered by the patent.

On the other hand, patent licensing has a number of beneficial aspects. Such agreements allow firms which might otherwise not be in a position to do so, to obtain access to new technologies. Also, patent licensing encourages the innovative activities of smaller firms which do not have the financial resources to exploit their inventions themselves throughout the whole Community.

In recognition of the beneficial effects which patent licensing agreements can have, the Commission adopted a group exemption in this area, which is characterized by three main principles:

(i) in the first place, it recognizes the need for a certain degree of protection for the holder of a patent (licensor) and his licensees. This will create a favourable environment for the transfer of new technology throughout the Community and at the same time stimulate and reinforce R&D activities of undertakings, which generate advanced techniques and new products;

(ii) secondly, it aims to assure effective competition and, subject to certain limitations, the freedom of intra-Community trade for the patented products;

(iii) thirdly, it provides legal security for the contract partners.

As to the problem of territorial protection for both the licensor and the licensee, the regulation exempts the grant of exclusivity by the licensor to the licensee and allows each party to be protected against any competition, active or passive, from the other party throughout the duration of the agreement.

The licensee may be granted the same full protection against competition from other licensees for up to five years from the time the product is first put on the market within the Community. After this initial period, licensees must be free to supply the product in the territories of other licensees in response to unsolicited demand from customers in those territories ('passive sales'). A ban on manufacturing or actively selling the product in other licensees' territories is exempted for the duration of the contract.

The exemption of territorial protection is subject only to the general condition that the licensed patents or parallel patents are still in force in the protected territory and that the licensee manufactures the licensed product himself or has it manufactured by a connected undertaking or by a subcontractor.

The Regulation provides a non-exhaustive list of obligations which do not preclude the exemption, such as obligations on the licensee to obtain from the licensor products necessary for the exploitation of the invention, to pay a minimum royalty, to keep know-how communicated to him secret and to restrict his manufacture of the product to one or more technical fields of application. Such obligations, which are normally not restrictive of competition, are also covered in the event that because of the particular economic or legal circumstances, they do fall within Article 85, even where the licence is non-exclusive.

Also listed are certain clauses which cannot be exempted by the regulation because they cannot be presumed to have the positive effects required by Article 85(3). These can only be exempted by individual decision in the light of the specific circumstances of each case. Such clauses notably include no-challenge clauses, agreements of indefinite duration, non-competition clauses, and quantity and price restrictions.

An opposition procedure identical to the one in the R&D Regulation is included for agreements which contain restrictions not expressly provided for in the Regulation, as long as they do not appear on the 'black list'.

Know-how licensing

Know-how licensing agreements are now also covered by a block-exemption Regulation, Commission Regulation No 556/89 of 30 November 1988 (OJ L 61, 4.3.1989). This measure was enacted in recognition of the increasing economic importance of non-patented technical information such as descriptions of manufacturing processes, recipes, formulae and drawings. The number of agreements concluded for the exploitation of such information has increased significantly in recent years. Like patent licences, know-how agreements are pro-competitive and have beneficial effects upon the economy, in facilitating the transfer of technology and boosting innovation, but they may, in particular circumstances, inhibit competition by imposing territorial restrictions. Moreover, given that the transfer of know-how is frequently irreversible, the Commission felt that it was necessary to provide greater legal certainty for undertakings as regards the compatibility of such agreements with the competition rules.

The Regulation encompasses pure know-how agreements concluded solely for the exploitation of such information, as well as mixed know-how and patent licensing agreements that are not covered by the patent licence block exemption. Know-how, for this purpose, is defined as a 'body of technical information that is secret, substantial, and identified in any appropriate form'.

The structure of the know-how regulation is the same as that of the patent licence Regulation. Thus, it lists those obligations of a restrictive nature that benefit from automatic exemption pursuant to Article 85(3) of the EEC Treaty, including arrangements involving territorial protection of the licensor and the licensee against one another in respect of any exploitation of the know-how. This protection is generally available for 10 years from the date of the first licensing agreement entered into for each relevant territory within the EC. As between licensees, a 10-year and a five-year period of protection, both starting with the date of the first licensing agreement entered into for a territory within the EC in respect of the same technology, are permitted respectively against manufacture, use or active sales and against passive competition.

The Regulation also provides examples of obligations which are not regarded as restrictive of competition and whose inclusion in an agreement will not affect the applicability of the exemption. These include requirements that the licensee does not divulge the know-how to third parties, grant sub-licences, assign the licence or exploit the know-how where it remains secret after the termination of the agreement. The obligation to inform the licensor of any experience gained in exploiting the know-how and to grant him a non-exclusive licence in respect of improvements to, or new applications of the know-how is, subject to certain conditions, also permissible.

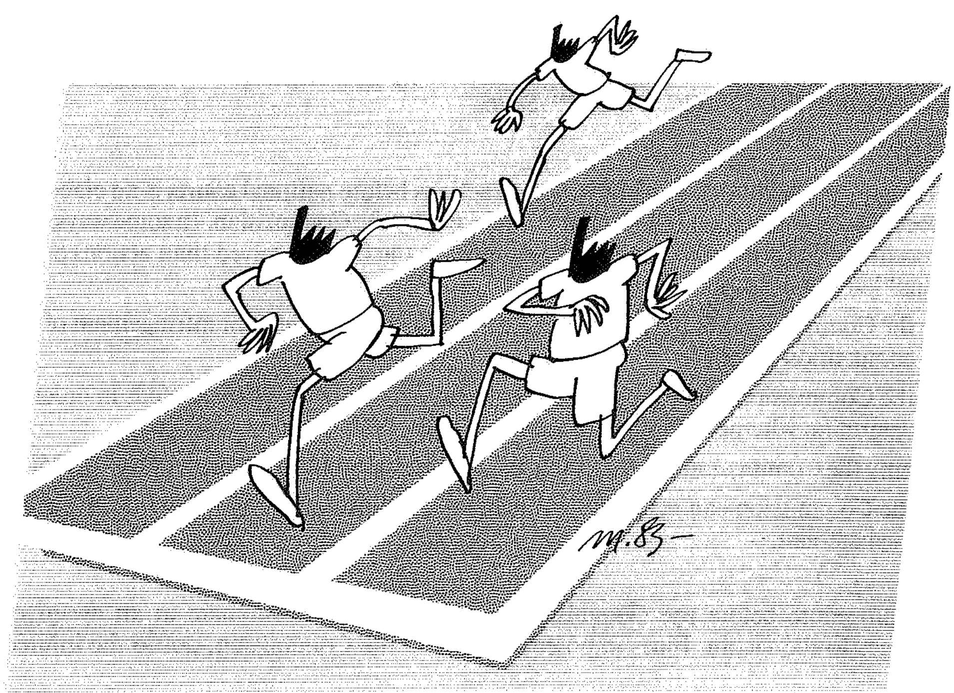
Finally, the Regulation lists provisions which, if contained in a know-how licensing agreement, would preclude the application of the block exemption. These include non-challenge clauses, agreements providing for automatic prolongation, non-competition clauses and quantity and price restrictions. Such agreements must be notified to the Commission which will decide whether an individual exemption is justified according to the particular circumstances of the case.

As in other group exemptions, the know-how Regulation provides for an opposition procedure allowing the exemption to be extended to agreements containing restrictions which are not expressly mentioned in the Regulation but which are nevertheless, compatible with Article 85(3) of the EEC Treaty.

IV — Enforcement of the competition rules

Enforcement by the national courts

As was stated in Chapter I, the European Community has, at its disposal, a number of instruments for applying and implementing Community policy. Community rules, in the form of regulations and decisions are directly applicable and binding in the Member States. Regulations are generally applicable, while decisions are binding on those to whom they are addressed. Treaty provisions and directives are also capable of conferring rights upon private litigants to the extent that they have direct effect as defined by the European Court of Justice.



In practical terms, it is now established that the Community competition rules create rights and obligations for private legal parties which may be raised in national legal proceedings. Accordingly, any company or individual who claims to have suffered injury as a result of actions which were in breach of Community competition law has access, in principle to a national remedy, and is entitled to make a claim for damages. However, the exact legal nature of the claim and the level of damages available will vary according to local jurisdictional rules and procedures.

To date, undertakings concerned about a possible breach of the competition rules have tended to use the Community's own complaints procedure (see the following section of this chapter) in preference to direct action against the alleged offenders in the national courts. This is despite the fact that the powers of the Commission and the Court of Justice, while extensive, do not include the award of damages to injured parties.

Where a person or company suffers loss, as a result of such an infringement, it may therefore, be appropriate to seek relief using available local remedies. In this connection, plaintiffs should be aware of the possibility, available to all national judges, of referring questions of Community law to the European Court of Justice for a preliminary ruling. Courts of final appeal are obliged to seek a preliminary ruling, where a decision on the question is necessary to enable it to give judgment.

Enforcement by the Commission

Running parallel to the possibility of such actions before national courts is an elaborate procedure of application of the competition rules by the Commission. In some ways, this procedure has further-reaching consequences for the firms involved than actions at national level, in that, for example:

(i) the Commission has the power to impose administrative fines for infringement of the competition rules;

(ii) the Commission has extensive powers to collect the information it needs in order to determine whether an infringement is taking place;

(iii) only the Commission has the power to grant exemptions on the basis of Article 85(3);

(iv) the Commission can take interim measures to bring damaging behaviour to an immediate halt.

The procedure before the Commission cannot, however, culminate in an award of damages to the victim. Fines imposed are paid to the Commission, not to the injured party.

The initiation of a procedure

There are a number of ways in which a procedure before the Commission involving the competition rules can be set in motion:

(a) notification, for negative clearance or for exemption;

(b) complaints;

(c) own-initiative action by the Commission;

(d) sector investigations by the Commission.

Notification

The mechanism of notification

Agreements between enterprises and decisions by associations (e.g. trade associations) may be submitted to the Commission to seek a decision from the latter that the agreement does not violate Article 85(1) at all (this is a negative clearance) or that the agreement does fall under Article 85(1) but meets the conditions for exemption under Article 85(3). Although the correct terminology is 'application for negative clearance' and 'notification for exemption', the term 'notification' is used for both possibilities. In fact, applicants will normally submit one notification to the Commission seeking negative clearance or, in the alternative, individual exemption.

Note: No notification is necessary when an agreement falls under one of the group exemptions.

Notification must be made in writing on an official form issued by the Commission (Form A/B). This form requires the applicant(s) to give detailed information relating to the parties to the agreement and the essential features and aims of the agreement. To avoid any possible misunderstanding, it is wise to attach a copy of the agreement in its entirety to the form.

Notification need not be made by all those concluding an agreement, but whoever takes it upon himself to notify must in any event be a party to the agreement. Officially authorized representatives are also permitted to submit a notification.

Finally, enterprises should be aware of the importance of submitting accurate, complete and truthful information in their notifications. The Commission has the power to impose fines of up to ECU 5 000 where applicants intentionally or through negligence supply incorrect or misleading information in a notification.

Copies of Form A/B and the accompanying explanatory memorandum prepared by the Commission can be obtained from the Commission's Information Offices in each Member State and also outside the Community (a list of these adresses is given at the end of this brochure).

The importance of notification

There are three main reasons why notification can be very important to firms:

(i) as a rule the Commission cannot grant negative clearance or an individual exemption with regard to any agreement which has not been notified to it in the proper manner;

(ii) no administrative fines can be imposed by the Commission for activities which take place after notification and until the Commission reaches a decision, final or provisional, as to the applicability of Article 85(1) and/or Article 85(3), provided those activities do not go beyond those described in the notification;

(iii) where the Commission has established an opposition procedure for 'borderline' cases, the operation of this procedure requires notification of the agreement.

The fines which can be imposed for actual violation of Articles 85(1) and 86 must be distinguished from the (more minor) fines which can be imposed where a notification intentionally or negligently contains misleading or untruthful information.

There are two exceptions to the general rule that, to obtain an exemption under Article 85(3), the agreement in question must be notified to the Commission:

(1) agreements which fall under one of the group exemptions are automatically exempted (subject to notification, to qualify under the opposition procedure);

(2) certain types of agreement do not have to be notified, and can nevertheless, if the case arises, be exempted by the Commission retrospectively to the date on which the agreement was concluded. In broad lines, the requirement to notify does not apply to:

   (a) agreements between parties located only in one Member State and not relating to imports or exports, in other words, agreements which are purely domestic or local in scope;

   (b) agreements between two parties in which the sole restriction is a unilateral restriction on one of the parties as to prices and terms of resale or as to the exercise of industrial property rights or know-how;

   (c) agreements between two parties which have as their sole object:

      - the development or uniform application of certain standards or types, or
      - joint research and development, or
      - specialization in manufacturing, where the market share is not more than 20% and aggregate annual turnover not more than ECU 500 million.

A caveat should be added:

(i) in case any doubt exists as to whether a particular agreement falls under one of the categories for which notification is not required, the parties should not hesitate to notify;

(ii) the advice 'when in doubt, do notify' is especially important because the benefit of immunity from fines is available only with respect to notified agreements and agreements covered by group exemptions.

Quick checklist in connection with notification

When deciding whether or not an agreement should be notified to the Commission, undertakings should run through the following questions:

(i) Does the agreement have any connection at all with competition? If not — for example, if the agreement concerns a simple sale of goods — there is no need to contemplate notification.

(ii) If the agreement does feature certain restrictions on competition, are the competition rules nevertheless inapplicable because, for example, the effects are minimal, or the activity is covered by one of the relevant Commission notices? If so, parties need not notify.

(iii) If the agreement seems likely to contain elements which are contrary to Article 85(1), but also appears to the parties to fulfil the requirements for exemption under Article 85(3), parties must determine:

(a) whether the agreement falls under one of the group exemptions.
If so there is no need to notify. The agreement is safe and no fines can subsequently be imposed;

(b) whether the agreement is one of the types of agreement for which notification is not required. If so there is no need to notify. Exemption can if necessary be obtained later, even in the absence of notification. One risk in not notifying is, however, that immunity from fines is not guaranteed.

If neither of the above applies, parties should make the proper notification on Form A/B as soon as possible after concluding the agreement (or even before). The importance of timely notification lies in the fact that fines may still be imposed for the period preceding notification.

Complaints

General

Anti-competitive behaviour can be brought to the attention of the Commission by way of a complaint.

Potential complainants should first carefully consider a number of questions:

(i) Is the object of the complaint autonomous behaviour by undertakings, or is the behaviour imposed by national legislation? In the latter case, the competition rules do not apply.

(ii) Is there a transfrontier effect involved in the behaviour? If not, the matter would be one of national, not Community, competence.

(iii) Are all the other elements of either Article 85 or 86 fulfilled? For actions under Article 85, the complainant should check whether the agreement in question is perhaps *de minimis*. In that case, there is no point in complaining. For Article 86 cases, a dominant position is required — not always an easy requirement to prove — and there must be an abuse thereof.

(iv) Would action before a national court be preferable in order to obtain damages?

In short to avoid wasting the time of all involved, complaints should only be submitted after careful consideration.

Who can complain?

Those entitled to submit complaints are Member State authorities, individuals or legal persons, such as companies or trade associations.

One essential requirement is that a complainant must have a legitimate interest in the termination of the objectionable behaviour. Parties to an agreement would in any event be deemed to have a legitimate interest. Furthermore, any third party who can show that the alleged anti-competitive behaviour is damaging — even potentially — to him, will normally have a legitimate interest.

Consequences

When a complaint is submitted by a party having a legitimate interest in the matter, the Commission will examine whether a violation of the competition rules is in fact taking place. If the complaint turns out to be well-founded, the Commission can then take the necessary measures to put an end to the infringement. If, on the other hand, the Commission, after examining the matter, finds that the complaint is not justified, it must inform the complainant of its reasons for not pursuing the matter. The complainant must then be allowed a certain period of time to submit any further comments, after which the Commission will either continue its investigation, if new facts have come to light, or definitely reject the complaint.

Form and contents of a complaint

There are no specific requirements as to the form in which a complaint is made. However, given the fact that the Commission is only obliged to investigate a complaint by a party showing a legitimate interest in the matter, it is in the interest of the complainant clearly to present the facts involved in writing. A simple letter is sufficient. The complaint should in any event include:

(a) the name and address of the complainant;

(b) the identity of the undertaking(s) which are the subject of the complaint;

(c) evidence which support the complainant's claim to a legitimate interest in the matter;

(d) a clear description of the substance of the complaint and, if possible, the reasons why the complainant believes the behaviour in question constitutes an infringement of Article 85 and/or 86;

(e) if the complaint is signed by a representative, evidence of his authority to act on behalf of the complainant.

The party who is the subject of the complaint will be informed of the complaint against him and will be given the opportunity to present his views. In this context, the complainant would be well advised to indicate clearly which parts of his complaint are to be considered as confidential and thus not to be transmitted to the party in question.

Informal or anonymous complaints

The Commission also receives oral — sometimes anonymous — complaints. The difference with the 'formal' complaints described above is that the Commission is under no obligation to examine such so-called informal complaints, although it may of course do so if it wishes.

Therefore, where there is serious evidence that an infringement of the competition rules is taking place, any undertaking which is being harmed by the behaviour in question should contemplate the advantage of lodging a formal complaint in writing.

Own-initiative intervention by the Commission

There is a variety of ways in which the Commission can become aware of possibly anti-competitive behaviour. These include questions raised in the European Parliament, articles in newspapers, information received from Member State authorities, or contacts with interest groups, such as consumer organizations. Although the Commission is not obliged to pursue matters which come to its attention in this way, it can decide on its own initiative to examine further, such cases and will definitely do so if the information it has received seems to point to a serious infringement of the competition rules.

Furthermore, the Commission has the power to conduct general inquiries into economic sectors where it feels competition is being restricted or distorted. Such inquiries have, for example, taken place in the brewery industry and the margarine industry.

Fact-finding by the Commission: procedural decisions

Where the Commission decides that commercial activities which have come to its attention seem to pose problems in the context of the competition rules, it will normally need more information to be able to reach a definite opinion on the legality of the behaviour in question.

There are two basic ways in which the Commission can obtain information from undertakings:

(i) written requests for information;

(ii) investigations.

Requests for information

The Commission can send written requests (including telexes) for information, not only to undertakings which are suspected of infringements, but also to third parties who may be in a position to clarify certain matters. For example, where the Commission is examining the behaviour of a dominant firm, it may ask smaller firms who have dealings with that firm to indicate whether they have ever been subject to specific abusive treatment by it.

Requests for information involve the following consequences:

(i) where the undertakings interrogated reply promptly, correctly and completely to the Commission's letter, no further complications need be feared (although the Commission may, of course, subsequently request additional information);

(ii) if in their reply the undertakings concerned provide incorrect or incomplete information, the Commission has the right to impose fines of up to ECU 5 000;

(iii) if the undertakings choose to ignore the initial request for information altogether, or if their reply is incomplete, the Commission may as a second step take a formal decision ordering complete information to be supplied. Failure to respond to this formal decision is not to be recommended, because daily default fines of up to ECU 1 000 can be imposed by the Commission until a complete reply is finally received.

In sum, undertakings who receive a request for information from the Commission must seriously bear in mind:

(a) that if they decide to reply, that reply must be correct and complete;

(b) that if they do not reply to the first request for information, they stand the risk of subsequently being forced to reply anyway, if necessary, by means of daily default payments.

Investigations

The Commission has the power to send authorized officials to the premises of undertakings in order to gather the information it needs. The officials who make an inspection visit are entitled to examine the company's business records and documents, take copies or extracts thereof, request explanations and enter all premises, land or vehicles belonging to the company. Again, as in the case of written requests for information, undertakings who submit to such an inspection but produce the requested material in incomplete form run the risk of fines of up to ECU 5 000.

Undertakings are not obliged to admit Commission officials who come on inspection, but the Commission may then proceed to take a formal decision ordering them to comply, if necessary reinforced by a daily penalty payment of up to ECU 1 000 for each day the undertaking refuses to admit the Commission inspectors.

The Commission is not obliged first to give the undertaking concerned the opportunity to comply with an investigation based on a simple mandate before passing on to the more forceful instrument of ordering the undertaking to comply by a formal decision. Normally, the Commission will resort to an unannounced visit by decision at the outset where a serious risk exists that the undertakings, if forewarned of the inspection, will destroy any incriminating evidence.

Undertakings who receive a visit from Commission inspectors are allowed to ask for a legal adviser to be present, but the inspection can not be unduly delayed to await the arrival of such a person.

The procedure leading to a final decision

The three basic types of decisions which the Commission can take in application of Articles 85 and 86 are:

(i) decisions granting negative clearance;

(ii) exemption decisions pursuant to Article 85(3);

(iii) decisions ordering the termination of an infringement.

The procedural decisions which the Commission can take in connection with its powers of investigation, for example, ordering an undertaking to admit Commission inspectors, have been dealt with in the preceding paragraph.

Other measures which may occur when the Commission deals with a case are:

(a) interim measures;

(b) provisional decisions;

(c) informal settlements.

Negative clearance

When an undertaking has made an application on Form A/B, seeking formal assurance from the Commission that its agreement or other commercial activities are not deemed to infringe the competition rules, the Commission must first give any other interested parties the chance to make their views on the matter known. This is done by publishing the main facts of the case in the *Official Journal.* Any interested parties are given a specific period of time to react to this publication and thus new facts may be brought to light which may cause the Commission to reconsider its position.

A second formality which must be observed before negative clearance can be given is consultation of Member State authorities, who meet for this purpose in the body referred to as the 'Advisory Committee on Restrictive Practices and Dominant Positions'.

If after these steps have been observed the Commission maintains the view that negative clearance is justified, a formal decision is taken which states that on the basis of the facts in its possession, there are no grounds for the Commission to take any action under Article 85(1) and/or Article 86 against the agreement or other commercial activity involved.

It is clear that if new facts subsequently arise or if the circumstances involved change substantially, the Commission retains the power to reconsider the matter. To date, however, no cases have occurred in which the Commission has gone back on a decision granting negative clearance.

Exemption

As in the case of negative clearances, a decision granting exemption must be preceded by publication in the *Official Journal* of the main elements involved, giving interested parties the opportunity to submit any observations, and by consultation of the Advisory Committee on Restrictive Practices and Dominant Positions.

The Commission's decision indicates why the agreement or other activity in question is deemed to violate Article 85(1) and what elements have been found by the Commission which fulfil all the requirements for justifying an exemption under Article 85(3).

Exemption is always granted for a fixed period of time, which can be extended. The decision may impose certain obligations on the undertakings involved and in some cases, the parties may be requested to modify certain aspects of their agreement before exemption can be granted at all.

Normally, exemption can only be granted as of the date of notification. Only in the case of certain types of agreement which need not be notified (see above) can exemption be granted as of the date on which the agreement was concluded.

Decisions attacking an infringement

Procedure

When a matter comes to its attention through a complaint, a notification or in any other way, the Commission may reach the preliminary conclusions that a violation of Article 85(1) or 86 is taking place and, in the case of notifications, that the conditions for granting an exemption under Article 85(3) are not present.

The Commission must give the parties concerned notice of its objections to their behaviour in the form of a written communication known as the 'statement of objections'. Annexed to the statement of objections is a list of the documents which constitutes the Commission's file in a particular case. In order to prepare their response, parties may examine the file on the Commission's premises, although documents of a confidential nature, for example, concerning other undertakings' business secrets or internal Commission notes, are normally not accessible. Parties are given a specific time-limit — normally one or two months, depending on the complexity of the case — to respond in writing to the Commission's objections.

After their written response, parties can also request an opportunity to argue their case orally. This 'oral hearing' is organized by the Directorate-General for Competition and is conducted by the Hearing Officer. This official ensures that the rights of the defence are respected and has the right to make observations to ensure that in the procedure leading to the Commission's decision, due account is taken of all the relevant facts, whether favourable or unfavourable to the parties concerned.

Following the oral hearing, the Commission must consult the Advisory Committee on Restrictive Practices and Dominant Positions.

Only after all these procedural steps have taken place can the Commission come to a final decision.

Contents of the decision

Where an infringement is found to exist, the Commission will order the undertaking involved to put an end to it forthwith, a so-called cease and desist order. Of course, where the parties have already terminated the infringement, for example, during the course of the procedure before the Commission, the decision may simply consist of a declaration that the behaviour in question constituted an infringement.

If appropriate, the Commission also has the power to order positive action by the undertakings involved. For example, where a dominant undertaking has been found to abuse its position by refusing to supply a customer, the Commission may require that firm to resume supplies within a specified period and ensure appropriate supply arrangements for the future.

Fines

The Commission has the power to impose fines of up to ECU 1 million or 10% of the world annual turnover of the undertaking concerned in the previous business year (whichever of the two is greater), where undertakings are found to have infringed Article 85(1) or 86, intentionally or through negligence.

Whether or not a fine will be imposed, and the determination of the amount of the fine, will depend, among other things, on the seriousness of the behaviour, how long it went on and the size of the undertakings involved. A deliberate infringement will normally deserve a heavier fine than where undertakings can only be accused of negligence. Activities which have been frequently attacked by the Commission in the past will also warrant heavier fines, because such undertakings should realize, through the case-law built up by the Commission and the Court of Justice, that this behaviour is not permitted.

With respect to notified agreements, fines cannot be imposed for the period between the moment of notification and the Commission's decision, whether provisional or definite (see below).

Fines are, however, possible for the period during which the agreement was in force before notification.

Also, where the Commission refuses to grant an exemption, the result is that the agreement in question, whose illegality is thus confirmed, may give rise to actions in national courts, for example, for damages.

Interim measures

Depending on the complexity of any given case, it may take the Commission one or two years or even more to reach a final decision. During that time, the behaviour in question may give rise to serious and irreparable damage to, for example, a complainant, whose very existence may be threatened, or it may be totally unacceptable in the general public interest. In such cases of urgency, the Commission has the power to take immediate action in the form of so-called interim measures to stop the objectionable behaviour. Such measures are of a temporary nature aimed at safeguarding the status quo and do not determine the final outcome of the matter being dealt with.

Provisional decisions

The general rule is that once an agreement has been notified, no fines can be imposed with respect to the period after notification. This immunity from fines can, however, be lost where the Commission takes a provisional decision informing the parties that after preliminary examination, it is of the opinion that Article 85(1) applies and exemption under Article 85(3) is not justified.

If the parties disregard this warning, they run the serious risk of being fined in the Commission's final decision.

Informal settlements — administrative letters

For the sake of expediency, many cases before the Commission are concluded by way of an informal settlement, notably where the undertakings involved voluntarily eliminate any objectionable practices. In fact, the Commission normally takes 20 or so formal decisions each year, whereas the number of informal settlements is usually several hundred.

In some cases, informal settlements take place by way of 'administrative letters' in which the Commission services inform the parties that it sees no reason to take any action under the competition rules and that the relevant file will therefore be closed. Such letters are administrative documents and do not have the legally binding effects of decisions, but may nevertheless be useful as guidance. Also, the Commission's recently instituted practice of publishing a notice of its intention to issue an administrative letter in certain cases, allowing third parties to react before it takes any further steps, enhances the value of such administrative letters.

Publicity

Decisions granting negative clearance, exemption or ordering the termination of an infringement, as well as interim measures and provisional decisions, must be published in the *Official Journal.* Procedural decisions, such as those formally requesting an undertaking to supply information, need not be published in the *Official Journal,* but the Commission may nevertheless decide to do so, for example in cases of general interest.

The Commission normally issues press releases regarding the decisions it has taken. Press releases can also be used to make the general public aware of informal settlements which for some reason contain important elements which are of general interest.

Finally, the Commission's monthly *Bulletin*, as well as the annual *Report on Competition Policy,* contain information on the decisions and informal settlements that have taken place.

Control over the Commission by the European Court of Justice

The European Court of Justice has the following powers of review over decisions taken by the Commission:

(i) the Court has the power to confirm, reduce, cancel or increase fines and penalty payments imposed by Commission decisions;

(ii) all formal decisions by the Commission — negative clearances, decisions granting or refusing exemption, orders to terminate infringements, decisions requesting information, orders to submit to an investigation and provisional decisions relating to the immunity from fines — can be reviewed and, if necessary, annulled or varied by the Court.

Furthermore, appeals can be brought before the Court where the Commission has failed to act, for example, failure to examine a formal complaint that has been submitted to it or to inform the complainant of its reasons for not pursuing the matter after preliminary examination.

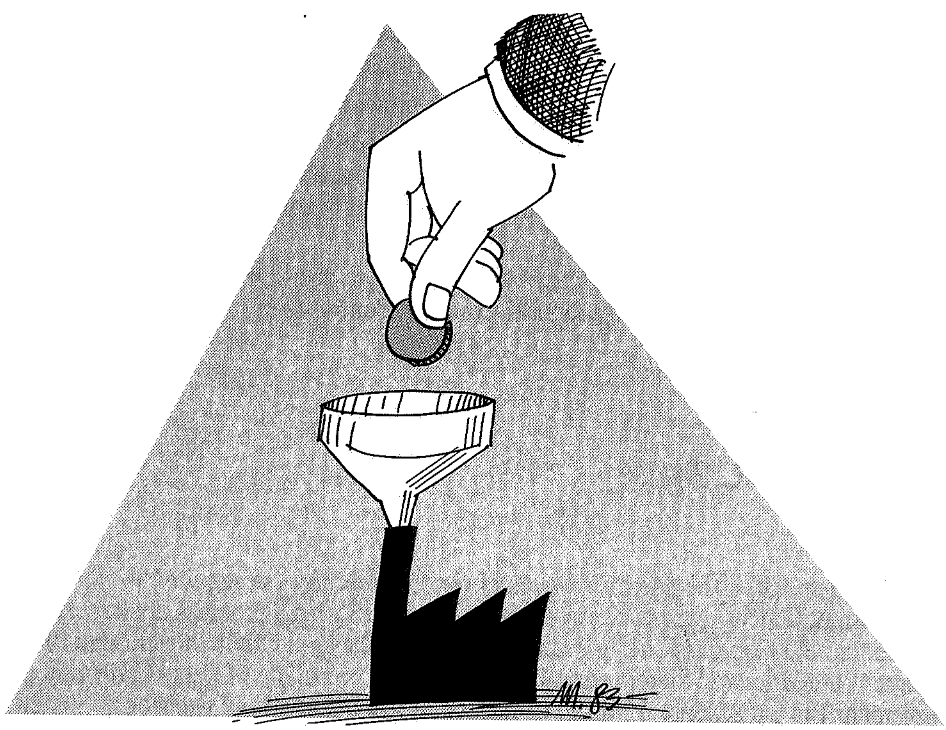
Those entitled to bring actions before the Court are all natural or legal persons against whom a decision has been taken as well as any other parties who are directly and personally affected by a decision.

V — State aids

Another aspect of Community competition policy that is likely to be of interest to businesses is the control of national aids. Under Articles 92 and 93 of the EEC Treaty this control is exercised by the Commission.

Article 92, EEC Treaty

Article 92(1) provides that, as a general rule, all government aid to business is forbidden: '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 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.'

The concept of 'aid' is a good deal wider than just government grants, cheap loans and interest subsidies, where the gratuitous element is immediately obvious. It also covers such forms of support as tax concessions, public guarantees of corporate borrowing from banks or the capital market, provision of goods and services on preferential terms, and, in some circumstances, the acquisition of public shareholdings in businesses. Any other measure having an equivalent effect will also fall within the definition.

Article 92(2) goes on to provide that certain types of aid are nevertheless compatible with the common market, namely aid having a social character which is granted to individual consumers, provided that it is granted without discrimination related to the origin of the products concerned, aid to make good the damage caused by natural disasters, and aid required to compensate for the economic disadvantages caused to certain areas of the Federal Republic of Germany by the division of Germany.

Article 92(3) then lists several other categories of aid that may be considered compatible with the common market:

(a) aid to promote the economic development of areas where the standard of living is abnormally low or where there is serious underemployment;

(b) 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;

(c) 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; and

(d) such other categories of aid as may be specified by a decision of the Council acting by a qualified majority on a proposal from the Commission.

Article 93, EEC Treaty

Under Article 93(3), the Member States of the Community are required to notify the Commission, well in advance, of any plans to introduce new aid schemes or alter existing ones so that the Commission can determine whether they fall within one or other of the excepted categories and therefore can be allowed to proceed. The Member State may not implement the aid scheme until the Commission has taken a final decision.

The Commission has two months in which to define its position on a notified scheme. If it considers the scheme to be compatible with the common market, the Member State is informed that the scheme may go ahead.

If it does not think it will be able to authorize the scheme, however, it opens a special procedure, which is laid down in Article 93(2). Under this procedure, the Commission gives the Member State a certain period, usually a month, in which to defend its scheme against the objections which the Commission has raised. Comments are also invited from the other Member States and from other interested parties, the latter being informed by publication of a notice in the *Official Journal of the European Communities.*

At the end of the procedure, the Commission takes a final decision in which it takes into account the arguments of the Member State concerned and the reactions of the other Member States and interested parties. It may decide to drop its objections or to order the Member State to abandon the scheme or to alter it in some way.

In any event, the Commission is obliged to follow the Article 93(2) procedure before turning down any notified aid scheme.

If the Member State disagrees with the Commission's decision on its aid scheme, it has two months in which to demand a judicial review by the Court of Justice.

A Member State failing to comply with a decision within the prescribed time, however, can itself be brought before the Court of Justice by the Commission or any other interested Member State.

The Commission has the power to order a Member State to recover from the recipient any aid it has granted unlawfully, that is to say, without prior notification of the scheme or before, or in defiance of, the Commission's decision in the case of a scheme that was notified.

The Commission also has a duty, under Article 93(1), to keep existing aid systems under constant review and to issue appropriate recommendations to Member States where the progressive development or functioning of the common market so requires. Existing schemes include both those in force before the common market was founded and those introduced later with the Commission's approval. If the Commission finds that, for one reason or another, such an aid scheme is no longer compatible with the common market, it issues appropriate recommendations either to amend or abolish it. If the Member State refuses to take the action recommended, the Commission initiates the Article 93(2) procedure. In the case of an existing scheme this does not have the same effect of suspending implementation as it does in the case of a new scheme, that is the Member State can continue to award aid under the scheme until the Commission has taken a formal decision.

VI — Small and medium-sized enterprises

One of the Commission's main concerns in the competition policy area is to strengthen and preserve small and medium-sized enterprises (SMEs) as an essential element in a healthy and competitive environment. The Commission remains convinced that such businesses form one of the basic foundations of the European economy because of the contribution they make to the competitive structure of the market, their flexibility and their dynamism.

Articles 85 and 86, EEC Treaty

An active competition policy makes a significant contribution to creating and maintaining an auspicious environment for SMEs and the competition rules often provide a valuable weapon in protecting their interests. For example, Article 85 prohibits agreements through which the parties undertake to apply dissimilar conditions to equivalent transactions and to impose on contracting third parties, the requirement that they accept supplementary conditions which have no connection with the subject of the contract. The ban on the abuse of dominant positions helps to protect SMEs against powerful competitors, suppliers or customers. For instance, the Commission has taken action against the charging of abnormally low prices intended to squeeze out small competitors and against refusals to supply products that are essential to the activity of SMEs. Competition policy similarly enables the Commission to oppose operations that would improperly increase a firm's dominant position on the market.

The consistent and effective implementation of the competition rules also presupposes that SMEs observe such rules themselves. The Commission is aware that this may impose certain constraints on SMEs, and while an internal Commission study concluded that the implementation of the competition rules did not impose excessive burdens, it was felt nevertheless that SMEs should benefit from simplified procedures. This is reflected in the derogation provided for agreements of minor importance, which are not covered by Article 85(1), and which is explained in greater detail in Chapter II.

The desire to limit the constraints on SMEs is also reflected in the various block exemption regulations which, subject to certain conditions, provide for exemption from the prohibition laid down in Article 85(1) (see Chapter III). The following features are of particular importance to SMEs:

(a) no notification is required, thus avoiding time-consuming procedures;

(b) several block exemption regulations are of direct relevance for SMEs either because of the conditions for application (market share and turnover criteria) or because of the nature of the activity concerned, for example:

   (i) non-reciprocal exclusive distribution agreements between competitors are only allowed if at least one of the parties has an annual turnover of less than ECU 100 million;

   (ii) the block exemption regulation on exclusive purchasing agreements, which normally involve SMEs (e.g. public houses and service stations) prevents the purchaser from being excessively bound to the supplier in terms of time and the range of products he buys;

   (iii) the regulation on motor vehicle distribution agreements ensures that car dealers who are usually SMEs are not made overly dependent on the supplier and affords greater freedom as to the dealer's use of spare parts and sales to other authorized dealers;

   (iv) the patent licensing and know-how block exemption regulations both allow small firms (as licensees) to gain access to new technologies and also encourages the innovative activities of small firms, who (as licensors) can thus exploit their inventions throughout the Community via (bigger) licensees. This helps to safeguard existing jobs and to create new ones;

   (v) the block exemption on specialization agreements, which applies only where market share and turnover thresholds (20% and ECU 500 million) are not exceeded, was specifically created to allow SMEs to improve their production processes and thereby strengthen their competitive position;

   (vi) the research and development block exemption regulation provides that competing undertakings which together have a market share of less than 20% may engage in joint research and development and joint exploitation of the results. This criterion implies that nearly all agreements of this type involving SMEs will be covered;

   (vii) the franchising block exemption regulation, which gives franchisors the possibility of establishing a uniform network with limited investments, will assist the entry of new small and medium-sized competitors to the market. Independent traders will also be able to set up outlets more rapidly, and with a higher chance of success than if they had to do so without the franchisor's experience and assistance.

State aids

All Member States dispense aid in one form or another to small and medium-sized firms. As a rule, this aid will fall under Article 92(1) of the EEC Treaty.

The Commission, however is conscious of the handicaps faced by smaller firms. Their legal form and size puts them at a disadvantage in obtaining finance. They may be too small for long production runs, so their costs of production are high. They may lack the scientific and technical resources for research and development and, very often, they will also suffer from handicaps in the field of management, organization and marketing.

The Commission also recognizes the importance to the single market of having a healthy and substantial network of small and medium-sized firms. These contribute to economic growth and employment creation as well as performing an essential role in the maintenance of effective competition and in the balanced social and economic development of the regions.

These factors together make it easier for the Commission to condone aid to a small or medium-sized firm than to a large company, and this is reflected in the application of the State-aid rules.

Aid authorized by the Commission to the small-business sector

The type of aid Member States choose to extend to small firms will depend on the problems that have to be solved, which will vary at different stages of a business's life: whether it is just starting up or is already an established business, being extended or switching to a new field, or changing hands.

The aid to small and medium-sized firms which the Commission has authorized in the past under Article 92(3) (c) of the EEC Treaty has often taken one of the following forms:

(i) grants, low-interest loans or loan guarantees to help small businesses get started;

(ii) low-interest loans or loan guarantees for investment by small businesses, which offer them terms matching those which the largest companies are able to obtain on the capital market or from banks;

(iii) public support to encourage the flow of risk capital to the small-business sector; the Commission has, for example, authorized a number of aid schemes involving specialized public agencies buying temporary stakes in small firms, the extension of government guarantees for private venture capital companies taking temporary stakes in such firms, or the grant of subordinated government loans enabling the firm to obtain further loans on that basis from the banking sector;

(iv) grants for research and development. As small firms do not always have the staff or facilities to carry out R&D themselves, some Member States have introduced, with the Commission's approval, aid schemes designed to reduce the cost of R&D work contracted out to others. The Commission's framework for aids in the R&D field, which was adopted in 1985, establishes criteria which are particularly favourable for small firms;

(v) grants or low-interest loans to innovation projects undertaken by small or medium-sized businesses (development of new products or manufacturing processes or radical improvement of existing products or processes), which might not proceed without government support because of the high risk they involve in both technological and financing terms;

(vi) grants or low-interest loans to investment projects involving energy or raw material savings or the replacement of oil by alternative fuels;

(vii) grants towards the cost of improving small firms' management or sales policy with the help of outside consultants or computerization.

In line with this general approach to small business, the Commission has cleared a number of proposals for setting up new aid schemes for the small-firm sector or for altering existing schemes. In some cases it has insisted on a lowering of the size limits for eligibility to ensure that only small or medium-sized firms can benefit under the scheme.

Conclusion

A concise overview of the complicated rules which form EEC competition law cannot pretend to give a ready answer to every imaginable question that may arise in practice.

It is hoped that this brochure will provide undertakings with a sufficiently complete picture to enable them to recognize situations in which the competition rules may be relevant and to deal, at least in the first instance, with potential conflicts.

Where undertakings are, for whatever reason, not in a position to reach an acceptable conclusion about the legality of a given matter, expert advice should of course be sought. In this connection, companies may consult specialist lawyers, national or European trade associations, federations of industry, chambers of commerce, European Parliamentarians, and, last but not least, the competition services of the European Commission.

It is important for the success of the single market that healthy competition is preserved. The Community's competition policies and rules will, therefore, continue to have a central role in post-1992 Europe, and it is in the interests of all companies to enhance their knowledge and awareness of this field.

Most of the legislative texts referred to in this brochure can be found in *Competition law in the EEC and in the ECSC*, Office for Official Publications of the European Communities, 1986.

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