

EC Competition Law and May 2004

The Impact on the Czech Republic*



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This article summarises the changes in EC competition law introduced in May 2004 as they affect the Czech Republic.

On 1 May 2004, huge changes were introduced to the way in which EC competition law is enforced. The recent enlargement, with ten new EU Member States, is probably the most important change, because it results in a scale change in the size of the European Union. However, that change has also led to other important changes: a reappraisal of how enforcement is spread across competition authorities in the European Union and an effort to see whether other modernising steps should be taken. Coincidentally, the EC Merger Control Regulation has also been subject to a review mechanism and the related changes to this Regulation also came into force on 1 May 2004.

Taking the changes in the order of likely significance to companies, the main changes are:

- (1) A revised EC Merger Control Regulation came into force after an extensive review of the existing one, bringing a new substantive test.¹
- (2) The modernising features of Council Regulation 1/2003² came into force, above all with the abolition of notifications to the European Commission (the 'Commission') for clearance of agreements.
- (3) The decentralisation aspects of Council Regulation 1/2003 came into force, above all the shared enforcement of the whole of Article 81 of the EC Treaty ('EC') with national competition authorities and national courts, meaning that they can also apply Article 81(3) EC.
- (4) A further ten countries, including the Czech Republic, joined the European Union,³ bringing new markets and opportunities for competition, an even greater breadth to the European Union and, as noted, a scale change in how the European Union has to be organised.

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These four aspects will now be outlined in turn, focusing on the main impact in the Czech Republic (although similar points apply for all the accession countries).

EC merger control after May 2004

Case allocation

After 1 May 2004, since the Czech Republic is part of the European Union, if a merger or acquisition has a 'Community dimension', generally the consequences for the Czech market will be decided in Brussels by the Commission.

In practice, this means that when multinational companies are making acquisitions which involve assets in the Czech Republic, they will no longer be thinking of parallel filings with the Commission and with the Office for the Protection of Competition (the 'Competition Office') (among others). Instead, they will be making one filing in Brussels, giving a 'one-stop-shop' clearance for what will then be 25 countries in the European Union and 28 countries, including the members of the European Economic Area (EEA).

It would be misleading to think that the Competition Office in Brno will not be involved at all in these cases, since the Office will participate in the EU Member States Advisory Committee which is part of the EC merger control procedure. Beyond this, there is often a degree of informal cooperation between the Commission and those Member States which have particular knowledge of relevant markets that are affected. The Commission can also refer Community dimension cases to the Competition Office in Brno for review under Czech law, if there are likely effects on a distinct Czech market. Under Council Regulation 139/2004, this can take place either before or after a notification is made to the Commission.⁴ The sorts of case under consideration here are those where the impact on competition is on a local market, eg where there might be a pipeline system in only part of a country or a localised supermarket or petrol station overlaps.

Nevertheless, this is a major change with rulings on competition in the Czech market being made in Brussels as part of the overall EU- or EEA-wide clearance.

After 1 May 2004, some also argue that the Czech market will be reviewed more often for two reasons: first, because information on Czech markets will have to be provided as part of the Commission filing even if they are not the focus of competitive

concern. Secondly, some argue that where there are many filings worldwide, some companies are reluctant to file in small jurisdictions unless there is a clear overlap and the parties have assets in that jurisdiction. This is hard to judge, but what is clear is that the issue should no longer arise after Czech entry to the European Union because compliance with EU filing requirements is more generally accepted. (Mainly, in view of its economical 'one-stop-shop' benefit in covering many countries at once and the seriousness of a failure to comply.)

In practice, it is likely that more merger cases will go to Brussels to be reviewed by the Commission simply because it may be easier to meet the Community dimension test in the EC Merger Control Regulation. It may be recalled that this can be done in two ways⁵:

- (1) The first involves an assessment of the worldwide turnover of both companies together and the EU-wide turnover of each undertaking involved separately. If certain thresholds are met and the two companies do not have more than 66 per cent of their turnover in the European Union in the same Member State then the case goes to the Commission.
- (2) The second involves looking at lower thresholds and the spread of impact across the Community resulting from the transaction. Again, the worldwide turnover of the companies together will be looked at (a lower figure than under the first rule) and then there will be a consideration of whether each company has more than a certain amount of EU turnover. In addition, there will be an examination of whether the parties have defined levels of turnover in at least three Member States together and separately.⁶

With 25 EU members, it is likely that more cases will meet these thresholds than was the case with only 15 EU members, whether one looks at the overall financial amounts or the point that in the second version of the Community dimension test, at least three Member States have to be affected.

In addition, from 1 May 2004, there is a new ability for companies to ask for a case to be dealt with by the Commission in Brussels if at least three national filings are required in the European Union.⁷ However, since we are dealing here with cases where the Community dimension test has *not* been met, the Member States in question can still object to central treatment of the case in Brussels and insist that the national filings be made, with local decisions in each case. It remains to be seen if this will be an attractive option to companies or

whether they will prefer to make the national filings in any event.

There will continue to be many merger cases dealt with at national level in the Competition Office. This will be where national procedures apply, under the level of the Community dimension test, if the national filing thresholds are met.⁸

Substantive tests

Turning to substantive review in merger control, there are two main points to emphasise. First, as one widens the geographical scope of the EU market, it may be expected that there will be more of a tendency to find lesser markets than the whole of the European Union. In particular, experience suggests that there may be some regional markets, whether combining parts of the 'old EU' with the 'new EU' (such as a market comprising Austria, the Czech Republic, Slovakia and Germany), or involving just the more Central European countries (eg perhaps Poland, Russia, the Baltic States, Slovakia, the Czech Republic and Germany).

Geographical market definition is therefore an area in which we will have to continue to be very careful in our assessments. It will not always be the case that regional (or national) markets will exist, because the countries that joined the European Union on 1 May are in many cases *already* part of a general European market. There may also be a dynamic tendency towards a full European market as the new acceding countries become more fully integrated with the old. However, the distances between, eg, Prague and Lisbon, and the differences between the various regions may speak to market differentiation in some cases.

Secondly, there may be some important substantive variations between EU and Czech merger control review. As of 1 May 2004, the Commission applies a new so-called 'SIEC test'. The letters SIEC stand for 'significant impediment to effective competition', in particular through the creation of single or collective dominance.⁹ The important point is that the new EC merger test is not only concerned with an assessment of dominance but can also include anti-competitive effects of non-coordinated behaviour of non-dominant companies.

The sort of issue which this is designed to address is where, eg, a merger involves the second and third players in a market whose products are close substitutes. Even though the merger may not result in single firm dominance, there could be the

creation or strengthening of a collective dominant position. Where the particular conditions for that do not apply¹⁰ and yet the acquisition will give the ability to players in the market *independently* to raise prices, it has been suggested that there is an anti-competitive effect against which the Commission should be able to intervene.

This is new, complex and controversial since the previous 'dominance' based test was fairly easy for companies to grasp and accept. The new, wider test may well lead to uncertainty as to which cases will be problematic, at least for a few years while the system is established. The SIEC test also extends the possible scope of the Commission's intervention in a way that many do not like. Nevertheless, from 1 May 2004, it is the EC legal standard.

The Czech review is somewhat simpler at present, in line with the position in most of the EU Member States. It focuses rather on an aspect that is included in the SIEC test but is narrower than this test. In other words, the issue is whether a merger or acquisition *creates or strengthens* a dominant position in the Czech Republic. In general, it will be interesting to see whether all the Member States choose to switch to the EC test in order to increase cohesion, or whether some will continue to apply the simpler dominance test.

Modernisation

For some years now, the Commission has been modernising the EC competition rules. What this means in practice is essentially two things:

- (1) The Commission has sought to focus on restrictions on competition by those with market power or involving more significant effects, with a greater emphasis on economic assessments than previously.
- (2) The Commission has been modernising its legislation to fit a system with no notifications for 'exemption', since from May 2004 this is abolished.

Block exemption 'ceilings'

The modernisation process has been reflected in amendments to the general block exemptions on issues such as vertical restraints and transfer of technology licensing, so that they are only available up to a certain market share 'ceilings'.¹¹ Generally, for vertical restraints, the ceiling is a 30 per cent share for the supplier on the market on which it sells the relevant goods or services. In the Commission's

new block exemption for technology transfer agreements, which entered into force on 1 May 2004, the ceilings are a 20 per cent share of the relevant technology or product market, held by the parties *together* in the case of licensing between competitors, and a 30 per cent market share held by either party in the case of licensing between non-competitors.

If agreements do not have certain so-called 'black-listed' or 'hard core' (serious) restrictions *and* the market shares of the parties concerned are under certain of these ceilings, then the block exemption can be relied on as a safe harbour for the legality of the relevant agreement and the restrictive clauses therein.

If, on the other hand, these market share ceilings are exceeded, a more specific review is required and the restrictions may have to be amended, above all to give further openings to the market. A recent example of this in Belgium involved the Interbrew company, which had to amend its beer supply contracts to various outlets so as to give more openings to the market.¹²

The overall theme is therefore clear: under modernisation there will be more limits to block exemptions where large market shares are involved and, above those exemptions, more specific and demanding assessments and solutions may be required. Against this, one may note that both the vertical restraints and technology transfer block exemptions should be wider in scope. This should leave the focus of enforcement in more relevant areas, ie the significant restrictions where there is market power.

Abolition of notification

The other main change associated with modernisation is the abolition of the notification system to the Commission.

For many years, it has been possible to review agreements and, if an agreement involves restrictions not covered by a block exemption, then, where a high level of legal certainty was sought, a notification could be made to the Commission seeking exemption under Article 83(3) EC. Such notification also gives immunity against fines for the practices concerned. The idea of notification was then to obtain a full exemption decision, stating that a restrictive agreement or practice was lawful for a stated time, or at least a so-called 'comfort letter' indicating that the Commission had no objection to the restrictions concerned.

On 1 May 2004, this changed dramatically insofar as such notifications are no longer possible.

Companies are not able to obtain immunity in this way, nor decisions of this type and will have to assess for themselves whether their agreements can be justified. They will also have to be prepared to defend their assessments before the Commission, national competition authorities and in the national courts.

The Commission has indicated that it is prepared to give informal guidance in the form of a written statement (so-called 'guidance letters') with regard to novel questions and has issued a notice on this practice.¹⁵ However, this is not meant to be notification 'by the back door'. The procedure is meant to apply to 'genuinely unresolved' questions and therefore to be of limited application.

The focus on *economic* assessments is therefore generally welcome. However, it has been at a price in terms of legal certainty. The introduction of more market share ceilings to block exemptions means that there is more insecurity for companies as to the solutions required across Europe. For example, if the relevant market for supply of a product is European, then one approach can be taken for Europe as a whole. If, on the other hand, there are national or regional markets with variations in market positions and market power, then corresponding variations may be required to the agreements to reflect these factual variations. There may also still be national notification requirements, although it is understood that the proposed amendment to Czech law will remove this.

There may also be more insecurity insofar as there will no longer be exemptions for a given period of time. It remains to be seen for how long clearance decisions will be effective, given the risk that plaintiffs may seek their review and may not be clearly prevented from doing so as with a formal exemption decision.

In general, with the abolition of the notification system, it is expected that the Commission will be more active with investigations started on its own initiative, whether into specific practices or on a sectoral basis. It will be interesting to see if the Competition Office takes a similar approach if the notification system is removed, giving the Office a greater ability to define its investigating priorities.

Decentralisation

Decentralisation is also a dramatic change in the way that the competition rules are enforced.

Application of Article 81(3) EC by national competition authorities and courts

For years we have been used to the idea that Article 81(3) EC can only be applied by the Commission. When Council Regulation 1/2003 entered into force on 1 May 2004, together with the principles of direct effect of Articles 81 and 82 EC, for the first time national competition authorities such as the Competition Office, the Commission and any national court are able to rule on Article 81(3) EC.

This is an issue of great interest, because it may well lead national competition authorities to be more active in targeting restrictions that they did not look at before. Many national competition authorities used to look only at restrictions with clear national effect, not affecting trade between EU Member States, partly for jurisdictional reasons and partly because they only had exemption powers under their national laws, not EC law. This now changes so they may be active on a wider range of restrictions.

However, there is also some trepidation because it is thought that Article 81(3) EC involves a complex economic assessment. As a result, many practitioners are pushing for specialised national competition courts. Without any criticism of ordinary judges, it is simply thought that procedures will be more effective (and cheaper) if the judges involved are more regularly concerned with such economic assessments. At the moment, these issues could arise in front of any court, however low it is in the overall hierarchy and (almost) no matter what is the court's daily work, since competition issues can have a wide reach.

Otherwise, practitioners are thinking that the advice required of them after this change may also have to be somewhat different. Until now the tendency has been to assess closely the enforcement practice of the Commission in a certain field and to have a very focused understanding as to what is likely to be allowed or not. Such assessments may be more difficult in the future, if the test is whether any competition authority or court dealing with the case would find an infringement or would be likely to apply Article 81(3) EC. It is likely to be a more general assessment than taking a view on whether Brno or Brussels would accept a certain situation in the circumstances.

Nevertheless, the Commission will still be key on the big issues, for the declaratory decisions (which only it can take and which are specifically designed to clarify the position on certain types of new or

important practice¹⁴) and also because of the principles confirmed in the European Court's *Masterfoods* judgment.¹⁵ In short, this judgment requires that national authorities and courts must not take decisions which run counter to a Commission decision or are likely to run counter to a Commission decision in proceedings on the same issue or matter. Moreover, if a national competition authority were not to follow agreed EC competition law, it appears that the Commission could pull a case to Brussels¹⁶ (although clearly that is likely to be the exception and would be no doubt controversial).

Enforcement coordination

Under Regulation 1/2003, there are structures for coordination between the Commission and the national competition authorities involving the transfer of cases and related files and the exchange of confidential information.¹⁷ All this is very radical when one looks back at how little was allowed before,¹⁸ but clearly it is essential if there is to be an adequately cohesive, yet decentralised enforcement system.

Similarly, there are parallel but different cooperation procedures as regards the Commission and the national courts.¹⁹ The Commission is informed of judgments involving competition issues and can provide written observations in some circumstances, as can the national competition authority, in this case the Competition Office in Brno. If a court allows it, representatives of the Commission may also act as a form of *amicus curiae* in explaining orally how the principles of competition law may apply to a given dispute.

The enforcement concept is one of a European Competition Network (ECN), with the Commission at the centre, but national competition authorities fully involved. Again, one can only say how dramatically this has all changed in recent years. Not that long ago there were few competition authorities in the European Union and only some of those, such as the Bundeskartellamt in Germany, were very active. Now, there are important and effective competition authorities in many EU Member States, taking many decisions, producing new thinking on issues and influencing Brussels and each other in the process.

After 1 May 2004, a competition case can be dealt with in Brno or Brussels or handled by several national competition authorities or arise before a national court.

According to the principles of work-sharing in the notice on cooperation between the Commission and national competition authorities, it is likely that those cases with their main competitive impact in the Czech Republic will be dealt with by the Competition Office, since the Office in the Czech Republic should be best placed to deal with them, unless a special principle or precedent is involved, in which case the matter may be dealt with by the Commission.

On the other hand, if three or more EU Member States are affected by a restriction, the case is likely to be handled in Brussels. In between, there may be joint action by national competition authorities. This may become a developing area. For example, it may be of interest to note that the Nordic competition authorities often appear to work together and have signed an official agreement on such procedures. It may be that in the years to come interventions by, eg, the Austrian and Czech authorities or the Czech and Slovak authorities together should be expected.

Under the new decentralised system, the Czech authorities, whether the Competition Office in Brno or national courts, *must* apply EC competition law if there is an effect on trade between Member States. This concept is interpreted very widely, so that in practice the application of EC competition law may often occur.

This process should also have a harmonising effect on national competition law, since the scope for applying EC law is very wide and, where EC and national competition law is applied in parallel, on Article 81 EC issues there should be no divergent outcomes. (However, Member States can apply stricter rules on dominance issues.²⁰)

If the national courts are uncertain as to the interpretation of EC competition law, they can always refer a question to the European Court of Justice in Luxembourg.

Finally, it should be emphasised that in applying EC competition law, the Czech authorities will follow the *Czech* procedural rules.

Accession/enlargement

Commission investigations

After 1 May 2004, as a result of Czech entry into the European Union, the Commission is able to intervene directly in the Czech Republic, with so-called 'dawn raids', usually meaning inspections on company premises and new powers to carry out such

inspections, even in private homes.²¹ Clearly this is controversial, but reflects concerns about cartel documents being kept at home. One may think that the Commission will only use this right to enter private homes in very clear cases and there are various restrictions on it doing so.

However, the point is clear that after 1 May 2004 the Commission *is* able to carry out such investigations on Czech soil. (It is understood that there is also an amendment proposed to the Czech competition law to give the Competition Office similar powers.)

Likely enforcement priorities

In general, there are likely to be some interventions by the Commission in the early years but not too many. The ECN involves a concept of decentralisation of enforcement that should mean that the Commission would leave much to the Competition Office. The Commission may also allow some time for transition on Czech entry to the European Union.

However, this may not apply if there are big issues at stake or major complaints. As a practical matter, it would not be surprising to see the Commission intervene if it saw companies which it thought should know better, since they are operating extensively in the 'old European Union', infringing the rules in the 'new EU' Member States. Clearly, sooner or later the Commission will be keen to ensure that the message has got through that full compliance with the EC competition rules in the new accession states is also required.

It is also important to realise that there should be more focus on restrictions on trade and competition between the Czech Republic and the other accession countries and on restrictions between the Czech Republic and the old 15 EU Member States. Until May 2004, there was a possibility to address the latter restrictions under the Europe Agreement.²² However, in practice it is thought that this provision was little used. Now we expect such restrictions to be more directly addressed.

A focus on the more serious restrictions can also be expected, in other words cartels, restrictions on parallel imports, collective action to hinder foreign entry and the former monopolies and oligopolies that came about through privatisation and still hold dominant positions.

This will give new remedies to companies against restrictions in the Czech Republic, or the 'old EU' Member States, or the 'new EU' Member States. In

other words, if Czech companies find that it is difficult to obtain access to some of the existing markets of the European Union, or in other accession countries, they will now have at least three ways in which they can tackle the issue: they can go to the Commission in Brussels and complain, or they can go to the Competition Office in Brno and complain, or they can go before the national courts.

State aid

Finally, there will be major issues on state aid after accession. There are already a number of cases running concerning pre-accession aid where it is argued that the aid will have effects after accession which can and should be reviewed (eg the current Czech banking cases).²⁵ After accession, enforcement of the state aid rules is in Brussels with the Commission. All new aid is also to be subject to Brussels review. It is understood that the Competition Office in Brno will retain a monitoring role as regards state aid, but will no longer take actual decisions in relation thereto.

Conclusion

All this adds up to a tremendous amount of change on 1 May 2004. It may lead to a fair amount of uncertainty and turmoil as people adapt to the new system. However, it is undoubtedly a necessary evolution given the new scale of the enlarged European Union and an exciting and welcome prospect.

The key for those in the Czech Republic (and the other countries joining the European Union) is to remember the sort of advice which various 'old EU' Member States have given to their companies during the evolution of the Common Market, above all in 1992, ie to take advantage of the EU market and be active in it, since it *is* a market. If you do not and others compete harder, you may suffer. If you do take part, it provides a great opportunity.

Finally, EC competition law has become more modern, giving plenty of scope for arguments to justify business practices driven by valid concerns. It is only as regards the classic infringements that enforcement has become tougher. In short, one should not assume too quickly that restrictive practices are unlawful. Often there are justifications that can be put forward to persuade the authorities to allow them. ■

Notes

- * This article is based on a paper given at the Conference on 'The Implementation of European case-law in the Czech Legal Order', on 11 March 2004, Prague, organised by EMP in cooperation with the Hugo Grotius Foundation, and the Chamber of Commerce of the Czech Republic.
- 1 Council Regulation 139/2004, OJ 2004 L 24/1.
- 2 OJ 2003 L 1/1.
- 3 Cyprus, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia, Slovenia and the Czech Republic.
- 4 Council Regulation 139/2004, Arts 4 and 9.
- 5 See, generally, Wilmer Cutler Pickering LLP's Guide to the EC Merger Control Regulation, 2001 (new edition under preparation), and Commission Press Release IP/04/70 and MEMO/04/9, 'New Merger Regulation frequently asked questions' both dated January 2004, available on the European Commission's website, www.europa.eu.int.
- 6 The first test requires €5 billion worldwide turnover of the parties together and €250 million EU-wide turnover for each separately; the second test requires €2,500 million worldwide turnover together, €100 million EU-wide turnover for each separately and then that both parties have more than €100 million turnover together in three Member States, with a minimum of €25 million each in those three Member States.
- 7 Article 4(5) of Council Regulation 149/2004.
- 8 It is understood that these thresholds are being reviewed and may be raised; see further the Competition Office's website, www.compet.cz.
- 9 Article 2(2) and (3) of Council Regulation 139/2004 and recitals (24) to (26) thereto.
- 10 Case T-342/99, *Airtours v Commission* [2002] ECR II-2585, available on the website of the European Court of Justice, www.europa.eu.int/cj.
- 11 See Commission Regulation 2790/1999 on Vertical Restraints, OJ 1999 L 336/21 and the related 'Vertical Guidelines' at OJ 2000 C 29/1; and the New Block Exemption on Technology Transfer Agreements and related 'IP Guidelines', adopted on 7 April 2004 and available on the European Commission's website, http://europa.eu.int/comm/competition/index_en.html, together with Commission Press Release IP/04/470.
- 12 See OJ 2002 C 283/14 and Commission Press Release IP/03/545, 15 April 2003, available on the European Commission's website.
- 13 See Commission Press Release IP/04/411, 30 March 2004, and the texts available on the European Commission's website for the various notices related to decentralisation. For a summary of the draft notices, including that for Art 81(3) EC, see Ratliff, 'Major Events and Policy Issues in EC Competition Law, 2002-03' [2003] *International Company and Commercial Law Review* 19 at 25-32. The texts are available on the Commission's website.
- 14 Article 10 of Council Regulation 1/2003.
- 15 Case C-344/98, [2000] ECR I-1369, available on the European Court of Justice website.
- 16 See Art 11(6) of Council Regulation 1/2003.
- 17 Articles 11-14 of Council Regulation 1/2003.
- 18 See, for example, the '*Spanish Banks*' case, Case 67/91, [1992] ECR I-4785.
- 19 Article 15 of Council Regulation 1/2003.
- 20 Article 3 of Council Regulation 1/2003.
- 21 Article 21 of Council Regulation 1/2003.
- 22 Article 64, OJ 1994 L 360/1.
- 23 See Commission Press Releases, IP/03/1791, 19 December 2003 and IP/04/115, 28 January 2003, available on the Commission's website.