

News brief



EU modernisation reforms

Shaking the competition

On 1 May 2004, and coinciding with the expansion of the EU from 15 to 25 member states, the EU's competition law framework will change fundamentally. Regulation 1/2003 will devolve full competition law powers to the national competition authorities (NCAs) and courts, shifting activity from the EU's centre to the member states (www.practicallaw.com/A28129). The European Commission (the Commission) and the NCAs, with their new powers, will move from a process of prior clearance of agreements to retrospective enforcement of competition law.

For those who notified deals to the Commission to obtain comfort and clarity, particularly a party to a complex and cutting edge transaction, the removal of the safety net of immunity and regulatory approval will raise real and deep concerns. Parties will be left exposed to fines, unenforceable agreements and damages claims. Egregious behaviour could risk disqualification for directors.

The current system

The relevant substantive law is (and will remain) in Article 81 of the EC Treaty. Article 81(1) prohibits agreements between undertakings or associations of undertakings that have the object or effect of the prevention, restriction or distortion of competition. Such agreements are void and the parties may face fines of up to 10% of worldwide turnover and damages claims. Article 81(3), however, provides that Article 81(1) will not apply to agreements where the technical and economic benefits outweigh the detriments arising from the agreement in such

a way that there is a net benefit to society, and where consumers (not merely end consumers) get a fair share of the benefits. It only allows restraints that are indispensable to the agreement. This is a policy, fact and economics driven analysis.

In order to obtain the benefit of an Article 81(3) exemption, an undertaking has to notify the relevant agreement to the Commission or fall within one of the block exemption regulations that specify terms on which agreements will be treated as satisfying Article 81(3). National courts and some NCAs may apply Article 81(1) to strike down an agreement; they cannot apply Article 81(3) to save it. They generally defer to Commission decisions and are bound by Article 81(3) decisions.

In practice, the Commission was swamped with notifications. Exemptions have rarely been granted (and have been limited to agreements that contain a point of principle, are of economic importance or help the development of competition law) and have taken years.

Most notifications have been terminated by "comfort" letters. These usually indicate that, on the basis of the information provided to the Commission, the Commission intends to take no further action, but reserves its rights to re-open the case should circumstances change. Although comfort letters are not formally binding on national courts and provide no legal guarantee, it is unlikely that a national court would reach a different conclusion to the Commission.

The new system

From 1 May 2004:

- There will be no process of exempting agreements by the Commission and Regulation 1/2003 does not enable member states to exempt. (In the UK, the Office of Fair Trading is proposing to follow suit and remove the (little used) notification procedure from the Competition Act 1988.)

The changes assume that, as the principles on which Article 81(3) exemptions are granted should by now be sufficiently clear, the costs of notification outweigh the benefits and so it is no longer required. Companies are to take specialist advice and stay prudent.

- The Commission will retain the right to take a formal decision finding that Article 81 is "inapplicable ... where the Community public interest requires" it to do so. This is a reserve power, to be used sparingly on policy grounds. (NCAs are not prohibited from issuing such statements, however.)
- The power to consider whether Article 81(3) operates will be devolved to NCAs and the national courts. However, given the proposed absence of any notification system, the power will only be exercised when an NCA investigates, or a national court considers, the agreement or practice after the event. The burden of proof will be on the parties wishing to claim the exemption to establish that the agree-

ment satisfies Article 81(3). Standards of proof are for member states to determine.

(See also box "Key features".)

Issues for business

Three key issues arise from modernisation:

Onus on the parties. In the substantial number of cases where agreements fall within block exemptions, nothing will change. For those agreements outside the block exemptions, the parties will need to assess whether their agreement satisfies Article 81(3) and will bear the risks of error. This is already an issue because notifications filed today will not be determined before 1 May 2004 (unless they raise an exceptional issue of principle). As from 1 May 2004, outstanding applications would lapse.

An assessment as to whether the agreement satisfies the criteria within Article 81(3) can often be undertaken with some certainty. However, difficulties lie with innovative or complex agreements, particularly horizontal arrangements (those between undertakings at same stage in the distribution channel). These would previously have been notified, and their exemption or comfort negotiated and obtained. The consequences of their being undermined during their life, both as regards enforceability and damages, could be severe.

Article 81(3) contains subtle and imprecise concepts which have policy connotations. The courts, in particular, are likely to have difficulties in assessing identifiable technical and economic benefits and balancing them against the specific need for the restriction of competition to achieve those benefits, and whether they are fairly shared with consumers. To date, parties have sometimes pushed the boundaries in such circumstances, reassured that they could remove or weaken unnecessary but attractive restrictions to obtain clearance (provided they were comfortable that there was no damages or enforceability risk).

Key features

Notification to the European Commission, and associated immunity from fines, will be abolished.

Article 81(3) of the EC Treaty can be applied by national bodies to relieve agreements falling under Article 81(1).

Member states must have the power to impose fines for breaches of Articles 81 and 82.

The Commission will have increased investigatory powers to police cartels, including the power to search private homes and conduct interviews.

More information will be exchanged between the Commission and between the national competition authorities.

The process could be managed more delicately.

Post Regulation 1/2003, erring on any of these assessments could invalidate the whole agreement and expose the parties to fines and damages claims. Even if the void parts of the agreement are severable so that the remainder is saved, it may produce a very different commercial relationship between the parties.

Timing for consideration of Article 81(3) criteria. Currently, the Commission examines, on notification, the future competitive impact of the agreement and overall benefits across its term. If the Commission considers that the agreement meets the Article 81(3) criteria, it authorises the agreement for a specified period, and it is then effectively protected (unless the Commission (very rarely) uses its reserve powers). The critical point is that this has been a forward-looking process weighing possible future risks and outcomes and assessing the agreement as a whole.

Now, an agreement will be assessed at the point in time at which it is challenged or investigated but it is unclear if the tests will be applied as at that time or as at the date of the agreement. It may well be that a long-term agreement would have qualified for exemption at the time it was entered into (on a forward-looking assessment) but, some of the various risks

having crystallised, or the competitive or the technical environment having changed, would fail if assessed on tests applied midway through the process. Will agreements be more vulnerable because the assessment becomes, in practice, an ongoing snapshot of the then current competition environment; or will the courts and local regulators go through the artificial exercise of applying a test as at the date of the agreement and ignoring subsequent events? Whatever the legal position adopted, the position is going to be very different presentationally.

Forum shopping. The new regime opens enforcement up to 25 jurisdictions. Procedures, enforcement standards and, perhaps, the practical application and interpretation of EC law (whatever the theoretical position) will vary across the wider Europe. Despite the procedures proposed for co-ordination (which are not yet fully worked out), this opens enormous possibilities for selection of jurisdiction, particularly by aggressive claimants attacking allegedly infringing operations across multiple jurisdictions. There is no one-stop shop any more.

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