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A Departure from a Formalistic Approach in the Assessment of Restrictive Vertical Agreements in Favour of a More Economics-Based Approach? Case Comment to the Supreme Court Judgment of 15 May 2014 (Ref. No. III SK 44/13)

by

Małgorzata Sieradzka*

I. Background information

The discussed judgment of the Supreme Court is in line with its other jurisprudence with respect to the classification of price agreements as practices restricting competition under Article 6(1)(1) of the Competition and Consumer Protection Act[1] of 16 February 2007 (hereafter: Competition Act 2007). Despite the firm stance taken on the assessment of price agreements by the UOKiK President, the Supreme Court once again emphasizes the necessity for an economics-based approach[2]. In the opinion of the Supreme Court, not every vertical price-fixing agreement results in a threat to the public interest. A departure from a rigorous application of the ban on competition restricting practices (Article 6(1)(1) of Competition Act 2007) to all types of vertical agreements has an impact on the application of legal provisions governing the imposition of financial penalties. Considering the optional nature of fines, the question arises about their purpose in cases where the public interest has not been jeopardized.

II. Facts

In the decision of 11 December 2008 (No. RKT-114/2008), the UOKiK President found a vertical agreement concluded by Zakłady Chemiczne Hajduki S.A. and several undertakings operating in the wholesale market of paints, varnishes and auxiliary

* Dr. Małgorzata Sieradzka, advocate, Lazarski University, Warsaw, Poland; malgorzata.sieradzka@lazarski.pl.

[1] Journal of Laws No. 50, item 331 as amended.

[2] In a previous judgment of 23 November 2011 in Case *Röben*, Ref. No. III SK 21/11.

products, as a competition restricting practice. The agreement consisted of the direct fixing of sales prices of products manufactured by Hajduki and sold by the contractors. By the decision, the UOKiK President imposed a fine on both Hajduki and on the other participants of the agreement.

The claimant, V – Sp. z o. o. (one of the undertakings participating in the agreement), contested the decision of the UOKiK President before the Court of Competition and Consumer Protection (in Polish: *Sąd Ochrony Konkurencji i Konsumenta*; hereafter, SOKiK). The appeal was however dismissed by SOKiK in the judgment of 11 October 2011. The 1st instance judgment was once again challenged by the claimant this time before the Court of Appeals. This appeal was partially accepted in that the Court of Appeals significantly reduced the amount of the original fine. In turn, the UOKiK President filed a last resort appeal (cassation) against the ruling of the Court of Appeals with the Supreme Court. The Supreme Court dismissed the appeal of the UOKiK President in the reviewed judgment of 15 May 2014.

III. The Supreme Court's ruling

The Supreme Court found no grounds for consideration of the cassation appeal lodged by the UOKiK President. In the judgement discussed, the Supreme Court did not classify the agreements involving minimum or fixed resale prices as agreements restricting competition 'by object' in the meaning of Article 6(1) of Competition Act 2007, but instead, referred to its own views expressed on this matter in the *Röben* judgment of 23 November 2011 (III SK 21/11). The Supreme Court confirmed its earlier findings and upheld the general principle on the classification of agreements setting minimum or fixed resale prices (also derived resale prices, such as margin levels) as falling into the category of agreements restricting competition 'by object' (pursuant to Article 6(1) first sentence of the Competition Act 2007).

The Supreme Court did not share the view of the UOKiK President which extended the prohibition to all vertical price agreements because of their anti-competitive object. Application of the ban contained in Article 6(1) of Competition Act 2007 to all types of price-fixing vertical agreements should be regarded as a formalistic approach. It should be borne in mind that in case of brand competition a positive effect of vertical agreements competition can be observed. According to the Supreme Court, a rigorous application of the prohibition of Article 6(1(1)) of Competition Act 2007 is not justified.

The Supreme Court rightly pointed out that not every agreement belonging to this category threatens the public interest, or infringes values important to antitrust law; or that there always is a need to impose a financial penalty. Any assessment of restrictive vertical agreements must be flexible and must take into consideration the object of such agreements and a threat to or violation of the public interest.

The Supreme Court's ruling must be welcomed for two reasons: first, without questioning the past decision-making practice of the UOKiK President and existing jurisprudence on classifying price agreements as those restricting competition by

object, the Supreme Court took account of the necessity to examine whether an agreement may threaten the public interest. Second, if the protected values are, in fact, not infringed, one has to consider whether the imposition of a penalty is justified at all (rationality of the imposition of sanctions – author's note), and if so, whether it should not be reduced (proportionality of the sanction – author's note)[3].

IV. Case analysis

Price-fixing agreements, referred to in Article 6(1(1)) of Competition Act 2007, can be horizontal or vertical in nature (distinction between the two is commonly adopted in case-law and literature but not reflected in the Competition Act). Horizontal agreements involve competitors and as such are deemed to constitute the most serious threat to competition (severest distortions of competition are called hard-core restraints). Conversely, vertical agreements, concluded between non-competitors, are recognized as less harmful to competition. In circumstances such as those at hand, a vertical price agreement was concluded between entrepreneurs operating at different levels of the supply chain – the supplier and its distributors – with resale prices being the object of the agreement.

The analysis of the case law of the UOKiK President shows that the Polish antitrust authority does not consider relevant the actual form (horizontal or vertical) of a price agreement. Instead, the authority mainly focuses on the circumstances in which the agreement was concluded and its actual implementation. The Supreme Court in its judgment emphasized, however, the necessity to depart from such an inflexible approach to the classification of vertical price agreements as restricting competition. Differentiating the status of price agreements will justify a variation in their legal classification.

1. Vertical price agreements vs infringements of the public interest

Vertical price agreements (setting minimum or fixed resale prices) are classified as competition restricting agreements due to their anti-competitive object, in other words, they are seen as containing hard-core restrictions. Views that consider vertical price agreements to be prohibited due to their anti-competitive effect remain in a small minority.

The Supreme Court stated in its judgment that it might be necessary to deal with agreements that are not intended to infringe the public interest pursuant to Article 6(1(1)) of Competition Act 2007. Public interest is endangered when practices are meant to restrict the creation or development of market competition[4]. If anticompetitive

[3] Reference to infringements of the public interest is more often noted in court rulings – see judgment of the Court of Appeals in Warsaw of 5 November in Case VI ACa 160/13.

[4] Judgment of 21 March 2005, XVII Ama 16/04, Journal of the Competition and Consumer Protection Office [2005] No. 2, item 27.

practices result in an infringement of the public interest, then the premise has to be dealt with of public enforcement of competition law. A threat to, or an infringement of the public interest, is the pre-requisite for public enforcement of competition law – its absence excludes an intervention by the antitrust authority. Not every agreement in the category of vertical price agreements threatens to, or in fact infringes, the public interest. The Supreme Court's position should be viewed as 'a green light' that the assessment of vertical agreements should not exclude their economic aspects, which are to be taken into account with regard to this type of vertical agreements[5].

2. Vertical price agreements – object or effect category?

It is worth recalling that the Supreme Court upheld in the analysed judgment its established general principle on the classification of agreements that set minimum or fixed resale prices (as well as resale price derivatives) as falling into the category of practices which restrict competition by their object[6]. Differences between horizontal and vertical price fixing agreements are shown above. It should be stressed here that an agreement's classification has an impact on the evidentiary procedure held before the UOKiK President. In the light of Article 6(1)(1) of Competition Act 2007, the anticompetitive aspect of an agreement is mirrored in its anticompetitive object or effect. The classification of an agreement by the antitrust authority as restrictive by object influences proceedings before the UOKiK President. The burden of proving an agreement's present or future anti-competitive effects rests on the authority. Acknowledging, therefore, the view that vertical price agreements may belong to the category of anti-competitive agreements, because of their anticompetitive effect, entails the necessity to examine their effects. The occurrence of anti-competitive effects of a vertical price agreement must thus be proved by the antitrust authority.

3. Vertical agreements and the *de minimis* rule

The Supreme Court pointed out that the classification of vertical agreements as agreements restricting competition by their object does not justify the rigorous application of the prohibition contained in Article 6(1(1)) of Competition Act 2007 to all agreements of this type. To this end, it is worth repeating that the *de minimis*

[5] The necessity to include among others the market conditions is pointed out by A. Jurkowska-Gomułka, ‚Stosowanie zakazu porozumień ograniczających konkurencję zorientowane na ocenę skutków ekonomicznych? Uwagi na tle praktyki decyzyjnej Prezesa Urzędu Ochrony Konkurencji i Konsumentów w odniesieniu do ustawy o ochronie konkurencji i konsumentów z 2007 roku' [‚Effects-Oriented Application of the Prohibition of Competition Restricting Agreements? Some Comments on the Decisions Issued by the Polish Competition Authority on the Basis of the Competition Act of 2007'] (2012) 1(1) *internetowy Kwartalnik Antymonopolowy i Regulacyjny* 45–47.

[6] Anti-competitive object of agreements – see judgment of 17 July 1997 in Case C-219/95 *P Ferriere Nord SpA v Commission of the European Communities* [1997] ECR I-4411; judgment of 6 April 2006 in Case C-551/03 *P General Motors BV v. Commission* [2006] ECR I-3173.

exemption from the prohibition on restrictive agreements[7] under Article 7(1) of Competition Act 2007 applies to agreements concluded between: 1) competitors, whose combined market share in the calendar year preceding the conclusion of the agreement at stake does not exceed 5% (horizontal agreements); 2) entrepreneurs, who are not competitors, if the market share of any of them in the calendar year preceding the conclusion of the agreement does not exceed 10% (vertical agreements). The *de minimis* rule applies to those agreements, which due to the low market share of their participants, affect competition in the relevant market only slightly[8]. The *de minimis* exemption does not apply to agreements which are particularly detrimental to competition. It does not apply, inter alia, to price agreements and other terms of sale (defined in Article 6(1)(1) of Competition Act 2007). The aforementioned agreements are prohibited irrespective of the market share of their parties.

Having regard to the fact that the *de minimis* exemption applies to a certain category of arrangements (e.g. price, quotas), their object or effect is not taken into account in their examination.

In view of the analyzed judgment, in which the Supreme Court stressed the need for an individual approach to the agreements that set minimum or fixed resale prices, and thus the necessity to identify their true purpose, it is worth mentioning the features of concerted practices[9], namely:

1) the manner in which they manifest themselves;
2) objective target of the concerted practice, that is, the aim participants intend to achieve and the economic and legal context in which such practices occur;
3) various forms[10];

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[7] Called 'prohibition relativization' by T. Skoczny; see T. Skoczny, 'Instrumenty relatywizacji i racjonalizacji zakazów praktyk ograniczających konkurencję' ['Instruments of relativization and rationalization of the bans on competition restricting practices'] [in:] *Granice wolności gospodarczej w systemie społecznej gospodarki rynkowej – księga jubileuszowa z okazji 40-lecia pracy naukowej prof. dr. hab. Jana Grabowskiego* [*The limits of economic freedom in the social market economy – a jubilee book on the 40th anniversary of scientific work of Prof. Jan Grabowski*], Katowice 2004, p. 249ff; see also in this regard D. Miąsik [in:] T. Skoczny (ed.), *Ustawa o ochronie konkurencji i konsumentów* [*Competition and Consumer Protection Act*], Warszawa 2009, p. 453.

[8] T. Skoczny, [in:] T. Skoczny (ed.), *Ustawa*..., p. 436; K. Kohutek, [in:] K. Kohutek, M. Sieradzka, *Ustawa o ochronie konkurencji i konsumentów* [*Competition and Consumer Protection Act*], Warszawa 2008, p. 296; P. Grabowski, ‚Zasada de minimis w nowych wyjaśnieniach Komisji Europejskiej i polskiej ustawie antymonopolowej' (‚The de minimis rule in the new guidelines of the European Commission and in the Polish antimonopoly act'] (2003) 3 *Przegląd Prawa Handlowego* 26.

[9] See Case 56/65 *Societe Technique Mniere v. Machinesbau Uln GmbH* [1966] ECR 235; Case 15/74 *Centrafarm &Peijper v. Sterling Drug* [1974] ECR 1147; Case 48/69 *Imperial Chemical Industries Ltd. V. Komisji* [1972] ECR 16.

[10] See decision of the UOKiK President of 8 December 2009, 7/2009, Journal of the Competition and Consumer Protection Office [2010] No. 1, item 1.

4) object or effect of the agreement, from which a distinction between an infringement by object and an infringement by effect can be made[11].

Although the Competition Act 2007 does not provide a distinction between horizontal and vertical agreements[12], yet such differentiation should be taken into account in the assessment of agreements in the light of Article 6(1(1)) of the Competition Act 2007. The *de minimis* exemption does not apply to price agreements. However, the legislator did not define precisely whether such agreements restrict competition by object or by effect. Considering the above, it must be assumed that Article 6(1(1)) allows for the differentiation of anti-competitive agreements on the basis of their nature (horizontal vs vertical). It does not, however, determine whether a certain type of agreement should be classified as an agreement with the object to restrict competition or an agreement the effects of which may restrict competition[13].

4. Criteria for setting fines

According to Article 106(1)(1) of the Competition Act 2007, the UOKiK President may impose, by way of a decision, a fine on an undertaking not exceeding 10% of the revenue earned in the accounting year preceding the year when the fine is imposed. This is so even if the undertaking has unintentionally infringed the prohibition laid down in Article 6 of the Competition Act 2007, as regards the scope not exempted by Articles 7 and 8 thereof. Thus the decision imposing a financial penalty is optional in nature. Nevertheless, the imposition of fines has become a general rule in order to ensure the effectiveness of the UOKiK President's sanctioning policy.

The Competition Act 2007 does not provide an exhaustive catalogue of grounds on the basis of which the amount of the fine to be imposed is determined. Article 111 only provides that setting the amount of the fines, referred to, *inter alia* in Article 106 (including also those for vertical price agreements – note by the author), requires certain factors to be taken into consideration in particular. They include: the duration, gravity and circumstances of the infringement of the provisions of the Competition Act as well as previous infringements[14]. It is apparent that the amount of the fine to be imposed should depend on the level of the competition threat and the infringement of public law resulting from the competition restricting practices. Doctrine emphasizes, with regard to the imposition of fines for competition restricting practices, the necessity to take into consideration factors such as: the undertaking's economic potential, the

[11] M. Sieradzka, 'Glosa do wyroku TS of 04.06.2009 C-8/08 *T-Mobile Netherlands BV and others v. Raad van bestuur van de Nederlandse Mededingingsautoriteit*' ['Case comment to ECJ judgment C-8/08 *T-Mobile Netherlands BV and others v. Raad van bestuur van de Nederlandse Mededingingsautoriteit*'] (2010) 2 *Glosa* 97.

[12] A. Jurkowska, [in:] T. Skoczny (ed.), *Ustawa*..., p. 386.

[13] ibid. see K. Kohutek, 'Glosa do wyroku SN of 15 May 2014, Case III SK 44/13' ['Case comment to the judgment of the Supreme Court of 15 May 2014'], LEX/el.

[14] In-depth analysis of penalty mitigation – see M. Sieradzka, 'The importance of 'subjective fault' in fixing pecuniary penalties for competition-restricting practices (Part I)' (2013) 12 *Przegląd Ustawodawstwa Gospodarczego*.

impact of the practice on competitors or contractors, admissible fine levels under provisions of the Competition Act and the purpose the fine is to serve[15].

The amount of fines for the infringement of Article 6 of the Competition Act 2007 is calculated as a percentage of the undertaking's turnover. In the case in question, an objection was raised with regard to an infringement of Article 106(1)(1) in conjunction with Article 6(1)(1). The objection noted that unreasonable consideration was given to the revenue generated from the price agreement, as the main criterion for setting the amount of the fine.

Can the amount of a fine be measured by a certain percentage of the undertaking's revenue where the revenues from product sales covered by the anticompetitive agreement constitute a small percentage of its total income?

Before giving an answer to the above question, it should be stressed that any penalty imposed should serve its purposes. The imposition of fines is an instrument designed to facilitate compliance with the provisions of the Competition Act as well as prevent future infringements[16]. Penalties are applied with various aims – prevention being the most important of them. A penalty serves a dual function: it should have an effect on all addresses of a legal norm and it should protect consumers against re-offences. The preventive function applies also to professional trading participants and its purpose is to deter undertakings from unlawful behaviour as well as to strengthen awareness of anticompetitive behaviour of law-abiding businesses[17]'. A penalty as a repressive measure applies to the penalized undertakings – for them, the penalty should be onerous[18]. The constitutional principle of proportionality in relation to the setting of fines requires the UOKiK President, who exercises his/her discretional powers here, to inflict sanctions the severity of which cannot go beyond the limits of their intended purpose[19]. EU case law also emphasizes that the principle of proportionality demands that the limits of what is appropriate and indispensable for achieving the legitimate objectives pursued by respective regulations should not be exceeded. Where there is a choice between several appropriate measures, the least onerous one should be applied; the resulting inconveniences cannot be disproportionate to the goal pursued[20].

Would a reduction in the penalty by the Court of Appeal, in the light of the facts established, prevent the penalty's purpose from being achieved?

It is worth noting first that an imposed penalty is to ensure the realization of certain functions of penalties and be proportionate to the magnitude of the infringement.

Analyzing the facts of the case, it can be said that fine setting criteria were properly applied by the Court of Appeals. In particular, the fine inflicted (its amount) served its purpose of a repressive (inconvenience for violating competition law) as well as preventive and disciplinary measure (dissuades future violations). Making a decision

[15] M. Sachajko, [in:] T. Skoczny (ed.), *Ustawa…*, p. 170.

[16] Judgement of the Supreme Court of 24 September 2010, VI ACa 117/10, Lex no. 684113.

[17] Judgment of SOKiK of 7 January 2014, XVII Ama 1/12.

[18] Judgement of SOKiK of 30 October 2013, Case XVII Ama 35/12.

[19] Judgment of the Court of Appeals in Warsaw of 28 June 2012, VI ACa 1379/11.

[20] Judgment of 11 September 2014 in Case C-382/12 P *Mastercard Inc. v. Commission;* ECLI:EU:C:2014:2201.

on the penalty level, all circumstances related to the implementation of the agreement were taken into consideration on an individual basis. The UOKiK President examined also the premise of 'the previous infringement of the provisions of the Act' (Art. 111) and found no reason to increase the penalty since there was no previous infringements of the said provisions.

As rightly pointed out by the Supreme Court, when imposing a penalty, the antitrust authority should consider the significance of the revenue earned from the sale of the goods covered by the agreement. In other words, the amount of the fine to be imposed need to be related to the revenue earned. It should also take into account the actual circumstances of the case, including negligible revenues earned from the sales covered by the agreement or benefits derived, which may be of marginal economic importance. Proper implementation of the principle of equal treatment demands the evaluation of the factual significance, which is to be ascribed to the revenue level in assessing the circumstances of a particular case.

IV. Conclusion

The discussed judgement of the Supreme Court, following its earlier judgment in the *Röben* case, presents a further step towards a more economics-oriented approach towards the assessment of competition restricting agreements. According to the Supreme Court, not every vertical agreement results in a violation of the public interest, a realisation stressed by the Court. The Supreme Court also pointed out, without questioning the general classification of price agreements as practices restricting competition by object, the need to depart from the strict application of the prohibition of Article 6(1(1)) of Competition Act 2007 to all types of vertical price-fixing agreements. Such approach will affect the application of the provisions governing the imposition of fines, including the function of penalties and their proportionality to the seriousness of the infringement. The analysed judgment of the Supreme Court is an example of departing from a formalistic approach not only with regard to the assessment of vertical agreements, but also to the principles of imposing pecuniary penalties.