

Reports

Austria

Sales Restrictions in a Production Joint Venture: Return of the Formal Approach

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In September 2017, the Austrian Supreme Court, sitting as Appellate Cartel Court (*Kartellobergericht*), handed down a decision concerning sales restrictions entered into by the partners of a production joint venture (JV).¹ In organising the distribution of the jointly produced products, the parties had opted to exclusively allocate markets among themselves. The highest Austrian competition court found that such an exclusive distribution agreement was akin to a naked restraint and constituted a restriction of competition by object. Arguably, this reasoning places too much weight on the type of agreement (market allocation) and does not sufficiently consider its economic context, notably the contribution to the creation of the joint venture.

I. Background

In 1989, Semperit, an Austrian producer of rubber products, formed a joint venture with Thai conglomerate Sri Trang Group, a processor of natural rubber. The joint venture, Siam Sempermed Corporation Ltd (SSC), was to produce high quality medical examination gloves made from a mixture of natural rubber and latex. The two groups each held 50% of shares in the joint venture with corresponding voting rights and special rights to appoint SSC's upper management. The rationale of the creation of SSC was to combine Semperit's know-how regarding the production of natural rubber-latex gloves and Sri Trang Group's access to and processing know-how of natural rubber.

The JV agreement stipulated that SSC's products (examination gloves) were to be exclusively distributed by the JV partners. Semperit was granted exclusive distribution rights for Europe and the Middle East for the share of SSC's production attributable to

Semperit. The remaining production capacity was to be distributed by SSC outside the exclusive area attributed to Semperit according to the instructions of Sri Trang Group.

Starting in 2015, Sri Trang Group commenced to market its share of the joint venture's output also in Europe. In response, Semperit initiated arbitration proceedings with the aim to prohibit the sale of SSC's examination gloves by Sri Trang Group in the areas exclusively attributed to Semperit. Sri Trang Group considered that the exclusive allocation of distribution rights infringed Article 101 Treaty on the Functioning of the European Union (TFEU)² and Section 1 Austrian Cartel Act (ACA)³ and was therefore void. Against this backdrop Sri Trang applied for and was granted leniency status by the Austrian Federal Competition Authority (FCA). Following Sri Trang Group's arguments, the FCA initiated proceedings before the Cartel Court (*Kartellgericht*) aimed at the prohibition of the exclusive allocation of markets in the framework of SSC amongst the JV partners.

The Cartel Court held that the exclusive allocation of the EU and Middle East markets to Semperit (i) did not constitute an ancillary restraint objectively necessary for the foundation of SSC, and (ii) amounted to a restriction of competition by object, which was

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- 1 Higher Cartel Court, Decision of 6 September 2017, 16 Ok 10/16f.
- 2 Consolidated Version of the Treaty on the Functioning of the European Union [2008] OJ C 115/47.
- 3 Austrian Cartel Act 2005 (*Kartellgesetz 2005*), Federal Law Gazette I, No 61/2005, as amended.

not exempted under any block exemption regulation or Article 101 (3) TFEU. In qualifying the agreement as a restriction by object, the Cartel Court relied on the European Court of Justice's (ECJ) judgments in *Toshiba*⁴ and *Siemens*⁵. The Court made limited findings of fact. It however indicated that the market for examination gloves was worldwide in scope. The combined market share of Semperit and Sri Trang Group amounted to below 15% at the worldwide level, but was slightly higher in the European Economic Area (EEA).

On appeal to the Supreme Court, Semperit contested the qualification of the territorial allocation as a restriction by object. It argued that the *Toshiba* and *Siemens* judgments were irrelevant, as they related to 'naked' market sharing among competitors, whereas the case at hand concerned an exclusive distribution arrangement for the output of a production joint venture. Based on the ECJ's judgment in *Groupement des Cartes Bancaires*,⁶ Semperit argued that the objectives and the economic and legal context of an alleged restriction must be considered in determining whether it is to be qualified as 'by object' or 'by effect'. In addition, Semperit argued that the territorial allocation between the JV partners constituted an ancillary restraint within the meaning of the Commission's Ancillary Restraint Notice⁷ and the Guidelines on the Application of Article 101(3) TFEU.⁸ In particular, Semperit asserted that it would not have contributed its know-how to the joint venture in the absence of an exclusive right to sell the joint venture's products in its own core markets.

4 Case C-373/14 P *Toshiba Corporation v European Commission* [2016] ECLI:EU:C:2016:26.

5 Case C-239/11 P *Siemens AG and Others v European Commission* [2013] ECLI:EU:C:2013:866.

6 Case C-67/13 P *Groupement des cartes bancaires (CB) v European Commission* [2014] ECLI:EU:C:2014:2204.

7 European Commission, Commission Notice on restrictions directly related and necessary to concentrations [2005] OJ C 56/24.

8 European Commission, Communication from the Commission — Notice — Guidelines on the application of Article 81(3) of the Treaty [2004] OJ C 101/97.

9 Case C-345/14 *SIA 'Maxima Latvija' v Konkurences padome* [2015] ECLI:EU:C:2015:784.

10 Case C-32/11 *Allianz Hungária Biztosító Zrt et al v Gazdasági Versenyhivatal* [2013] ECLI:EU:C:2013:160.

11 Case C-172/14 *ING Pensii — Societate de Administrare a unui Fond de Pensii Administrat Privat SA v Consiliul Concurenței* [2015] ECLI:EU:C:2015:484.

II. The Supreme Court's Judgment

The Supreme Court upheld the judgment of the Cartel Court in its entirety. It qualified the allocation of an exclusive distribution right to Semperit as a horizontal market sharing agreement between competitors regardless of its legal, economic and historical context. While acknowledging that it did not constitute a naked restraint, the Supreme Court nonetheless found that the agreement constituted an infringement by object. It noted in this regard that, unlike in *Groupement des Cartes Bancaires* or *Maxima Latvija*,⁹ the case at hand did not concern complex multisided markets. The Supreme Court moreover considered, in line with the ECJ's judgments in *Allianz Hungaria*¹⁰ and *ING Pensii*,¹¹ that the intention of the parties was not a necessary factor in determining whether an agreement was restrictive. Rather, what mattered was whether the coordination reveals in itself a sufficient degree of harm to competition. As regards this question, the Supreme Court's findings are very limited. It simply noted that the aim of the agreement was to limit competition on the EEA market, and to foreclose competition by Sri Trang Group on that market.

The Supreme Court moreover refused to qualify the allocation of an exclusive right to distribute JV products as an ancillary restraint. Whilst its treatment of this question is rather perfunctory, the judgment indicates that some form of distribution arrangements may well qualify as ancillary to the creation of a production joint venture. However, the Supreme Court considered that the exclusive allocation of distribution areas among JV partners for the entire duration of the JV went beyond what was objectively necessary for the creation of the joint venture.

In reaching its decision, the Supreme Court rejected Semperit's request to refer the case to the ECJ for a preliminary ruling under Article 267 TFEU, as it considered that the ECJ's case law was sufficiently clear for the Austrian courts to decide in the case at hand.

III. Comment

The case is illustrative of the difficulties which national courts and authorities face in distinguishing between 'by object'- and 'by effect'-type infringe-

ments of Article 101 TFEU. Whilst the Austrian Supreme Court's judgment correctly identifies the criteria established by the ECJ to distinguish between the two categories of infringements, its application of the criteria to the facts of the case is very short, and the result is arguably not in line with the principles as set out in recent ECJ case law:

The Supreme Court's qualification of Semperit's exclusive right to distribute JV products in the EEA as a by object infringement appears to rest on the finding that the aim of the agreement was to foreclose intra brand competition by Sri Trang Group. This reasoning appears to equate a restriction of the parties' freedom of action (here: Sri Trang Group's freedom to market JV products in the area allocated to Semperit) with a restriction of competition. The case law however indicates that a restriction in the freedom of action does not necessarily constitute a restriction of competition, as was made explicit by the ECJ in *Wouters*.¹² Whilst the judgment acknowledges that the legal qualification of a practice as 'by object' or 'by effect' has to take account of the legal and economic context, the actual discussion of that context is very brief. Essentially, the Supreme Court distinguishes the case at hand from *Groupement des Cartes Bancaires* and *Maxima Latvija* by pointing out that these cases concerned complex multisided markets. Beyond this reference to recent judgments in which the conduct at issue was deemed not to constitute a 'by object' infringement, the Supreme Court does not explain why the exclusive allocation of distribution of the JV output in the EEA to Semperit 'reveals in itself a sufficient degree of harm to competition'¹³ to come under the 'by object' umbrella.

Indeed, if one subscribes to the interpretation that the 'by object' label is reserved to practices which are not plausibly pro-competitive¹⁴ or which may be presumed to have a *net* negative impact on competition¹⁵ in the economic and legal context of which they are part, the Supreme Court's reasoning appears questionable. The need to ensure indirect network effects on platform markets is but one example of credible pro-competitive reasons which may underlie a practice. In the case at hand, the territorial allocation concerned the output of a production joint venture. Production joint ventures may give rise to various efficiencies, including marginal costs efficiencies due to economies of scale, elimination of overhead costs, and improved product quality.¹⁶ Under the Block Exemption Regulation for Specialisation Agreements,¹⁷

such joint ventures even benefit from an exemption from the prohibition of Article 101(1) TFEU, provided that certain conditions are met. These conditions include, in particular, a market share threshold of 20%. In addition, Article 3(3) of the Specialisation Block Exemption Regulation requires that the parties either accept an exclusive purchase or supply obligation, or jointly distribute the specialisation products.

At first sight, the solution adopted by Semperit and Sri Trang Group does not appear to be inherently more harmful than JV setups which would have been block exempted. Given their market share of less than 20%, the parties would have benefited from block exemption had they agreed to distribute the JV products in a joint team, or via a third party distributor.¹⁸ In each case, there would have been no intra brand competition in the distribution of the JV products. The Specialisation Block Exemption Regulation however provides a legal presumption that the potential restriction of competition which stems from this is outweighed by the efficiencies which specialisation and joint production agreements give rise to. By contrast, the Austrian Supreme Court's qualification of the exclusive allocation of distribution rights for JV products as 'by object' restrictions effectively means that an economically similar JV setup – which however does not meet the formal conditions of the Specialisation Block Exemption Regulation – is presumed to be anticompetitive. In the authors' view, it

12 Case C-309/99 *Wouters v Algemene Raad van de Nederlandse Orde van Advocaten* [2002] ECLI:EU:C:2002:98, para 97. See also eg Case C-136/12 *Consiglio nazionale dei geologi v Autorità garante della concorrenza e del mercato* [2013] ECLI:EU:C:2013:489, para 53; Case T-99/04 *AC-Treuhand AG v Commission* [2008] ECLI:EU:T:2008:256, para 126.

13 Case C-67/13 P *Groupement des cartes bancaires (CB) v European Commission* [2014] ECLI:EU:C:2014:2204, para 57.

14 Pablo Ibáñez Colomo and Alfonso Lamadrid de Pablo, 'On the notion of restriction of competition: what we know and what we don't know we know' in Damien Gerard, Massimo Merola and Bernd Meyring (eds), *The Notion of Restriction of Competition: Revisiting the Foundations of Antitrust Enforcement in Europe* (Bruylant 2017).

15 Luc Peepkorn, 'Defining "by object" restrictions' [2015] 3 *Concurrences* 40, 41.

16 European Commission, Communication from the Commission — Communication from the Commission — Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union to horizontal co-operation agreements [2011] OJ C 11/1, para 181.

17 Commission Regulation (EU) No 1218/2010 of 14 December 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to certain categories of specialisation agreement [2010] OJ L 335/43.

18 cf arts 3(b) and 1(1)(q) Regulation (EU) No 1218/2010.

is doubtful whether mere differences in the legal structure of a joint venture really should give to such significant variations in assessment.

On a more general note, the Austrian Supreme Court's judgment however also may illustrate the difficulties faced by national courts and competition authorities in applying the ECJ's case law. The ECJ's style of reasoning, which typically avoids broader discussion of the social and economic interests at stake

and contains frequent word-for-word citations of older case law, may well have advantages in terms of legal stability in many cases. In areas where the law is not a model of clarity, such as with regard to the distinction between 'by object' and 'by effect' restrictions, some clearer guidance may however help to contribute to a more accurate and uniform application of the EU competition rules by national decision makers.