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10% of Annual Turnover is the Price to Pay for Entering into Prohibited Agreements and Abusing Dominance

Many managers in Bulgaria still wonder, what is wrong with discussing the price of your product or the cost of your raw materials with your competitors. The new Bulgarian Protection of Competition Act provides a clear and stark answer – it could cost your firm 10% of its annual turnover.

Lack of knowledge of what constitutes entering into 'prohibited agreements' (a legal euphemism that denotes arrangements such as cartels, other forms of tacit coordination among competitors, and in some cases - arrangements between non-competitors), or what represents an abuse of dominant position, is still the lead reason for companies to be fined under Bulgarian anti-trust law.

While the sanctions in Bulgaria were previously as low as BGN 5,000 and rarely reached the legal maximum of BGN 300,000, with the new Protection of Competition Act (the "**Act**" or "**PCA**") that came into effect in December 2008, they were brought in line with the levels under European law. This put the risk for companies into the range of *millions* with the maximum limit set at 10% of annual turnover.

A number of local and international companies have already put in place internal review and compliance programs. These include reviewing existing contracts and practices, past participation in industry associations, correspondence, preparing internal anti-trust rules, and doing training for the staff and management. Even after these measures are in place, a concerted effort to refresh and police them is needed to prevent sanctions for the companies and the general upset of business that accompanies an anti-trust prosecution.

Experience shows that managers – especially those representing the company in industry associations and having other contacts with competitors, and sales personnel at all levels (and especially those active in the field) are at the highest risk of committing an infringement and bringing their company to bear liability.

1. What are Prohibited Agreements and Abuse of Dominance?

The Bulgarian competition authority – the Commission for the Protection of Competition ("**CPC**" or the "**Commission**") applies both Bulgarian competition law (the PCA) and European competition law (Regulation (EC) 1/2003[1]) in the area of prohibited agreements and abuse of dominant position.

The definition of these infringements are the same under both Bulgarian and European law:

Under the PCA and Article 81 of the EC Treaty, the following shall be prohibited:

[1] Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty

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New sanctions under anti-trust law can reach 10% of the annual turnover of the company.

Lack of knowledge and training among management and sales personnel are a major risk factor.

The CPC applies both Bulgarian and European anti-trust law - they sanction the same types of anti-competitive conduct.

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all types of agreements between undertakings, decisions by associations of undertakings as well as concerted practices of two or more undertakings having as their object or effect the prevention, restriction or distortion of competition on the relevant market.

In respect of abuse of dominance, the Act prohibits the actions of undertakings enjoying monopolistic or dominant position, as well as the actions of two or more undertakings enjoying a collective dominant position that may prevent, restrict or distort competition and impair consumers' interests.

Dominance is defined as the position of an undertaking which, in view of its market share, financial resources, possibilities for access to the market, level of technology and economic relations with other undertakings may prevent competition on the relevant market, because it is independent of its competitors, suppliers or customers

Behind these vague one-sentence definitions, lies a large body of cases of the European Courts, the European Commission, and more recently the Bulgarian Commission for the Protection of Competition and the courts, which seek to clarify which behavior is anti-competitive and to sanction it.

The most hard-core prohibited agreements are cartels. Cartels are not only agreements among competitors on the price at which they will sell their products, or at which they will buy their raw materials. Cartels can also be various agreements among competitors on where and to whom they will sell or not sell their products (sharing the market territorially or by clients), agreements to reduce production or otherwise regulate the supply or demand in the market (like production or purchasing quotas), etc. Bid rigging (e.g. coordinating offers in a public or private procurement procedure) and commercial boycotts are also cartels. Cartels can take various other forms and therefore each joint action with competitors (including joint selling, joint purchasing, mutual distribution etc.) should be subject to anti-trust compliance review.

While cartels are the best known types of anti-trust violations, one should not loose sight of a number of other lesser known infringements, which will be treated as harshly by the regulators. Chief among them are concerted practices, which involve the exchange of sensitive information between competitors, allowing them to anticipate and therefore coordinate their market behavior. Examples of this include exchanges of information on intended price increases, but also more subtle and complex forms of coordination, such as those done by way of pooling of information within industry associations.

Agreements with distributors, wholesalers and retailers may also be prohibited. Depending on the portion of the market affected, various exclusivity arrangements, territorial restrictions, cross-selling restrictions, exclusive allocation of clients, etc., can be regarded as prohibited. Licensing and other specific types of agreements may also contain anti-competitive clauses.

Where a company is dominant in the market it is under a higher standard of scrutiny in respect of its market conduct. Dominant companies may be held liable not only for their agreements and other joint actions with other market players, but also for their unilateral actions. While under the new PCA there is no longer a presumption of dominance where the company has a market share above 35%, the CPC's methodology notes that dominance can exist in product and geographic markets where the company's share exceeds 20% and is almost certain where the share is above 70%.

The range of actions which can constitute abuse is vast and its assessment is complex. Two large groups of abuses exist – exclusionary abuses – where the dominant company uses its market power to eliminate competitors (e.g. pricing below cost, price and margin squeeze, tying distributors with exclusivity, unjustified refusal to supply, anti-competitive rebate schemes, etc.) and exploitative abuses – where the dominant company capitalizes on its market position to reap the benefits of its power by

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Anti-trust infringements include prohibited agreements and abuse of dominance.

Prohibited agreements cover cartels fixing prices of products or raw materials, sharing markets or clients, setting production or buying quotas, etc.

Bid rigging and commercial boycotts are also cartels.

Exchanging information with competitors on future market plans or sending commercially sensitive information to competitors is also prohibited.

Distribution and licensing agreements can also contain anti-competitive clauses.

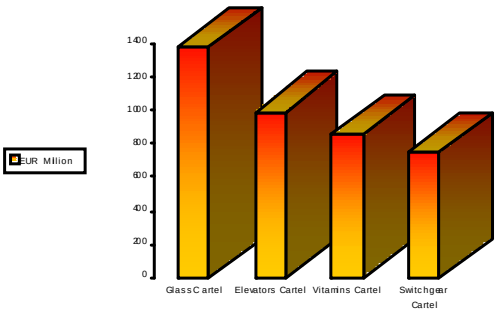
A company may be in a dominant position if its market share is greater than 20%.

Dominant companies can be sanctioned if they price below cost, tie distributors, refuse to supply without justifiable reason, or otherwise foreclose their competitors.

applying excessive pricing, imposing unfair trading conditions etc.

2. Previous Experience

The sanctions that are now introduced in Bulgaria have long been part of EU law and are routinely applied by the European Commission. It is important to note that the sanctions that are applied by the European Commission are applied by reference to the worldwide turnover of the entire economic group of the infringer. The record sanctions applied to cartels on a European level include: EUR 1.38 billion in total for the glass cartel (*2008*), EUR 992 million in total for the elevator cartel (*2007*), EUR 853 million in total for the vitamins cartel (*2001*), EUR 750 million in total for electric switchgear cartel (*2008*).



Fines for abuse of dominance, although generally lower, do not lag far behind. The record currently is being held by the EUR 1.4 billion fines imposed on Microsoft, including for failure to comply with an earlier decision of the European Commission.

The current Bulgarian records (under the old sanctions amounts), stand at BGN 2.4 million in total for an alleged motor vehicles insurance cartel and BGN 1.8 million for an alleged cooking oil cartel. In fact, in addition to being the chief proponent of the new sanctions amounts, the CPC's policy towards higher sanctions was expressed in the past in it imposing several sanctions to the same company for different counts of violation, thus sometimes exceeding the maximum amount of BGN 300,000 that existed under the old Act.

3. What is new?

3.1. Sanctions

Where undertakings have entered or engaged in prohibited agreements, decisions or concerted practices (either under Bulgarian or under EU law) or have abused their dominant position the Commission may impose a sanction on the infringing undertaking amounting to up to 10 per cent of the total turnover for the preceding financial year. A sanction in the same amount can be imposed on an undertaking for failing to comply with a decision of the Commission.

The Commission may also impose periodic penalties in an amount of up to 5 per cent of the average daily turnover for the preceding financial year, calculated on a daily basis for each day of non compliance with:

1. a decision of the Commission ordering the termination of an infringement, including by imposing the appropriate behavioural or structural remedies;

2. a ruling of the Commission, imposing interim measures.

The Commission may impose a sanction to the amount of up to one percent of the average daily turnover for the preceding financial year for each day of:

1. failure to comply with the obligation for assistance to the investigation;

2. failure to furnish complete, accurate, true and not misleading information;

3. impeding an inspection of the Commission.

3.2. Abolition of Individual Exemptions

Under the former PCA, companies could apply to the CPC to exempt their agreement from the general prohibition, because the agreement would have lead to certain positive effects, which outweighed any negative effects on competition.

In line with the European anti-trust reform package introduced by Regulation (EC)

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The 10% rule has resulted in EU sanctions in excess of EUR 1.3 billion for a single cartel case.

Sanctions under Bulgarian law have risen to 10% of annual turnover for violations of EU or Bulgarian anti-trust law.

Failure to cooperate in an investigation can cause sanctions of up to 1% of annual turnover.

Continued violations are sanctioned by fines of up to 5% of daily turnover per each day.

1/2003[2], the new PCA abolishes the possibility for individual exemption of agreements which fall under the general anti-trust prohibition.

It is now upon the parties to such agreements to prove that where their agreement falls within the general prohibition, it is capable of being exempted by reason that it contributes to the improvement of the production or distribution of goods or the provision of services or to the promotion of technological and/or economic progress, while ensuring a fair share of the resulting benefits to the consumers and it does not impose on the undertakings concerned restrictions that are not indispensable to the attainment of these objectives and does not afford such undertakings the possibility of eliminating competition in respect of a substantial part of the relevant market.

3.3. Change of *De Minimis Thresholds*

Certain agreements which normally would be considered anti-competitive, may be exempt from the general prohibition because their effect would be so small (‘*de minimis*’) that their prosecution would not be justified. The *de minimis* effect is judged primarily based on the market share of the goods and services affected by the agreement. Hard-core prohibited agreements, such as cartels, are not exempt, even if they affect a very small share of the market.

The new Act brought the Bulgarian *de minimis* thresholds in line with the EU standard – from 5 to 10 per cent market share for horizontal agreements, decisions and concerted practices and from 10 to 15 per cent market share for agreements, decisions and concerted practices the parties to which are not competitors.

3.4. Interim Measures

In a major development, and in contrast to the former Protection of Competition Act, the Commission has been granted the right to impose interim measures in infringement proceedings.

If, during an investigation, there is sufficient evidence of an infringement, in urgent cases where there is a risk of serious and irreparable damage to competition, the Commission may, at its own initiative or on request of the persons whose interests are affected or threatened by the infringement, order the immediate termination of the practice by the undertaking or the association of undertakings, or impose other necessary measures, taking into account the objectives of the Act.

3.5. Leniency

The leniency procedure was introduced for the first time in 2003 with the former PCA. It allowed for granting immunity or significant reduction of sanctions to companies which either were the ‘whistle-blowers’ of a cartel or contributed crucial information to the investigation.

In fact leniency is available also before the European Commission, in cartel cases investigated by it.

In Bulgaria no leniency applications have been made so far, perhaps because sanctions were considered not sufficiently high by infringers to warrant a leniency application, and also due to lack of knowledge of the significant benefits a leniency application can bring.

With the new sanctions amounts, this is a crucial area where the attention of managers should be focused, if they have found that employees of their company have engaged in a violation and want to avoid or significantly reduce the fine that will be imposed on the company.

The new Act provides extended regulation. The PCA provides that leniency will apply to the cases of a secret cartel. A “cartel” is defined for this purpose as an agreement and/or concerted practice between two or more undertakings – competitors in the relevant market, aimed at restricting competition through price fixing or fixing pricing conditions for purchase or sale, allocation of production or sales quotas or sharing of

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Anti-competitive agreements can be exempted from the prohibition if they can demonstrate positive effects. It is upon the company to prove these effects.

Agreements affecting a small part of the market are not covered by the prohibition, unless they are a form of cartel.

The CPC can impose interim measures to stop a conduct it considers anti-competitive.

Companies may avoid sanctions or see sanctions greatly reduced if they submit a leniency application, before others.

[2] Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty

markets, including rigging of public bids or tenders or public procurement award procedures. Leniency is expressly stipulated to apply to both infringements under national law and under Article 81 of the EC Treaty.

3.6. Dawn Raids

The new PCA, provides more detailed regulation on dawn raids, which is largely in line with the European law and precedent. The euphemism 'Dawn Raids' refers to the surprise inspections done by the competition authority (e.g. the CPC and/or the European Commission) often jointly with the police, and took their name from the fact that usually these surprise inspections happen in the early morning at the start of the business day of the company. The CPC, together with the police, has already made more than half a dozen such inspections, and the evidence collected has already served to find anti-trust infringements and impose sanctions. The CPC also has a dedicated laboratory that can extract data from seized computer hard disks and other information carriers.

The CPC has the power to visit the sites of the company or association under investigation for a suspected infringement of the PCA (including both anti-trust and merger control provisions) or Articles 81 and 82 ot the EC Treaty without a prior notice. An inspection requires, however, an authorisation by a judge from the Administrative court of the Sofia City.

The Commission may:

1. enter any premises, means of transport and other locations used by the undertakings and associations of undertakings;

2. examine all books and records, related to the business of the undertakings or associations of undertakings, irrespective of the medium on which they are stored;

3. seize or obtain information in hard, digital or electronic copy, copies of, or extracts from such books and records, irrespective of the medium on which they are stored or, where this is impossible, seize the originals, as well as any other material evidence;

4. seize or obtain electronic, digital and forensic evidence, including traffic data, from all types of computer data carriers, computer systems and other information carriers as well as seize the devices for transmission of information;

5. receive access to all types of information carriers, including information stored on servers, accessible by computer systems or other means located in the inspected premises;

6. seal for a certain period of time any premises, means of transport and other sites, used by the inspected undertakings or associations of undertakings, as well as commercial or accounting books or other information carriers;

7. take down oral statements of any representative or member of the management and staff of the undertakings or associations of undertakings, on circumstances, related to the subject matter and purpose of the inspection.

Any document or evidence found, may be seized if they contain data raising well-founded doubts of other infringements under the Act or under Article 81 or Article 82 of the EC Treaty.

Failure to cooperate may lead to fines. Fines can, for instance, be imposed if the investigated undertaking is found guilty of any of the following:

- Incomplete production of records (i.e. the production of books and records in incomplete form, the provision of incorrect oral information, a failure to provide clear explanations leading to relevant documents being overlooked, removal of relevant material, etc.);
- Incomplete access to company's premises;
- An unjustified refusal to comply with a request for oral explanation;
- Destruction of evidence during the investigation;

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The CPC can make surprise inspections with the help of the police.

During inspections the CPC can enter all premises, make copies of documents, have access to computer systems and servers, and seize documents and information carriers.

During inspections CPC officials can take statements from the employees and management.

During inspections the CPC and the police can seal premises.

- Refusal to cooperate with inspectors.

Where a party has impeded the collection of information in respect of certain facts, the Commission is entitled to assume that these facts have been proven, and base its decision upon them.

An inportant point to consider in this respect is that correspondence with in-house counsel is not covered by legal privilege and can be used as evidence against the company. Therefore if an infringement is found it is advisable to consult only the outside counsel, to the extent that these communications are covered by legal privilege and cannot be used as evidence.

4. Conclusions

In conclusion, timely action is needed by management to assess their company's compliance with anti-trust rules. Mistakes could have been made not only at the management level, but also at the lower levels, especially in the areas of marketing and sales. The fact that an infringement was committed by an employee who was not formally authorized to represent the company, or that the top management did not know about the infringement, is not an excuse that could avert sanctions. Management should be pro-active in adopting internal policies and rules to avoid infringements in the future and observe their continued implementation. Where during the compliance review a previous infringement is found, following careful consideration with outside counsel, the company can make a leniency application to avoid or reduce the sanctions that will be imposed upon it.

The new PCA provides a facilitated regime of submitting class-actions for civil damages on account of anti-turst violations against the infringing company. Please email us if you would like to receive a separate memorandum on this topic.

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Failure to cooperate with an inspection could result in serious sanctions.

Management is responsible for making a compliance review in the company.

The fact that an employee was not formally authorized to represent the company is not an excuse. Lack of knowledge on the part of management is not an excuse.

Past practices should be re-assessed and strict rules should be put in place. Management at all levels should be responsible for policing them.

When an infringement is discovered management should urgently consult and decide on whether to make a leniency application.

If you have any further questions concerning this note, please contact the head of our anti-trust practice group:

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