YEARBOOK of ANTITRUST and REGULATORY STUDIES
www.yars.wz.uw.edu.pl

Peer-reviewed scientific periodical, focusing on legal and economics issues of antitrust and regulation.

CSAiR
Centre of Antitrust and Regulatory Studies, University of Warsaw, Faculty of Management
www.wz.uw.edu.pl

When will the imposition of the requirement to co-finance the construction of necessary facilities constitute an abuse of a dominant position? Case comment to the judgment of the Supreme Court of 5 January 2007 – *Kolej Gondolowa* (Ref. No. III SK 17/06)

Facts

The President of the Office of Competition and Consumer Protection (hereafter, UOKiK) issued on 24 March 1999 a decision (RKR-500s-01 9/98/LP-454/99) in which he refused to accept the motion[1] lodged by *Koleja Gondolowa Jaworzyna Krynicka S.A.* (hereafter, KGJ) claiming that *Zakład Energetyczny Kraków S.A.* (hereafter, ZEK) had abused its dominant position on the local market for the supply of electricity. In the opinion of KGJ, the abuse took the form of the imposition upon KGJ by ZEK of onerous terms and conditions of their agreements. KGJ and ZEK concluded two functionally related contracts:

- an investment contract which obliged the parties to jointly finance the construction of the energy facilities necessary to build and operate by KGJ a cable-car system on Jaworzyna (KGJ – 53% and ZEK - 43%); and
- a contract concerning the gratuitous transfer from KGJ to ZEK of the jointly financed facilities.

The President of UOKiK did not agree with the position of KGJ. Instead, he stated that the return by ZEK of all the expenses incurred by KGJ would lead to a violation of the performance equivalency principle. A similar view was taken by the Court of Consumer and Competition Protection (hereafter, SOKiK) that stated that the demands of KGJ should be viewed as an attempt to apply competition rules so as to avoid the participation in the settlement of the joint investment. KGJ filed for cassation to the Supreme Court which remanded the case to the Court of Appeal for

[1] The possibility to file a motion for instituting antimonopoly proceedings is no longer provided under the provisions of the Act of 17 February 2007 on Competition and Consumer Protection (Journal of Laws 2007 No. 50, item 331; hereafter, Competition Act). That institution was replaced by the currently available right to notify UOKiK of a suspicion that a competition restricting practice has been applied (see Article 86 of Competition Acr); see also K. Kohutek, M. Sieradzka, *Ustawa o ochronie konkurencji i konsumentów. Komentarz* [*Act on Competition and Consumer Protection. Commentary*], Warszawa 2008, p. 904.

its examination as an appeal. The appeal was dismissed. Finally, the Supreme Court in its judgment of 5 January 2007 settled this dispute in favour of KGJ quashing the judgment of the Court of Appeal and remanding the case for re-examination.

Key legal problems of the case and key findings of the Supreme Court

The basic problem that arose in this case concerned the different legal qualifications of the contracts concluded between KGJ and ZEK in the light of the prohibition of the abuse of a dominant market position. The Supreme Court found, and in my opinion rightly so, that ZEK's conduct should be qualified as an abuse taking the form of the imposition upon KGJ of onerous terms and conditions of their agreements, which yielded unjustified profits to ZEK (see Article 9(2(6)) of the Competition Act[2]). This form of abuse constitutes an exploitative practice of a dominant firm.

Finding that the assessed conduct constitutes an abuse requires however the cumulative fulfillment of the three following prerequisites:

- the "imposition" of the terms and conditions by the dominant firm;
- the "onerousness" of these terms and conditions (from the perspective of the dominant undertaking's contracting party);
- the "yielding of unjustified profits" (to the dominant undertaking[3]).

The Supreme Court distinguished all of the abovementioned prerequisites, pointing out that all of them were fulfilled in this case.

Imposition of onerous agreement terms and conditions

For the purposes of Article 9(2(6)) of the Competition Act, the notion of "imposition" shall be interpreted broadly. In this respect, it is advisable to follow the position of the Supreme Court stating that the objective scope of "imposition" encompasses situations where the potentially exploited firm (which has interests in receiving the necessary energy from a dominant firm) has no option but to purchase goods (in this case: energy) from the sole existing supplier. Such findings are correct seeing as they refer to the state of competition existing on the market or, to be more precise considering the circumstances of the assessed case, to the state of the lack of competition in the given market (or its significant restriction).

Nonetheless, the fact that the relevant upstream market is characterised by the existence of a dominant undertaking does not – *per se* – translate into a lack of alternative supply options for undertakings operating on the downstream market

[2] That form of abuse was listed in the former Polish competition acts; see Article 5 para. 1 point 6 of the Act of 24 February 1990 on Counteracting Monopolistic Practices and Consumer Protection (consolidated text: Journal of Laws 1999 No. 52, item 547) and Article 8(2(6)) of the Act of 15 December 2000 on Competition and Consumer Protection (consolidated text: Journal of Laws 2003 No. 68, item 804).

[3] That prerequisite was not closely examined by the Supreme Court; thus discussing it will be omitted.

since they still have (or certainly can have) the possibility of receiving the necessary products/services[4] from other upstream firms[5]. However, in this case there was no such possibility. ZEK was a **natural monopolist** on the local market of electricity supply in Krynica. As a result, KGJ was in fact forced to use the supply of a local monopolist since it needed to gain access to the energy necessary for starting and operating a cable-car on Jaworzyna.

That does not mean that finding an exploitative practice (described in Article 9 para. 2 point 6 of the Competition Act) is limited only to situations where the undertaking, which imposes onerous agreement terms and conditions, possesses a monopolistic position. In my opinion however, enjoying such a position constitutes a factor that *per se* determines the fulfillment of the "imposition" criteria[6]. Possessing therefore merely a dominant, rather than monopolistic, position will require additional proof that, despite the existence of some substitutive goods[7], the downstream undertaking (undertakings) has in actuality very limited supply options or even – particularly when considering all case specific circumstances – that such options *de facto* do not exist.

The onerousness of the imposed terms and conditions

The second prerequisite requires that the terms and conditions imposed by a dominant firm (in this case: ZEK) are onerous from the point of view of its contracting party (in this case: KGJ). Concerning this issue, the Supreme Court took however in the case concerning KGJ and ZEK a view completely different from the opinions previously expressed by the President of UOKiK, SOKiK and the Court of Appeal. The prerequisite of onerousness should generally be considered to be fulfilled if the dominant contracting party is granted benefits that exceed those which would normally follow such contract. For that purpose it is necessary to examine whether, hypothetically, a dominant undertaking would be able to negotiate such onerous terms and conditions[8] in a competitive market, or a market that is at least more competitive than the one under scrutiny. It seems very unlikely that the result of such test would be positive in this case. The terms and conditions of the contracts between KGJ and ZEK (see: Facts) differed from the terms that could have been negotiated for similar

[4] See the definition of "goods" which includes not only products, but also all forms of energy, securities and other property rights, services as well as construction works (Article 4(7) of the Competition Act).

[5] These firms are the competitors of the dominant company.

[6] This of course does not determine the qualification of such monopolistic conduct as an abuse; this "only" confirms the fulfillment of the first of the prerequisites. The monopolist could effectively question the charge of an abuse by proving that, in spite of an "imposition" of certain terms and conditions, those terms were not onerous for his contracting party and eventually, that they did not yield unjustified profits to him.

[7] Offered by the competitors of the dominant company.

[8] See also judgment of SOKiK of 26 January 2005, XVII Ama 89/03, UOKiK Official Journal 2005 No. 2, item 25.

services (in this case: energy supply) under the condition of effective ("normal") competition.

The onerousness of the assessed terms and conditions consisted of the imposition on KGJ of the obligation of a gratuitous transfer to ZEK of the relevant facilities, even though KGJ incurred 53% of the expense of their creation. In consequence, on the basis of such obligation, ZEK was granted "free financing" of over half of the investment in the construction of the facilities. Negotiating a "donation" of that kind is highly unlikely on a competitive market. Therefore, one should share the Supreme Court's position rejecting the statement of SOKiK which incorrectly claimed that a free transfer of the facilities was not onerous to KGJ because it allowed the former to obtain (in return) access to a source of energy that was necessary to conduct its economic activity.

The conclusion of the Supreme Court is justified for at least two reasons. Firstly, a legal relationship for energy sale does not include the construction of facilities[9] or the financing/co-financing of such investment. Secondly, the possibility of gaining access to an energy supply network cannot be treated as equivalent to the non-dominant party's co-financing of the construction expenses (perhaps such a finding would be justified if, for a certain period of time, KGJ was supplied energy free of charge[10]). Under normal business practice in the energy supply field, the equivalent compensation for the energy supplied is the fee payable to the supplier by its customers. The fact that the energy received by this specific customer is to be used solely for profit-making activities (conducted by this customer), is irrelevant to the above assessment.

In practice however, cases in which a firm interested in receiving a certain service participates in the financing or co-financing of the construction of the facilities necessary for the provision of such service, can occur relatively frequently. There are no grounds to treat such cases as a *per se* violation of the prohibition of a dominant position abuse[11]. Nevertheless, when parties decide to finance the necessary investment jointly, than each of them simultaneously (and usually also proportionally to the expenditure incurred) participates in the profits associated with such investment. Similarly therefore, a part of the profits made by ZEK from the supply of the energy, which was made possible on the basis of the jointly financed facilities, should be transferred to KGJ. This case is quite unique, because one (and the same) undertaking appears in a "dual role". As such, KGJ is both an investor that should have the right to a share in the profits as well as the sole customer of ZEK, making it the sole source of those profits. In this context, KGJ should have therefore been temporarily released from its obligation of pay fees for the energy supplied by ZEK (or a proportional reduction of such fees)[12]. The Supreme Court supported this second view noticing that

[9] I.e. facilities which are necessary to render energy supply services.

[10] In this case ZEK however was not obliged to free energy supply to KGJ.

[11] It was pointed out by the Supreme Court that co-financing of investment by customers should not *per se* be treated as a monopolistic practice.

[12] Such solution would simultaneously comply with the principle of performance equivalency and above all would eliminate the grounds for finding an abuse of a dominant position by ZEK.

the prerequisite of onerousness would not be fulfilled (and consequently, no abuse would be found) if the free transfer of the facilities to ZEK led to an appropriate lowering of the price that KGJ would pay for the energy supplied by ZEK[13].

Final remarks (consumer welfare test)

An additional argument supports the position taken by the Supreme Court. One can refer to the consumer welfare test as a criterion for the legal qualification of the conduct of a dominant company in the light of its conformity with competition law[14] and, in particular, with its ultimate aim. That aim is to enhance or (at least) to satisfy consumer welfare[15]. With regard to Article 82 EC, the European Commission has also pointed out that the aim of the prohibition of abuse is to help markets to work better for the benefit of businesses and consumers[16]. When applying the abovementioned test to this case, it is justified to find that the conduct of ZEK did not promote consumer welfare or, in fact, that it even hindered its enhancement. It is in the interests of consumers[17] to create a new "product" (in this case: a cable-car) and to be able to buy it for a competitive, rather than inflated, price. Therefore the following findings seem to be justified:

i) the creation and operation of the cable-car facilities would probably be hindered if KGJ, behaving as if the given market was "more competitive" than it actually was, demanded from ZEK that the latter resigned from the condition requiring the gratuitous transfer of KGJ's investment for the construction of the facilities and the supply of energy[18] necessary for KGJ's activities;
ii) rejecting the qualification of the relevant contracts (see Facts) as an abuse of a dominant position would result in burdening KGJ with over half of the construction costs of the facilities without receiving an equivalent return from ZEK. The negative consequences of such solution would be "passed on" to

[13] The prices were not lowered in this case.

[14] Applying a consumer welfare test as a criterion for finding or excluding abuse is postulated in the literature; see e.g. R. O'Donoghue, A.J. Padilla, *The Law and Economics of Article 82 EC*, Oxford, Portland, Oregon 2006, p. 191 - 193.

[15] See M. Bernatt, A. Jurkowska, T. Skoczny, *Ochrona konkurencji i konsumentów* [*Competition and consumer protection*], Warszawa 2007, p. 20; see also K. Kohutek, [in:] K. Kohutek, M. Sieradzka, *Ustawa…*, p. 42 i 43.

[16] See the draft Guidance (of 3 December 2008) on the Commission's Enforcement Priorities in Applying Article 82 EC Treaty to Abusive Exclusionary Conduct by Dominant Undertakings (see points 1, 5, 19, 82 of that document) which refers to exclusionary abuses. However, exploitative practices of a dominant firm are, by their nature, even more able to harm consumers or trade partners (also in a direct way) than exclusionary ones.

[17] Consumers that constitute a certain group which, in the public interest, is meant to be protected by proper application of competition rules (see also Article 1 of the Competition Act).

[18] KGJ having faced the lack of an alternative offer of energy supply was actually forced to accept the terms and conditions required by ZEK.

consumers (the users of the cable-car) by fixing the prices for using the cable-car on a higher level than that which would normally be expected in a competitive environment. Such practice is very common in the economy; prices of goods/services offered by an undertaking usually include the costs which are, or were, being incurred by that undertaking to produce those goods or to render those services.

Dr. Konrad Kohutek
Member of Polish-German Centre for Banking Law, Jagiellonian University;
Lecturer in A. Frycz-Modrzewski Cracow Highschool;
Of Counsel at 'Kaczor, Klimczyk, Pucher, Wypiór' – Lawyers Partnership Company.