LISBON'S APPEAL COURT

PROCESS: 107/2001.L1

REDACTOR: TOMÉ GOMES

DATE: 4/10/2011

THEMATIC: ABUSE OF ECONOMIC DEPENDENCE

LEGISLATION AT ISSUE: ARTICLE 4, DECREE-LAW NO. 371/93, OF 29TH OCTOBER 1993, REPLACED BY LAW 18/2003, OF 11TH JUNE 2003 [NOW, LAW 19/2012, OF 8TH MAY 2012]; ARTICLE 102 TFEU

DECISION SUMMARY:

1. Within the scope of successive commercial purchase and sale transactions recorded in the current accounting process, in accordance with article 342, no. 1 and 2, of the Civil Code, it is the Plaintiff's responsibility to prove each transaction through credit notes as constitutive facts of the plea, while the Defendant has to prove the extinctive facts of such plea, such as the partial or whole sum of those entitlements, as well as the modifying facts that lead to the reduction of the set prices, through credit notes that qualify the respective invoices.

2. The characteristic features of indirect, integrated commercial distribution agreements are the legal independence of the retailer with regard to the supplier and the binding instructions and orientations set out by the supplier concerning the execution of the business policy that must be respected by the retailer, whereas the retailer is subject to the control and monitoring of the supplier, in a sustainable or long lasting cooperation framework; the distributor is usually obliged to promote the supplier's businesses, in respect to the goals and guidelines set out by the supplier, in spite of doing so with private autonomy.

3. However, the integration of the retailer in the supplier's commercial network may take on different modes and densities, depending on the form and level of cooperation set out by both parties, including the commercial concession framework contract.

4. Since the commercial concession contract is, per nature, an untypical legal distribution agreement, the agency contract must be applied by analogy, since it involves a similar activity and an analogous set of tasks in a stable and cooperative relationship and a common goal. Yet, that assimilation must be decided in each individual case, considering the specific characteristics of each contract.

5. The party that intends to exercise the right to cancel the concession contract must invoke and prove the facts resulting in the other party's nonobservance of main, ancillary or even minor contractual obligations but only when considered particularly severe or frequently repeated and

capable of undermining the subsistence of the contract. In other words, the right to cancel the contract must only be exercised in presence of a justified cause to terminate such agreement; such conditions are instated in respect to the usual extended duration of such contracts and their economic and social purpose.

6. When assessing the gravity of the legally relevant default, the following must be taken into account: "the importance of the default *per se* in the general framework of the contract in hands; the continuation or repetition of the situation of default; the time lapse since the closing of the contract and the moment in matter; the way that other relationships between the parties have transpired.

7. Under article 813 of the Civil Code, the creditor's lack of cooperation towards the debtor in the realization of the payment legitimates the debtor to suspend the agreed payment.

8. Since the Plaintiff overlooked such cooperation obligation by not clarifying the Defendant about which invoices were in due, as well as their exact amount, and the Defendant has done everything within its power to determine the due amounts, the latter has the right to suspend the payments.

9. In a situation of illegal resolution of the concession contract by the grantor, considering that the invoked justified grounds are not proven, under article 34/a) of Decree-Law 178/86, of 3rd July, that resolution becomes an irreversible situation of contract termination, portraying the consolidation of a definitive default of the contract with the resulting obligation to repair the damages, comparable to a situation of contract termination without advance notice, namely in terms of the right to compensation for loss of costumers under article 33 of the same legal diploma.

10. According to our legal regime, the "compensation for loss of costumers" is not meant to indemnify the concessionaire for the damages resulting from the loss of fees caused by the cessation of the contract, but to provide him a compensation for the capital gains that the grantor will obtain out of the raised customers, whose loyalty has been gained through the work developed by the concessionaire.

11. To determine the amount of compensation, under article 34 of Decree-Law no. 178/86, of 3rd July, in the version established by Decree-Law 118/93, of 13th April, a criterion of equity will be used, buoyed by a maximum limit (plafond) equal to a compensation calculated from the commercial agent's average annual remuneration over the past five years or, in case the contract has not lasted that long, from the commercial agent's average annual remuneration for the period of time it lasted.

12. It is a formal criterion of decision, equity, which leads us to ponder the specific circumstances of the case, not only having a purely subjective criterion, but a directive criterion of ponderation and appraisement of the concrete circumstances.

13. Considering that the compensation for the loss of costumers aims at compensating the concessionaire for the capital gains obtained by grantor through the work of the concessionaire on gaining the fidelity of the costumers while the contract produced its legal effects, the maximum limit mentioned works as a ceiling that aims at hindering the cost it represents to the grantor's financial capacity, portrayed by the average of the effective gains of the concessionaire during the time being of the contract.

14. When calculating the compensation, such limit shall not be taken into consideration as a descending starting point, but only when the amount calculated, in the light of equity, surpasses the cipher obtained by the application of such legal formula, in other words, through the method of prime tabulation of the obtained capital gain, calculated having in consideration the date of cessation of the contract by the grantor, taking into account the activity developed by the concessionaire, and only then confining it's result to the legal maximum limit.

15. The legal institute of abusive exploitation of the "state of economic dependence", also known as "relative dominant position", is relevant in Competition Law, aiming at sanctioning anti-competitive practices that translate into abusive exploitation of an undertaking by another, given the fact that the latter is in a position of supremacy in terms of producing or in terms of distribution of goods, therefore concerning a vertical relation, whether it's in an ascendant (v.g. retailer/supplier) or descending point of view (v.g. supplier/retailer).

16. Competition Law envisions to guarantee, concerning the framework of a free market economy system, the equality of opportunities for economic agents, an essential condition for the free expression of personality in socio-economic life, as enshrined in articles 2, 61, no. 1, 81/f) and 99/a) to c) and e) of the Constitution of the Portuguese Republic.

17. In the Portuguese legal order, as well as in the European Union legal order, the workable competition model prevails, inspired in the idea of competition as a necessary means to a balanced economic development; thus, under article 4 of Decree-Law no. 371/93, of 29th October – meanwhile revoked and replaced by Law no. 18/2003, of 11th June (Competition Act), a violation of competition law will only occur if the abusive exploitation of economic dependence affects the functioning of the market or the structure of competition..

18. In most dependent contracts, economic dependence may result from three cumulative factors: the existence of a contractual relationship; the importance of the contract for the weakest party's activity; the constancy of the commercial relation by which one of the parties organizes its respective activities.

19. The criteria that have been usually used to appraise the existence of economic dependence are: a) the brand's notoriety; b) the supplier's market share; c) the relevance of the supplier's products in the distributor's business volume; d) the availability of the latter to find an equivalent alternative for the goods or services supplied by the providing undertaking.

20. In spite of the concessionaire's legal autonomy towards the grantor, a case of economic dependence may occur, which can lead to the application of the legal institute of abusive exploitation of "the state of economic dependence".

21. All of the relevant components of the economic dependence legal type are constitutive facts of the established prohibition and the corresponding civil sanction, wherefore it is the party that intends to apply it that has the burden of proof, as enshrined in article 342, no. 1 of the Civil Code, even though it might be able to prove it through mere evidence.

22. As for the contract of commercial concession, in order to assess the degree of economic dependence, the importance of the brand's notoriety criterion will be as relevant as the notoriety and the reputation that such brand has in the market, but that factor cannot be appraised solely, so it must be assessed considering the brand's importance in the concessionaire's business volume.

23. As to the supplier's market share, even though this is a quite relevant criterion when it comes to abuse of dominant position, it loses some of its importance when it comes to cases of economic dependence, since what matters is to determine if the share that the supplier holds in the relevant market makes it a "mandatory partner" for its competing distributors.

24. As to how much the products of the supplier represent in the distributor's business volume, what is important is to evaluate the significance that the product at issue has in the concessionaire's business and in if its business structure organization is directed or confined to marketing that product.

25. Regarding the "equal alternative evaluation", what is imperative to assess are the conditions that the concessionaire has at its disposal to find an alternative solution within the market and the costs associated with necessary business organization adjustments to integrate new solutions. The contractual cessation regime has to be taken into account in the process of evaluation, especially the respect of the period of prior notice to terminate such contract by the grantor.

26. In the case in hands, given it was not proven that the defendant did not have any equal alternative within the market to arrange the provision of the type of products supplied by the Plaintiff, it has to be concluded that there was no state of economic dependence.

27. Even though the existence of a state of economic dependence is irrelevant in terms of Competition Law, it might lead to contractual or extracontractual liability, if the respective legal preconditions are observed.

PROCEEDINGS' RELEVANCE IN COMPETITION LAW ENFORCEMENT:

The proceedings take into consideration the existence of a contract of commercial concession in which the Defendant was contractually obliged to buy a certain amount of products supplied by

the Plaintiff so it could resale them in Portuguese territory. In addition, the Defendant was bound to promote the product and to assure after-sales service.

The Defendant, claiming the existence of an exclusivity clause between the parties, claimed to have asked a review of the prices of the supply contract numerous times, given the fact there were competing retail undertakings selling the same products through a parallel market. Since the Plaintiff did not respond to any of such requests and the Defendant considered that the Plaintiff's profit margins enabled such review, the Defendant decided to suspend the payment of the invoices.

The delay in payment, which culminated with the termination of the contract by the Plaintiff, constituted, according to the Defendant, an abuse of the Defendant's position of economic dependence towards the Plaintiff, infringing article 4 of the Decree-Law no. 371/93, of 29th October (revoked and replaced by Law no. 18/2003, of 11th June, which was later revoked and replaced by Law no. 19/2012, of 8th May).

Lisbon's Civil Trial Court considered the Plaintiff's compensation plea totally unfounded, acquitting the Defendant. Conversely, it found the Defendant's counterclaim partially well-founded, ordering the Plaintiff to pay a compensation to the Defendant in the global amount of $ 579.720,96 (escudos) for unlawful resolution of the contract, a compensation for the loss of costumers, a compensation for the Defendant's expenses caused by costumers' complaints, a compensation for transportation expenses of the F… product and a compensation for marketing expenses, as well as added possible interests to be calculated since the notification of the counterclaim/judicial challenge.

Unhappy with the ruling, the Plaintiff filed an appeal, denying the existence of such exclusive distribution and commercialization clause concerning the F… tires between both parties, given that the Defendant used to sell other products as well.

Furthermore, even though the Plaintiff might have had the possibility to review the pricing of the supply contract, it claimed that the first instance ruling did not show that that unwillingness to reduce prices had been deliberate and aimed to push the Defendant off the supply contract, so that the Plaintiff could sell the F… tires by its own means.

The Defendant also filed an appeal, claiming that it was its reputation that had enabled the introduction and development of the F… brand in the Portuguese tire market, acquiring the customers' loyalty.

In addition, the Defendant claimed that the Plaintiff never showed any willingness to discuss the violation of the exclusivity clause. Moreover, after the termination of the contract, the Defendant claimed that the Plaintiff reduced the price of its products in the Portuguese retail market, whilst during the contract it continuously increased such pricing, leading to the expulsion of the Defendant from this commercial relationship because of the accumulated losses.

So, considering the worldwide notoriety of the Plaintiff's brand in the tire market and given the fact that the Defendant was allegedly in a state of economic dependence towards the grantor (it represented 1/3 of the Defendant's business volume, therefore a considerate part of its accounting results depended on the pricing set out by the Plaintiff) and the fact that there was no equal alternative on the Portuguese market or on the foreign market (without prejudice of the unlawful resolution of the contract, given the violation of the minimum period of notice), the Defendant claimed that the Plaintiff had abused the Defendant's state of economic dependence towards it.

THE LISBON COURT OF APPEAL DECIDED UPON SOME RELEVANT QUESTIONS RELATED TO COMPETITION LAW ENFORCEMENT:

(1) DEFINITION OF ABUSE OF ECONOMIC DEPENDENCE – RELATIVE DOMINANT POSITION

(2) ABUSE OF ECONOMIC DEPENDENCE - SPECIFIC PREREQUISITES

(1) The legal institute of Abuse of Economic Dependence, also known as abuse of "relative dominant position", exists under Competition Law to sanction practices that might undermine the functioning of the workable competition and refers to *"practices carried out by an undertaking that abusively exploits another undertaking which economically depends on the first in terms of the production or the distribution of products, therefore concerning vertical relations, whether in an ascending point of view (v.g. retailer/supplier) or in a descending point of view (v.g. supplier/retailer)."*

Even though the legal institute of Abuse of Economic Dependence is not expressly regulated in the European Union Treaty or in the Treaty on the Functioning of the European Union, it appeared in the Portuguese legal order inspired in the French legislation, in article 4 of Decree-Law no. 371/93, of 29th October – revoked and replaced by Law no. 18/2003, of 11th June and, afterwards, by Law no. 19/2012, of 8th May (Competition Act). Its field of application are the cases where the legal institute of Abuse of Dominant Position cannot be applied ("Absolute Dominant Position", article 3 of the same legal diploma).

This is to say that this legal institute is meant to sanction an undertaking which is in a position of economic dominance over another economic agent in spite of not having the dominance of a product's or service's specific market, and uses that relative statute to abusively exploit that economic agent in a way that affects the functioning of the market or the structure of competition.

(2) For the analysis in hand, it is important to note that the concessionaire (Defendant) *"works under its own name and risk, acquiring the products and taking on the risk of their sale, which means its profit originates from the difference between how much it costs the concessionaire to buy the products from the grantor and the resale price, when it comes to sell them to the public, minus the commercialization costs."* Having this in consideration, the Appeal Court started by

analyzing whether this was a case of economic dependence, under article 4 of the Decree-Law no. 371/93, even though the concessionaire had legal autonomy.

Thus, the first step to address the existence of a situation of abusive exploitation of economic dependence by one undertaking towards another is to assess the existence of economic dependence of one undertaking towards another.

Given the fact that the legal provision does not state the prerequisites to evaluate the existence of a situation of economic dependence, the Court resorted to doctrine:

"a) brand's notoriety;

b) supplier's market share;

c) the significance of the supplier's products in the distributor's business volume;

d) the possibility to obtain «equivalent products» from other suppliers."

These prerequisites were, in principle, already implicit in the legal provision, resorting to teleological and systematic evaluation (as to forbidden practices that are prone to hinder, distort or restrict market competition).

a) Regarding the precondition of the brand's notoriety is concerned, the evaluation cannot be merely objective, for the conclusion would solely be that the level of economic dependence would be as high as the brand's reputation or notoriety in hand. Conversely, the Court considers that a relative/subjective evaluation must be undertaken, assessing the importance that that brand has in the business volume of the undertaking that is in a supposedly state of economic dependence.

b) As to the criterion of the grantor's share of the relevant market, the Court considers that it must be measured if such market share means such economic agent is a "mandatory supplier" of its competing distributors.

c) As to *the significance of the supplier's products* in the distributor's business volume, what matters is to evaluate the importance that the product at issue has in the concessionaire's business and if its business structure organization is directed or confined to marketing that product.

d) Regarding the "equal alternative evaluation", what is important to assess are the conditions that the concessionaire has at its disposal to find an alternative solution within the market and the costs associated with necessary business organization adjustments to integrate new solutions.

Moreover, taking into account that there is a commercial concession contract, the termination regime must be considered, given that a fixed-term contract gives the party, in general, the time necessary to consider the options at its disposal in case the contract is terminated. Conversely, if the contract is of indefinite duration (like the one in hand) it must be considered whether the way

the contract was terminated allowed the other party to adjust to that decision, even though the concessionaire cannot hope that the contract is *ad eternum*.

Therefore, the Appeal Court deliberated that *"(…) every piece of evidence points to the direction that the product over which the contract was celebrated was protected by a well-renowned brand in its relevant market (the tire market, brand "F…"), that that product represented about 1/3 of the Defendant's business volume and the Defendant was the brand's exclusive representative in the agreed territory (…).*

It can be also verified that, even though the products "F…" supplied by the Plaintiff only represent 1/3 of the Defendant's business volume, these were essential for its image in the market, which lead the undertaking to not give up on their commercialization in spite of the sacrifice of its economic results, which were of the Plaintiff's knowledge. Besides, F… was the only brand that produced jeep tires and radial construction trucks, which the Defendant used to sell until the termination of the contract (…)

Given the Plaintiff's inflexibility to review the pricing, the Defendant kept the interest in the concession contract, even though it kept on pushing for a revision (…)

It was also proven that there were other undertakings in the market selling the "F…" products at a lower price than the ones that the Plaintiff defined for the Defendant, even though the Defendant warned the Plaintiff about such fact, and even though the Plaintiff had the possibility to review the pricing, it decided not to. However, the proven facts do not attest the Plaintiff was a part of that parallel distribution.

Under these circumstances, the question in hand is whether the Defendant had an equivalent alternative within the market for the agreement it had set out with the Plaintiff; in other words, whether the Defendant could have had access to the type of products the Plaintiff supplied resourcing to other suppliers, in similar or even better conditions, without a considerable investment to adapt to the new reality in a reasonable period of time.

Having this in consideration, what we can conclude from the proven factuality is that the Defendant was not hindered from commercializing the Plaintiff's competing brands and even after the end of the contract it arranged supplies from other brands (…) It was also not proven that the Defendant had to undertake a serious adaptation to its business structure to adjust to that new reality, given that 2/3 of its business activity related to other brands. And even though the "F…" products were essential for the Defendant's market image, it was not proven that such image was affected by the end of the contract (…)

Therefore, according to the proven factuality, faced with the existence of parallel distribution of the "F…" tires, the Defendant opted to pressure the Plaintiff to review the pricing, instead of looking for an alternative solution within the market, which nothing proves were inexistent, at least since the sales started to fall, back in 1997."

The Appeal Court concluded that there was no state of economic dependence, given that the Defendant was unable to prove that it did not have an equivalent alternative within the market for the type of product the Plaintiff supplied. Therefore, under article 4 of Decree-Law no. 371/93, the Plaintiff's behaviour did not constitute an abusive exploitation prone to restrict competition.

Based on all the facts exposed above, the judges of Lisbon's Appeal Court found the Plaintiff's appeal partially admissible, whereas the Defendant's appeal was found totally inadmissible, counterbalancing the Defendant's credit against the Plaintiff's credits.