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THE NEW ANTITRUST RULES ON COOPERATIVE AND CONCENTRATIVE JOINT VENTURES ACCORDING TO REGULATION No.1310/97

The modifications introduced by Council Regulation No 1310/97 of 30 June 1997, published in *O.J.* L180 of 09/07/1997, were dealt in general in Newsletter No 3. Regulation No 1310/97, which entered into force on March 1, 1998 and contains, among others, provisions modifying Regulation No 4064/89 with respect to the notion of the joint venture which constitutes an operation of concentration. Two of the interpretative Commission Notices published in March of this year aimed at facilitating the interpretation of new provisions cover: "*The notion on the concept of full-function joint ventures*" and the "*Information on the assessment of full-function joint ventures pursuant to the competition rules of the European Community*" (in *O.J.* C66 of 02/03/1998).

Introduction

One of the main issues of Regulation No 4064/89 was constituted by the definition of the notion of concentration contained in Article 3 paragraph 2 stating, with reference to **joint ventures** in particular, that:

"*An operation, including the creation of a joint venture, which has as its object or effect the coordination of the competitive behaviour of undertakings which remain independent shall not constitute a concentration within the meaning of paragraph 1 (b).*

The creation of a joint venture performing on a lasting basis all the functions of an autonomous economic entity, which does not give rise to coordination of the competitive behaviour of the parties amongst themselves or between them and the joint venture, shall constitute a concentration ...".

This means that all the operations involving the creation of an autonomous economic entity could be regarded as

"concentrative", provided that the joint venture did not constitute the instrument for coordinating the behaviour of the parent companies. Under the terms of the second Commission Notice of December 1994 on the distinction between concentrative joint ventures on one hand, and co-operative joint ventures on the other hand, in order to be considered as an autonomous economic entity and therefore being concentrative, a joint venture:

"*... must operate on a market, performing the functions normally carried out by other undertakings operating on the same market. In order to do so the joint venture must have sufficient financial and other resources including finance, staff, and assets (tangible and intangible) in order to operate a business activity on a lasting basis. In respect of intellectual property rights it is sufficient that these rights are licensed to the joint venture for its duration. Joint ventures which satisfy this requirement are commonly described as '**full-function' joint ventures***" (*O.J.* C385/1 of 31 December 1994).

The requirement of absence of coordination of the competitive behaviour between undertakings was considered to be met in case of the withdrawal of such undertakings from the product market or from that part of the geographic market the joint venture was active on.

Therefore, in the original discipline, the consequence of the fact that an operation was qualified as suitable to give rise to a concentrative joint venture, was that the competitive assessment of the latter had to be referred to the substantial and procedural rules of Regulation No 4064/89 on the control of concentration, provided that the requisites for its application were satisfied under the terms of Article 1 of the Regulation itself.

Conversely, where, in addition to create a joint venture, the parent companies keep doing business on the same or on a connected market, or in case the operation consists in the creation of a joint venture and only some of the functional activities of the parent companies are transferred to the latter, so that the joint venture is not in the position to autonomously operate on the market in both cases, the **joint venture** has to be considered as **co-operative** and therefore would not fall within the scope of application of Regulation No 4064/89. The joint venture would thus fall within the (general) regime of Article 85 and therefore of Council Regulation No 17/62 of 06/02/1962, in *O.J.* 13 of 21/02/1962 (the application of which is not subject to the achievement of any threshold).

In this perspective, it usually happened that joint ventures, generating substantially analogous effects on the markets, were subject to a different discipline. This depended on the qualification given to the above mentioned parameters, not always being easily and immediately identifiable.

The application of different rules to the subject matter lead to consequences of a certain relevance.

First of all, while concentrative joint ventures could benefit from a rapid

evaluation process requiring the Commission to adopt a formal decision within one month from the notification (5 months if the case is raising serious doubts as to its compatibility with the common market), cooperative joint ventures were subject to the terms of Regulation No 17/62, providing for no time restriction (save for what set in the 1992 Commission internal rules limiting to two months the Commission evaluation, even if that deadline was not to be considered as peremptory, IP (92) December 23, 1992).

Secondly, the Commission had to take a definitive formal decision within the time limits imposed by the Merger Regulation, whilst the exemptions adopted in application of Article 85 in the form of the so called "comfort letters" only had temporary bearing and were therefore revocable, with a clear prejudice to the certainty of law.

Finally - and this is the most relevant aspect - there were different effects resulting from a declaration of incompatibilty in both cases. In fact, following an *ex ante* analysis, a joint venture bearing a Community dimension, and therefore subject to Regulation No 4064/89, could be prohibited or its approval be subject to substantial changes *requested* by the Commission, but virtually, **imposed** to the parties. (Among the joint venture cases that were prohibited see: Case *Aérospatiale - Alenia/De Havilland* of 2/10/1991 in *O.J.* L 334 of 5/12/1991; *MSG Media Service* of 9/11/1994, in *O.J.* L364 of 31/12/1994, *Nordic Satellite Distribution* of 19/07/1995 in *O.J.* L53 of 02/03/1996, *RTL/Veronica/Endemol* of 20/09/1995 in *O.J.* L134 of 5/06/1996; *Saint Gobain/Wacker-Chemie/Nom* of 04/12/1996 in *O.J.* L247 of 10/09/1997. With respect to joint venture cases declared compatible with conditions see among others: *Varta/ Bosch* of 31/07/1991, in *O.J.* L320 of 22/11/1991, Thyssen *Stahl/Krupp/Riva/Falck/Acciater* of 21/12/1994 in *O.J.* L251 of 19/10/1995; *RTL/Veronica/Endemol* of 17/07/1996 in *O.J.* L294 of 19/11/1996).

Conversely, the creation of a co-operative joint venture, subject to the exclusive evaluation of the general discipline of Article 85, unless submitted by the parties for a prior examination by the Commission for the granting of an exemption under the terms of Article 85.3, was subject to an *ex post* evaluation, which in case of a negative provision resulted in a declaration of annulment of the whole operation requiring the parties to wind up the joint venture.

Especially because of the uncertainties caused by the different treatments, the Commission aware of the problems raised by that distinction adopted a first Notice in 1990 and a second one in 1994, in order to better define the limits between concentrative and co-operative joint ventures. (See: *Commission Notice regarding the concentrative and co-operative operations under Council regulation (EEC) No. 4064/89 of December 21, 1989 on the control of concentrations between undertakings* in *O.J.* 90 C 203/10 of 14 August 1990 and *Commission Notice on the distinction between concentrative and co-operative joint ventures under Council Regulation*

(EEC) No 4064/89 of 21 December 1989 on the control of concentrations between undertakings in *O.J.* 94 C 385/01 of 31 December 1994). With the adoption of the subsequent Notices, the Commission provided for an identification of a typology of co-operative joint ventures which were to be considered as full function joint ventures. In this respect, the Commission tried to adopt a procedure with the aim to reduce as much as possible the incovenience caused by the fact that they had to undergo a different evaluation from the one provided for in Regulation No 4064/89 for concentrative joint ventures.

Nevertheless, notwithstanding the clarifications made by the Commission, several suggestions were put forward stressing the need for regime harmonisation measures guaranteeing equal treatment for both forms of joint venture.

It was not by chance that in the Green Paper the Commission itself suggested the opportunity to harmonise the assessment and evaluation of joint ventures abolishing the distinction between cooperative and concentrative joint ventures.

Modifications to Regulation No 4064/89 introduced by Regulation No 1310/97

The Green Paper of the Commission of 1996 indicated, together with the possible solutions, the grounds to the necessity for the Regulation to be amended. A consequence to this, was a proposal for a modified Regulation suggested by the Commission.

The European Parliament, supported by the opinion of the Economic and Social Committee, declared to be favourable to the Commission Proposal. Works continued until 30 June 1997, when the Council adopted Regulation No 1310/97 modifying Regulation No 4064/89 also with respect to the matter at issue.

In first instance, as already observed, Regulation No 1310/97 introduced a new definition of the notion of concentration which includes any operation suitable to produce a long lasting modification of the structure of the undertakings concerned. In that respect, Article 3 of the Regulation provides that: "*...The creation of a joint venture performing on a lasting basis all the functions of an autonomous economic entity shall constitute a concentration*".

According to Article 2 paragraph 4 of Regulation No 1310/97 it is moreover told that:

" To the extent that the creation of a joint venture constituting a concentration pursuant to Article 3 has as its object or effect the co-ordination of the competitive behaviour of undertakings that remain independent, such co-ordination shall be appraised in accordance with the criteria of Article 85(1) and (3) of the Treaty, with a view to establishing whether or not the operation is compatible with the common market.

In making this appraisal, the Commission shall take into account in particular:

- *whether two or more parent companies retain to a significant extent activities in the same market as the joint venture or in a market which is downstream or upstream from that of the joint venture or in a neighbouring market closely related to this market,*

- *whether the co-ordination which is the direct consequence of the creation of the joint venture affords the undertakings concerned the possibility of eliminating competition in respect of a substantial part of the products or services in question*" .

With respect to joint ventures, the new notion of concentration involves the elimination of the distinction between co-operative and concentrative joint ventures. As a consequence, the previous strict distinction which provided for the former to be subject to the general regime of Article 85 and qualified the latter as exclusively subject to the special rules of the Merger Regulation, no longer exists.

In fact, as regards the analysis of an operation of concentration, in the case in which a joint venture has the object or effect of coordinating the behaviour of undertakings which remain independent, i.e. the one previously defined as cooperative joint venture, the evaluation shall primarily be done according to the provisions of Regulation No 1310/97; however Article 85 of the Treaty shall also apply to evaluate the effects on the functioning of the market. Conversely, in the case of a full title joint venture, i.e. the one operating on an autonomous basis with respect to the parent companies (and previously defined as concentrative joint venture), the evaluation shall exclusively be done on the basis of Regulation No 1310/97.

This distinction finds an express confirmation in Recital 5 of the new Regulation. It states that:

"*it is appropriate to define the concept of concentration in such a manner as to cover operations bringing about a lasting change in the structure of the undertakings concerned; whereas in the specific case of joint ventures it is appropriate to include within the scope and procedure of Regulation (EEC) No 4064/89 all full-function joint ventures; whereas, in addition to the dominance test set out in Article 2 of that Regulation, it should be provided that the Commission apply the criteria of Article 85 (1) and (3) of the Treaty to such joint ventures, to the extent that their creation has as its direct consequence an appreciable restriction of competition between undertakings that remain independent; whereas, if the effects of such joint ventures on the market are primarily structural, Article 85 (1) does not as a general rule apply; whereas Article 85 (1) may apply if two or more parent companies remain active in the market of the joint venture, or, possibly, if the creation of the joint venture has as its object or effect the prevention, restriction or distortion of competition between the parent companies in upstream, downstream or neighbouring markets; whereas, in this context, the appraisal of all competition aspects of the creation of the joint venture must be made within the same procedure*".

Substantially the new discipline postulates the equivalence of cooperative and concentrative joint ventures, now both subject to the application of the Merger Regulation. While in the case of a concentrative joint venture the competitive assessment is only performed on the basis of the Merger Regulation, the evaluation of a co-operative joint venture, as to its compatibility, will primarily be performed **according to the provisions of the Regulation**. However, **in addition Article 85 shall be applied** when evaluating the legal effects that agreements between competitors can have on the market.

Interpretation of the modifications contained in Regulation No. 1310/97 also in the light of the new Commission Notice on the notion of joint ventures performing all the functions of an autonomous economic entity

In coincidence with the coming into force of Regulation No. 1310/97, i.e. 1 March 1998, the Commission adopted a Notice "on the concept of full-function joint ventures under Council Regulation (EEC) No 4064/89 on the control of concentrations between undertakings" (the so called **full function** joint venture).

Given the innovative character of the discipline, Article 2 of the Notice specifies that the same:

"*replaces the Notice on the distinction between concentrative and cooperative joint ventures. Changes made in this Notice reflect the amendments made to the Merger Regulation as well as the experience gained by the Commission in applying the Merger Regulation since its entry into force on 21 September 1990*".

As far as the notion of joint venture is concerned, the Notice provides that: "*joint ventures are undertakings which are jointly controlled by two or more other undertakings*". As previously observed, in order to constitute a concentrative joint venture shall satisfy both the requisites of joint control and lasting change in the structure of the undertakings concerned. In that respect, under the terms of Article 11 of Notice 98/C 66/01, a joint venture is considered as having the characteristics of *"full-function" joint ventures* when it performs, on a lasting basis, all the functions of an autonomous economic entity, thus bringing about "*a lasting change in the structure of the undertakings concerned*".

Under the terms of Article 12 of the Notice at issue, this essentially means that a joint venture must operate on a market, performing the functions normally carried out by undertakings operating on the same market. In order to do so the joint venture must have a management dedicated to its day-to-day operations and access to sufficient resources in order to conduct its business activities on a lasting basis.

A joint venture is not a full-function one if it only takes over one specific function within the parent companies' business activities **without having access to the market**. This is the case, for example, with joint ventures limited to R & D or production. Such joint

ventures are **auxiliary** to their parent companies' business activities. This also applies when a joint venture is essentially limited to the distribution or sale of its parent companies' products and, therefore, principally acts as a sales agency. However, the fact that a joint venture makes use of the distribution network or outlet of one or more of its parent companies normally does not disqualify it as 'full-function` as long as the parent companies are only acting as agents of the joint venture. In that respect, under the terms of Article 14:

"*The strong presence of the parent companies in upstream or downstream markets is a factor to be taken into consideration in assessing the full-function character of a joint venture where this presence leads to substantial sales or purchases between the parent companies and the joint venture*".

The fact that the joint venture relies almost entirely on sales to its parent companies or purchases from them only for a start-up period does not normally affect the full-function character of the joint venture. Such a **start-up period** may be necessary in order to establish the joint venture on a market. Normally this period of time shall not exceed three years, depending on the specific conditions of the market involved. (See case *EDS/Lufthansa* of 11/05/1995, in *O.J.* C163 of 29/06/1995; *Nokia/Autoliv* of 05/02/1996, in *O.J.* C069 of 07/03/1996).

Moreover, sales to the parent companies are to be made on the basis of normal commercial conditions.

Furthermore, Article 15 clarifies that the joint venture must be intended "*to operate on a lasting basis*". According to the Commission the fact that the parent companies commit to the joint venture the resources as described in Articles 12, 13, 14 of Notice 98/C66/04, normally proves that there is indeed such an intention..

If the agreement specifies a period for the duration of the joint venture, this does not prevent the joint venture from being considered as full function joint venture, provided that this period is sufficiently long to bring about a lasting change in the structure of the undertakings concerned.

By contrast, the joint venture will not be considered to operate on a lasting basis where it is established for a short term. This would be the case, for example, where a joint venture is established in order to construct a specific project, such as a power plant, but it will not be involved in the operation of the plant once its construction has been completed.

As regards the provisions that find application with respect to the assessment of the creation of the joint venture together with the market, as already observed, Article 2 paragraph 4 of the Regulation specifies that the co-ordination of the competitive behaviour of undertakings that remain independent shall be appraised in accordance with the criteria of Article 85(1) and (3) of the Treaty. This is also confirmed by Article 16 of the Commission Notice adding that:

" Further, the creation of a full-function joint venture may as a direct consequence lead to the coordination of the competitive behaviour of undertakings that remain independent. In such cases Article 2(4) of the Merger Regulation provides that those cooperative effects will be assessed within the same procedure as the concentration. This assessment will be made in accordance with the criteria of Article 85(1) and (3) of the Treaty with a view to establishing whether or not the operation is compatible with the common market. The applicability of Article 85 of the Treaty to other restrictions of competition, that are neither ancillary to the concentration, nor a direct consequence of the creation of the joint venture, will normally have to be examined by means of Regulation No 17".

Final Considerations

Finally, the major innovation brought by the new Merger Regulation with respect to joint ventures is to be seen in the fact that all joint ventures, whichever their nature, fall within the assessment based on Regulation No. 4064/89 as modified by Regulation 1310/97 on the control of concentration.

As a consequence, the Regulation also applies to joint ventures formerly defined as "co-operative". This implies that the former are subject to both the term for the notification set out in Article 4 ("*Concentrations with a Community dimension defined in this Regulation shall be notified to the Commission not more than one week after the conclusion of the agreement...*"), as well as the procedures for the appraisal and authorisation of the creation of a joint venture as set out in the light of Commission Regulation (EC) No 447/98 of 1 March 1998 *on the notifications, time limits and hearings provided for in Council Regulation (EEC) No 4064/89 on the control of concentrations between undertakings* in *O.J.* L61/98 of 2 March 1998.

The second Commission Notice 98/C66/06 clarifies that for joint ventures other than full function joint ventures which do not have a Community dimension "*There is no change in the provisions applicable to joint ventures*", i.e. Council Regulations No 17, (EEC) No 1017/68, (EEC) No 4056/86 and (EEC) No 3975/87. Hence, the regulations that the Commission adopted for the implementation of those Council Regulations, namely Regulations (EC) No 3385/94, No 99/63/EEC, (EEC) No 1629/69, (EEC) No 1630/69, (EEC) No 4260/88 and (EEC) No 4261/88, also cease to be applicable to these joint ventures.

Brief comments on the impact of Regulation No 1310/97 on the Italian legal framework in the light of the principles contained in L. 10 October 1990 No 287.

The Italian attitude with respect to the treatment of joint ventures is particularly interesting, since in the qualification and evaluation of the effects deriving from the creation of a joint venture, somehow an opposite trend can be witnessed with respect to the process followed by the Community. In fact, originally the Italian law did not

provide for a distinction between **co-operative** and **concentrative** joint ventures. In this respect it should be recalled that Article 5 lett. c) of L. 287/90 states that an operation of concentration shall be deemed to arise also "*when two or more persons undertakings create a joint venture by setting up a new company*".

In the frame of a formal analysis of Article 5 lett. c) one would assume that the creation of any joint venture shall be deemed as a concentration, regardless from any further distinction.

At the same time however, the principle contained in Article 1 paragraph 4 expects the Competition Authority to refer to the principles of Community law in competition matters as well.

Therefore, in the absence of any provision by the legislator, the question arose whether the same distinction between cooperative and concetrative joint ventures as the one provided for in Regulation No 4064/89 could apply and secondly, whether a concentrative joint venture, in order to be a concentrative one, should perform all the functions of an autonomous economic entity.

In the light of what set out in Article 1 paragraph 4, the Italian Competition Authority is compelled to apply the Community law. Since no position was taken by the national legislator, with respect to Article 5 the Competition Authority applied the principles of Community law with a restrictive interpretation i.e. intending Article 5 as only being meant to govern the creation of a concentrative joint venture.

From that restrictive point of view, the Competition Authority stated that the creation of a concentrative joint venture requires the joint venture to perform on a lasting basis all function of an autonomous economic entity and implies that there is no coordination of the competitive behaviour between the parent companies nor between a parent company and the joint venture; therefore, "*if the parties do not intend to create a joint venture under the terms of Article 5, paragraph 1 lett c) of Law 287/90, but rather to coordinate the competitive behaviour of independent undertakings, the case at issue is not deemed to be a concentration under the terms of Article 5 paragraph 3 of law No 287/90*", but rather to fall within the scope of application of Article 2 governing agreements (see case *Benetton/CSP*, in Bull. No 7/91)

It can therefore be affirmed that, notwithstanding the relevant differences in the wording, the correct interpretation of paragraph 4 of Article 5 reflects at national level the distinction between co-operative and concentrative joint ventures as provided for in Community law.

In the course of the years, though not giving up the opposition between cooperative and concentrative joint ventures, the Competition Authority, too uniformed itself to the evolution followed by the Commission, aiming at abandoning a strict distinction only based on relationships between parent companies and joint venture and focusing on the resources commit to the joint venture within the new economic entity and on the effects of such integration on the reference market.

An example is given by *Alitalia/Malev*, where the Authority did not identify any vertical coordination between the parent company Alitalia and the joint venture Malev by virtue "*of the relevant involvement of Alitalia in the management of Malev*". As a consequence, the fact that Alitalia was taking part "*to the rationalisation and to the development of routes and services supplied by itself (...) constituted a further confirmation of the fact that the acquisition of joint control of Malev by Alitalia (…) did not give rise to coordination of the competitive behaviour of two independent entities*".

With the introduction of Regulation No 1310/97 and particularly of the interpretative Notices, the Competition Authority will see itself forced to furtherly change its attitude, in the sense of recognising the full applicability of what is set out in Article 5 lett. c) with respect to the creation of any joint venture, provided that the latter can be considered as a full function joint venture under the terms of the Commission Notice on "*the notion of joint ventures performing all the functions of an autonomous economic entity*".

Article 5 lett c) will therefore not only be applicable to concentrative joint ventures, but also to the creation of joint ventures which give rise to the coordination of the competitive behaviour of two independent entities, provided that the joint venture performs the functions of an autonomous economic entity. It will be interesting to see how the Italian Competition Authority will change its approach in applying Article 5 lett.c) in the light of previous differently oriented precedents.

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