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Cartel Liability in the EU: What Can Parent Companies Say in Their Defence?

Steve Spinks and Anouck Meier of Sidley Austin give their insight into how the European Commission establishes parent-company liability for the antitrust misbehaviour of subsidiaries.

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CARTEL LIABILITY IN THE EU: WHAT CAN PARENT COMPANIES SAY IN THEIR DEFENCE?

When the children misbehave, the parents get punished.

Steve Spinks and **Anouck Meier**[1] examine the issue of cartel liability in the EU

Parents get blamed for their children's bad behaviour all the time. They often find themselves taking responsibility for the troubles caused by their children's wrongs. Single moms in particular might have to put up with getting blamed for the wrongdoing of their toddlers, teenagers and – if you happen to be a mother *company* – daughter undertakings. In the European Union, attribution of liability and the ensuing implications for the level and payment of fines has given parent companies a reason to worry about what their offspring might have been up to.

In other jurisdictions, any such questions regarding the proverbial piercing of the corporate veil get frowned upon. In the United States, for example, the question of parent company liability has a simple and straightforward answer: corporate separateness generally prevails and any imputation of liability to another legal entity can only be resorted to as an "extreme remedy."[2] European companies and their counsel, however, have been heedfully keeping an eye on the developments in this area of the law – and they have every reason to be on their guard. If they are held liable as a parent company, the 10-percent cap on fines is calculated on the basis of a higher turnover. Moreover, the attribution of liability on a higher level may facilitate actions for damages against parent companies and encourage complainants to bring such actions.

The European Commission ("Commission"), being both the investigator and prosecutor, has taken a broad view of its own ability to impute liability on parent companies. The issue of parental liability has, however, been hotly contested before the Community Courts. The majority of judgments concern annulment actions against European Commission *cartel* decisions. In the judgment of the European Court of Justice ("ECJ")[3] of 10 September 2009 in the Akzo Nobel case,[4] the Community judicature clarified joint and several liability of parent companies for cartel infringements committed by their wholly owned subsidiaries.

What does the well-developed EU law on the imputation of liability on parent companies say? The subjects of Article 101 TFEU[5], the Commission's main weapon against alleged cartels, are "undertakings," a concept that covers any entity engaged in an economic activity, regardless of its legal status and the way in which it is financed. This means that the notion of an undertaking in EU law is quite distinct from the notion of corporate legal personality in national commercial, company or fiscal law. It must be understood as designating a single economic entity even if it consists of several natural or legal persons. From the viewpoint of the principle of personal responsibility, it seems only logical that such an entity should be put on the stand when it has infringed competition law. It is

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exactly in this kind of circumstances – where a parent company and its subsidiary are found to constitute a single economic unit – that the issue of joint and several liability arises.

For this reason, the Commission will generally not seek to attach liability for being involved in an infringement only to one specific subsidiary. Rather, it will usually try to ensure that responsibility is attributed at the highest possible level within the undertaking. Typically, this means that the Commission will hold parents liable for the actions of their wholly owned subsidiaries, precisely because the Commission considers them to be part of one and the same undertaking. Therefore, in the case of a wholly owned subsidiary under investigation, the issue revolves around the question of whether or not it is part of a broader economic unit – an "undertaking" – with its parent, and whether therefore they can be held liable together.

The test that has developed through the case law focuses on the following question: Does the subsidiary determine autonomously its own market conduct or, rather, does the parent company exercise a decisive influence on its subsidiary's commercial conduct?[6] The reasoning behind the test is that, if it is found that the parent exercises a decisive influence, it must then follow that it is part of the same economic unit, and therefore the same undertaking as its subsidiary. The fact that they are part of a single undertaking then permits the Commission to hold them jointly liable, without also having to prove the personal involvement of the parent company in the infringement.

AG Kokott's reasoning in her Akzo Nobel opinion suggests that influence of some higher level of intensity may still be consistent with a subsidiary's autonomy

According to the case law,[7] in the specific scenario where a parent company owns, directly or indirectly, the totality (or almost the totality) of the shares of a subsidiary, the Commission is allowed to presume that the parent company in fact does exercise a decisive influence (hereafter the "Parent-Subsidiary Presumption"). The Parent-Subsidiary Presumption is based on the fundamental premise that a wholly owned subsidiary receives instructions from its parent company and will follow those instructions so that the market conduct of both the parent company and the wholly owned subsidiary is "unified." This presumption allows the Commission to hold the parent company liable for the subsidiary's conduct by simply proving that the parent company owns all or almost all of the shares of a subsidiary – unless the parent company is able to rebut the presumption and show that the subsidiary acted independently on the market.

The General Court (until December 1, 2009 called the Court of First Instance) in *Avebe*[8] stated that the fact that two shareholders each held 50 percent in a subsidiary, was sufficient to conclude that the Parent-Subsidiary Presumption applied and that the two shareholders jointly exercised a decisive influence on the subsidiary. It should be noted, however that the Court's stance was based on the specific facts of the case, which involved a purely contractual entity without separate legal personality. That entity had all the characteristics of a general partnership, in which the two 50/50 partners jointly made all decisions for and assumed all the commitments of the partnership. Under those circumstances, applying the Parent-Subsidiary Presumption was certainly not a great stretch.

The *Avebe* case raises issues about whether the Parent-Subsidiary Presumption can apply in the case of minority shareholdings in a corporation that <u>does</u> have its own legal personality. The Commission's decisional practice recognises the distinct situation of a corporation that is owned by two (or more) independent shareholders. In its 2005 *Rubber Chemicals* Decision[9], the Commission acknowledged that having two 50/50 shareholders with blocking rights over certain strategic decisions establishes a presumption that the company is in fact a *separate* undertaking from its shareholders. This "Separate Undertaking Presumption" should be even stronger where the creation of such a corporation is cleared under the Merger Regulation, which 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… ."[10] Some recent cases[11] suggest, however, that the Commission, in adopting what seems like an ever-expanding theory of "liability by association", has extended its scope of targets to minority shareholders in corporations. A number of relevant cases are currently pending before the General Court – a judgment in one of them might shed some welcome light on this particular conundrum.

Let's take a step back, however, and consider how a "single mom" with a "problem child" – a parent company of a badly behaved wholly owned subsidiary – can rise to her defence, i.e. how she can rebut the Parent-Subsidiary Presumption. In other words, when has the child grown up to the point where he takes his own decisions without having to obtain Mom's blessing – or, to put it in the terms used by the ECJ, without being subject to Mom's "decisive influence"?

In reality, it has proven extremely difficult to rebut the presumption. In fact, until now, not a single parent of a wholly owned subsidiary has been successful in doing so. The Commission's rationale seems to be that rebutting the presumption is difficult, because it is based on "what generally happens" and, therefore, companies have to produce proof of "very exceptional, abnormal and extraordinary circumstances" in order to rebut it.[12] However, proof of such highly exceptional or abnormal circumstances seems to render the Presumption irrebuttable but for a *probatio diabolica*.

To rebut the presumption a parent would presumably need to start by demonstrating that it did not have any right to interfere in the subsidiary's commercial policies. Alternatively, a parent which had such a right might have to show that it did not interfere and never gave instructions or guidelines regarding pricing, production, sales or other aspects of the subsidiary's operational commercial policy. The parent's case would no doubt be improved if it could demonstrate with cogent evidence that the parent did not instruct the subsidiary to participate in the anticompetitive conduct and/or that the subsidiary did so without the parent's knowledge.

It appears, however, that even proof of these factors may not suffice to establish that the parent and its subsidiary were not a single economic unit. The ECJ in the Akzo Nobel case (mentioned above) appears to have endorsed the views of Advocate General ("AG") Kokott. The AG stated that "the decisive factor is whether the parent, by reason of the intensity of its influence, can direct the conduct of its subsidiary to such an extent that the two must be regarded as one economic unit."[13] She emphasised, and the ECJ accepted, that the absence of a single commercial policy can be established only on the basis of an assessment of the totality of all the economic, organisational and legal links which tie the parent and the subsidiary.

For its part there are suggestions that the Commission would consider that only a demonstration of zero – or almost zero – influence could suffice to rebut the presumption. For instance, in recent hearings in a case before the General Court,[14] the Commission's counsel suggested that a contract which prevents a parent company from exercising control at all, could rebut the presumption. The Commission's counsel also mentioned scenarios of state intervention or regulatory measures which would impede intervention. Counsel also suggested that proof that the parental link was limited to a short term investment, legal obligations or contractual obligations vis-à-vis third parties could also contribute to a valid rebuttal.

AG Kokott's reasoning in her Akzo Nobel opinion suggests, however, that influence of some higher level of intensity may still be consistent with a subsidiary's autonomy. Her opinion suggests that the presumption can be rebutted by cogent evidence demonstrating that the wholly owned subsidiary's management had a wide degree of latitude in practice to determine its corporate strategy, set its operational policies, handle its own financing and decide upon and engage its own human resources. That kind of latitude might be relatively rare in the case of wholly owned <u>sales</u> subsidiaries, but it may well be more common in the case of wholly owned <u>production</u> subsidiaries. It is certainly common in the case of full function joint ventures reviewable under the Merger Regulation and other structural joint ventures. It remains to be seen, however, what degree of latitude would suffice to demonstrate that the parent and its wholly owned subsidiary are not a single economic unit. ■

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Footnotes

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2 Sonora Diamond Corp. v. Superior Court, 83 Cal. App. 4th 523, 539 (2000).

3 Recently renamed the Court of Justice of the European Union by the Lisbon Treaty, which entered into force on December 1, 2009.

4 Case C-97/08 P Akzo Nobel and Others v Commission [2009] ECR I-0000.

5 The Lisbon Treaty, which took effect on 1 December 2009, amended and renumbered the Treaty on the European Union and the Treaty establishing the European Community ("EC Treaty"). Articles 81 through Article 86 of the EC Treaty have been renumbered to Articles 101 to 106 and the Treaty has also been renamed to the Treaty on the Functioning of the European Union (abbreviated to TFEU). Accordingly, Article 81 EC will now be referred to as Article 101 TFEU, Article 82 EC is now Article 102 TFEU and Article 86 is Article 106 TFEU.

6 See judgment of the Court of Justice in case 48/69 ICI v Commission [1972] ECR 619, ¶. 133.

7 Case 107/82, AEG v Commission [1983] ECR 3151, at paragraphs 50 and 51.

8 Case T-314/01 Avebe v Commission [2006] ECR II-3085.

9 Commission Decision of 21 December 2005 (Case COMP/F/38.443 – Rubber Chemicals), published on DG Comp website.

10 Council Regulation No 139/2004, OJ 2004 L 24/1, Art. 3(4).

11 Case T-282/02 Cementbouw v Commission [2006] ECR II-319, ¶. 62.

12 Case T-39/07 ENI v Commission, pending, not yet reported.

13 Case C-97/08 Akzo Nobel v Commission, Opinion of Advocate General Kokott of 23 April 2009, ¶.93.

14 Case T-45/07 for Unipetrol v Commission, pending, not yet reported.