GETTING THE DEAL THROUGH

Vertical Agreements

The regulation of distribution practices in 34 jurisdictions worldwide

2008

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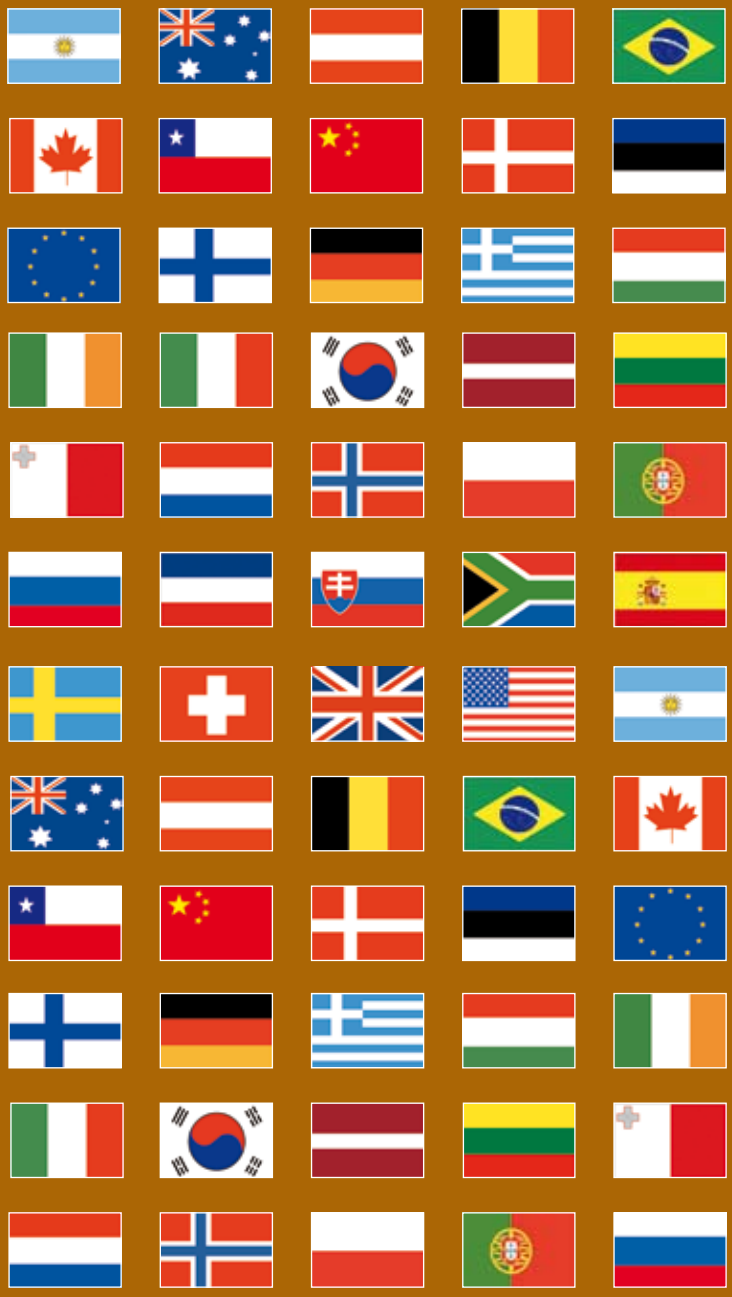

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GLOBAL COMPETITION REVIEW

Switzerland

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1 What are the legal sources that set out the antitrust law applicable to vertical restraints?

The relevant legislation in Switzerland is the Federal Act on Cartels and Other Restraints of Competition of 6 October 1995 (ACart). In addition, the Swiss Competition Commission (ComCo) issued an amended notice regarding the competition law treatment of vertical agreements of 2 July 2007, which entered into force on 1 January 2008 (Verticals Notice, VN). Both legal sources are available in English on ComCo's website (see www.weko.admin.ch/publikationen/00213/index.html?lang=en).

2 List and describe the types of vertical restraints that are subject to antitrust law. Are those terms defined and how? Is the concept of vertical restraint itself defined in the antitrust law?

ACart, article 5, distinguishes three types of unlawful agreements in terms of the intensity of the restraint of competition:

- agreements that do not significantly affect competition are lawful;
- agreements that significantly affect competition may be justified on grounds of economic efficiency; and
- agreements that eliminate effective competition are unlawful.

ACart, article 5(4) defines types of vertical agreements presumed to lead to the elimination of effective competition. Accordingly, agreements between undertakings on different market levels regarding minimum or fixed prices as well as clauses in distribution agreements regarding the allocation of territories, provided distributors from other territories are prohibited from sales into these territories, are presumed to eliminate effective competition. Although no precedents exist so far, the rules in ACart, article 5(4) are widely held to declare unlawful prohibitions of passive sales into exclusive territories (ie, absolute territorial protection).

The concept of vertical restraints itself is defined in VN, article 1. Vertical agreements include binding or non-binding agreements and concerted practices between two or more enterprises at different levels of the market, which concern the commercial terms on which the relevant enterprises may purchase, sell or distribute goods or services.

3 Are there particular rules or laws applicable to the assessment of vertical restraints in specific sectors of industry? If so, please identify the sectors and the relevant sources.

In the motor vehicle sector, there is a special Notice on the Competition Law Treatment of Vertical Agreements in the Motor Vehicle Trade of 21 October 2002 (also on ComCo's website).

4 Is the only objective pursued by the law on vertical restraints economic, or does it also seek to protect other interests?

The main objective pursued by the law on vertical restraints is the protection of competition. However, there also is a Notice of 19 December 2005 regarding agreements with limited market effects meant to provide a safe harbour for small and medium-sized enterprises (SME Notice).

5 What entity or agency is responsible for enforcing prohibitions on anti-competitive vertical restraints? Do governments or ministers have a role?

In Switzerland, only federal administrative bodies have the power to implement the ACart, namely, the ComCo and its Secretariat. The main administrative body enforcing the ACart is the ComCo. It is independent of the federal government (ACart, article 19(1)). The ComCo is the sole administrative body having power to issue decisions prohibiting anti-competitive vertical restraints and to impose fines (ACart, article 53(1)).

The Secretariat of the ComCo conducts investigations and preliminary investigations and prepares the ComCo's decisions (ACart, article 23(1)). The Secretariat has no power to open investigations without the consent of a member of the ComCo's presiding body (ACart, article 27(1)).

6 What is the relevant test for determining whether a vertical restraint will be subject to antitrust law in your jurisdiction?

The Swiss antitrust law applies to vertical restraints whose effects are felt in Switzerland, even if they originate in another country (ACart, article 2(2)).

7 To what extent does antitrust law apply to vertical restraints in agreements concluded by public or state-owned entities?

Swiss antitrust law applies equally to vertical restraints in agreements concluded by public or state-owned entities (ACart, article 2(1)). However, to the extent that particular provisions establish an official market or price system or that provisions entrust certain enterprises with the performance of public-interest tasks, by granting them special rights, such provisions take precedence over the provisions of the ACart (ACart, article 3(1)).

8 Are there any general exceptions from antitrust law for certain types of vertical restraints? If so, please describe.

The ComCo regards vertical agreements other than those explicitly listed in VN, sections 10(1) and 12 usually as non-significant restrictions of competition, provided the market share of all the

enterprises involved does not exceed a threshold of 15 per cent on any of the relevant markets (VN, section 13(1)).

9 When assessing vertical restraints under antitrust law (or when considering the application of exceptions from antitrust law) does the relevant agency take into account that some agreements may form part of a larger, interrelated, network of agreements or is each agreement assessed in isolation?

If competition in the relevant market is restricted by the cumulative effects of several similar parallel vertical distribution networks, the market share threshold of 15 per cent for non-significant restrictions of competition (see question 8) is reduced to 5 per cent. As a rule, there is no cumulative foreclosure effect if less than 30 per cent of the relevant market is covered by similar parallel vertical distribution networks (VN, section 13(2)).

10 In what circumstances does antitrust law apply to agency agreements in which an undertaking agrees to perform certain services on a supplier's behalf in consideration of a commission payment?

In Swiss antitrust law, there are no special provisions regarding agency agreements. Although there are no judicial precedents, it is likely that the Swiss authorities would apply similar principles as in European competition law.

11 Is antitrust law applied differently when the agreement containing the vertical restraint also contains provisions granting intellectual property rights (IPRs)?

Swiss antitrust law does not apply to effects on competition that result exclusively from laws governing intellectual property (ACart, article 3(2)). However, this exception does not apply to import restrictions based on intellectual property rights. VN, section 8(3) explicitly states that the Notice does not apply to vertical agreements containing provisions which relate to the assignment or use of intellectual property rights, provided that those provisions constitute the primary object of such agreements and provided that they are not directly related to the use, sale or resale of goods or services by the buyer or its customers.

12 In what circumstances does antitrust law apply to agreements between a parent and a related company?

Antitrust law applies to agreements between a parent and a related company as long as the related company does not belong to the same group. If a parent company effectively controls its affiliated companies, for example, by the majority of capital or of voting shares, the whole group as such is regarded as an independent economic entity. The ACart does not apply to group-internal relationships (group privilege). However, it should be noted that in a recent publication a member of the Secretariat cast doubt on whether or not the group privilege will be further accepted.

13 Can the legality under antitrust law of a given vertical restraint change over time?

The legality of a given vertical restraint may change over time, for example, because of a change in the market position of a supplier. However, any such increase in a given market share would have to be considerable because exceeding the 15 per cent de minimis threshold (VN, section 13(1)) does not necessarily alter the antitrust assessment.

14 Briefly explain the analytical framework that applies when assessing vertical restraints under antitrust law.

In Switzerland, certain types of vertical restraints are never permissible as they are considered as per se unlawful. These vertical restrictions are fixed or minimum resale prices as well as absolute territorial protection. These types of restrictions (cf ACart, article 5(4); VN, section 10(1)) may be directly sanctioned with fines and cannot be justified as having only a limited market effect on the basis of the SME Notice (No. 3(2)(b)).

Other vertical agreements that significantly affect competition in the market for certain goods or services are unlawful, unless they can be justified on grounds of economic efficiency (ACart, article 5(1)). Consequently, there is no rule-of-reason analysis to be undertaken but rather an efficiency test. According to ACart, article 5(2), an agreement is deemed to be justified on grounds of economic efficiency when:

- it is necessary in order to reduce production or distribution costs, improve products or production processes, promote research into or dissemination of technical or professional know-how, or exploit resources more rationally; and
- such agreement will not in any way whatsoever allow the enterprises concerned to eliminate effective competition.

The list of criteria for the efficiency test in ACart, article 5(2) is exhaustive. Further justification grounds such as general political considerations, cultural aspects or public health cannot be taken into consideration within the framework of article 5(2). According to ACart, article 8, agreements affecting competition whose unlawful nature has been ascertained by the competent authority may be authorised by the Federal Council at the request of the enterprises concerned if, in exceptional cases, they are necessary in order to safeguard compelling public interests.

The conditions under which vertical agreements affecting competition are generally deemed to be justified on grounds of economic efficiency may be determined by way of ordinances or communications (ACart, article 6(1)), for example, for agreements on research and development or on specialisation.

15 Is there a block exemption or safe harbour that provides certainty to companies as to the legality of vertical restraints in certain conditions? If so, please explain how this block exemption or safe harbour functions.

The VN is meant to provide certainty to companies, but concentrates rather on the illegality than on the legality of vertical restraints under specific conditions. Like its European counterpart, the VN contains some sort of 'safe harbour' provision. However, the term 'safe harbour' is misleading in that the VN expressly states that the benefit of the 'safe harbour' is only granted 'as a general rule' rather than without exception, thus depriving the 'safe harbour' of its primary role of granting certainty to the companies relying on it. Also, the provision is drafted so narrowly as to exclude from its scope the vast majority of vertical agreements that affect competition.

Formally, the 'safe harbour' works as follows: agreements containing no blacklisted practices are, generally, considered to be 'too insignificant to affect competition' (and therefore legal) if the market shares of the parties to the agreement are below 15 per cent (VN, section 13(1)) unless a cumulative effect in the market resulting from several parallel vertical agreements can be observed, in which case these market share thresholds drop to 5 per cent (VN, section 13(2)). However, if the market share of the supplier does not exceed 30 per cent, as a general rule any vertical agreement ist deemed to be 'justified', namely legal (VN,

section 15(2)), provided that it does not contain any black-listed practices. The latter comprise, inter alia, the direct or indirect setting of minimum or fixed prices for resale, the restriction of active or passive sales to end-users by members of a selective distribution system operating at the retail level of trade or non-compete obligations the duration of which is indefinite or exceeds five years (see the list in VN, section 12, including exceptions).

VN, section 15 sets out the framework for assessing the justification of a restriction according to ACart, article 5(2). This may be particularly the case if an agreement enhances economic efficiency, for example through a more efficient system of distribution in terms of product upgrading or improvements in manufacturing processes, or by lowering distribution costs – and the restriction of competition is necessary in order to achieve this goal (see questions 17 to 28).

16 What are the consequences of an infringement of antitrust law for the validity, or enforceability by one of the parties, of a contract containing prohibited vertical restraints?

A contract containing prohibited vertical restraints (a per se violation or a substantial restriction that cannot be justified) is null and void based on Swiss civil law (Code of Obligations, article 20).

17 How is the restricting of the buyer's ability to determine its resale price assessed under antitrust law?

Restricting the buyer's ability to determine its resale price by fixed or minimum prices is a per se violation under Swiss antitrust law and can be directly sanctioned by imposing a fine. In return, imposing a maximum sale price or recommending a sale price by the supplier is possible, provided that they do not amount to a fixed or minimum sale price as a result of pressure of, or incentives offered by, any of the parties.

18 Have there been any developments in your jurisdiction in light of the landmark 2007 judgment by the US Supreme Court in *Leegin Creative Leather Products Inc v PSKS Inc*? If not, is any response or development anticipated?

There have not yet been any developments in Switzerland following the US Supreme Court judgment in *Leegin*; quite the contrary. Whereas in the US resale price maintenance may no longer be treated as a per se violation but rather be assessed under the rule of reason, the VN moves even price recommendations into the spotlight and stipulates that they will in the future be regarded with increased suspicion by the ComCo (VN, section 11). Therefore, it is unlikely that any response to *Leegin* will happen. Fixing minimum resale prices is and will continue to be a hard-core, per se violation under Swiss law and may entail considerable fines.

19 How is the restriction of the territory into which a buyer may resell contract products assessed under antitrust law? In what circumstances (if any) may a supplier require a buyer of its products not to resell the products in certain territories?

A supplier may restrict active sales by the buyer of its products into the exclusive territory reserved to the supplier or granted by the supplier to another buyer, provided that passive sales are still possible without restriction (VN, section 12(b)(i)), namely provided that the supplier or buyer remain able to fulfil unsolicited orders from individual customers and that distribution through the customers of the buyer is likewise not restricted.

20 Explain how restricting the customers to whom a buyer may resell contract products is assessed under antitrust law. In what circumstances (if any) may a supplier require a buyer of its products not to resell the products to certain customers?

A supplier may restrict active sales by the buyer of its products to a customer group exclusively reserved to the supplier or granted by the supplier to another buyer, provided that passive sales are still possible without resctriction (VN, section 12(b)(i)), namely provided that the supplier or buyer remain able to fulfil unsolicited orders from individual customers and that distribution through the customers of the buyer is likewise not restricted.

21 How is the restricting of the uses to which a buyer (or a subsequent buyer) puts the contract products assessed under antitrust law?

A supplier may restrict the buyer's ability to sell components supplied for the purposes of incorporation to customers who would use them to manufacture rival products, namely the same type of products as those produced by the supplier (VN, section 12(b)(iv)).

22 Briefly explain how agreements establishing 'selective' distribution systems are assessed under antitrust law.

Restrictions on cross-supply between authorised dealers within a selective distribution system, also when dealers at different levels of the market are involved, are deemed significant restrictions of competition (VN, section 12(d)). Similarly, the restriction of active or passive sales to end-users by members of a selective distribution system operating at the retail level of trade is also regarded as a significant restriction of competition (VN, section 12(c)). But authorised dealers within a selective distribution system may be restricted in their freedom to resell the relevant goods or services to unauthorised dealers (VN, section 12(b)(iii)).

23 How is the restriction of the buyer's ability to obtain the supplier's products from alternative sources assessed under antitrust law?

Any direct or indirect obligation of a buyer to purchase from the supplier or from another company designated by the supplier more than 80 per cent of the buyer's total purchases of the contract goods or services and their substitutes on the relevant market are regarded as non-compete obligations (VN, section 6). Such non-compete obligations that are agreed to for more than five years or for more than one year after termination of the vertical agreement are deemed to be significant restrictions of competition.

24 Explain how restricting the buyer's ability to stock products competing with those supplied by the supplier under the agreement is assessed under antitrust law.

Restrictions of the members of a selective distribution system not to sell different brands are possible, as long as the restriction is not targeted at the brands of particular competing suppliers (VN, section 12(h)).

25 How is the requiring of the buyer to purchase from the supplier a certain amount, or minimum percentage, of its requirements, of the contract products assessed under antitrust law?

An obligation of the buyer to purchase from the supplier more than 80 per cent of his requirements of the contract products, based on the value of his total purchases in the previous calendar year, is regarded as non-compete provision (see question 23).

26 Explain how restricting the supplier's ability to supply to other buyers, or sell directly to consumers, is assessed under antitrust law.

If the buyer's market share does not exceed 30 per cent on the relevant market, he may restrict the supplier not to supply the contract products to other buyers (exclusive supply obligation. VN, section 15(2) does not address the restriction of the supplier. However, it seems quite likely that the ComCo may apply this provision by way of analogy or, alternatively, may refer to article 3(2) of the EU Verticals Block Exemption Regulation No. 2790/1999, which was used as model; cf VN, recital 11). Beyond the 30 per cent market share threshold, an individual assessment has to be undertaken whether or not the restriction can be justified on economic efficiency grounds (VN, section 15(3)).

Members of a selective distribution system must not be restricted to actively or passively sell to consumers (VN, section 12(c)). Suppliers must not be restricted either to sell components or spare parts to final consumers or repair workshops (section 12(e)).

27 To what extent are franchise agreements incorporating licences of intellectual property rights, relating to trademarks or signs and know-how for the use and distribution of products, assessed differently from 'simple' distribution agreements under antitrust law?

There are no special provisions for franchise agreements.

28 Explain how a supplier's warranting to the buyer that it will supply the contract products on the terms applied to the supplier's most favoured customer or warranting to the buyer that it will not supply the contract products on more favourable terms to other buyers is assessed under antitrust law.

There are neither special provisions nor precedents regarding the assessment of most-favoured-customer clauses under Swiss antitrust law. It is likely that the authorities will follow the assessment under European competition law.

29 Is there a formal procedure for notifying agreements containing vertical restraints to the agency? Is it necessary or advisable to notify it of any particular categories of agreement?

Agreements can be notified to the agency before the respective vertical restriction of competition takes effect (ACart, article 49a(3)). Such a notification seems advisable if the agreements in question entail a considerable investment, for example, the introduction of a new distribution system.

30 If there is a formal notification procedure, how does it work? What type of ruling (if any) does the agency deliver at the end of the procedure? And how long does this take? Is a reasoned decision published at the end of the procedure?

By notification of vertical restrictions of competition prior to their taking effect, the notifying company does not run the risk of getting fined (see ACart, article 49a(3)(a)). If the agency does not respond within five months of the notification, the notified restrictions of competition are deemed to be lawful. In return, if the company is informed by the agency of the opening of a procedure under ACart, articles 26 to 30 within those five months, and if it then continues the restriction of competition, a possible fine is not waived any longer. No reasoned decision will be published at the end of the formal notification procedure. However, there might be a press release of the competition authorities.

31 If there is no formal procedure for notification, is it possible to obtain guidance from the agency as to the antitrust assessment of a particular agreement in certain circumstances?

Besides the notification possibility and the ensuing opposition proceedings (see questions 29 and 30), companies may seek guidance from the Secretariat. According to ACart, article 23(2) , the duties of the Secretariat include advising companies on matters relating to the application of the law. However, officials of the Secretariat have recently indicated in public speeches that the Secretariat is reluctant to further provide guidance, allegedly due to shortage of staff.

32 Is there a procedure whereby private parties can complain to the agency about alleged vertical restraints?

Private parties can explicitly complain to the agency. According to ACart, article 26(1), the Secretariat may conduct preliminary investigations at the request of enterprises concerned. If there are signs of an unlawful restraint of competition, the Secretariat will open an investigation with the consent of a member of the ComCo's presiding body (ACart, article 27(1)). In return, if there are no such signs, the Secretariat will close the preliminary investigation without any further consequence. The approximate time period for such a preliminary investigation may be considerable and extend over a couple of years.

33 How frequently is antitrust law applied to vertical restraints by the agency?

Swiss antitrust law is often applied to vertical restraints, as Swiss authorities are particularly concerned about the allegedly higher prices in Switzerland compared to neighbouring countries. However, the number of decisions does not match the number of (preliminary) investigations the Secretariat conducts. In 2002, the Swiss authorities reported some 120 cases regarding vertical agreements. Based on 76 cases that had been closed by the time the annual report for 2003 was published, not one unlawful vertical agreement had been found. Either the ACart was not applicable, or there were no competition problems, or, in some cases, there was an amicable settlement. In 2004, 2005, 2006 and 2007, the Swiss authorities conducted about 70, 90, 80 and 46 (preliminary) investigations respectively. Based on the published statistics, one cannot allocate these cases to specific types of restraints, but a considerable share have concerned vertical restraints.

34 May the agency impose penalties or must it petition the courts or another administrative or government agency? What sanctions and remedies can the agency or the courts impose when enforcing the prohibition of vertical restraints?

The ComCo is empowered to impose penalties itself (ACart, articles 18(3), 53). The Secretariat, in return, conducts the investigations and makes proposals to the ComCo (ACart, article 23(1)). The ComCo may impose a fine of up to 10 per cent of the respective companies' turnover in Switzerland in the previous three business years. The amount of the sanction is dependent on the duration and severity of the unlawful behaviour. A remedy may consist in reaching an amicable settlement, which will be decided by the ComCo on a proposal from the Secretariat (ACart, article 30(1)).

Update and trends

After the coming into force of the amended Verticals Notice on 1 January 2008, no changes to the legislation are expected in the near future.

35 What investigative powers does the agency have when enforcing the prohibition of vertical restraints?

Parties to vertical agreements are required to provide the competition authorities with all relevant information and to produce all necessary documents (ACart, article 40). The competition authorities also may hear third parties as witnesses and require the parties to the investigation to make statements (ACart, article 42(1)). The competition authorities may even order searches and seize exhibits (ACart, article 42(2)).

36 What notable sanctions or remedies have been imposed? Can any trends be identified in this regard?

Up to now, there have not been any sanctions for vertical restraints in Switzerland. As far as remedies are concerned, the authorities are particularly interested in removing any obstacles to parallel imports and in scrutinising price recommendations having – allegedly – the effect of fixed prices. The new Verticals Notice now explicitly treats price recommendations with suspicion from the outset. It remains to be seen whether ongoing investigations regarding price recommendations will lead to a first-ever sanction for vertical restraints in Switzerland.

37 Can sanctions or remedies be imposed on companies having no branch or office in your jurisdiction?

The ACart applies to restrictive practices whose effects are felt in Switzerland, even if they originate in another country (ACart, article 2(2)). Consequently, sanctions or remedies may be imposed on foreign companies. If these foreign companies have no branch or office in Switzerland, an enforcement possibility may be the attachment of claims the foreign companies may have against Swiss or Swiss-based companies.

38 To what extent is private enforcement possible? Can non-parties to agreements containing vertical restraints bring damages claims? Can the parties to agreements themselves bring damages claims? What remedies are available? How long should a company expect a private enforcement action to take? Can the successful party recover its legal costs?

Private enforcement is possible under Swiss antitrust law. The right to sue, however, is limited to a person impeded by an unlawful restraint of competition from entering or competing in a market. Such a person may request removal or cessation of the obstacle (eg, conclusion of contracts at market terms), damages and reparations, and the remittance of illicitly earned profits (ACart, articles 12(1), 13). Up to now, the instrument of private enforcement has not been used very frequently. This is mainly due to the high burden of proof and the substantial cost risk.

39 Is there any unique point relating to the assessment of vertical restraints in your jurisdiction that is not covered above?

It seems to be quite remarkable that the stated aim of the ComCo, namely to use the VN to bring the Swiss provisions on competition law in line with the European competition provisions, has not been reached. Besides its more rigorous treatment of price recommendations, the VN states (in section 10(2)) that proof of continued inter-brand competition is not sufficient in itself to rebut the presumption that competition has been eliminated. If taken literally, this could be out of sync with European doctrine. According to the European Commission most vertical agreements do only raise anti-competitive concerns in cases of insufficient inter-brand competition (cf No. 6 of the Guidelines on Vertical Restraints). However, in a recent press release together with the coming into force of the VN on 1 January 2008, the ComCo stated more precisely that inter-brand competition is regarded as an important element in the assessment of restrictions, but that efficiencies are needed for a justification as well.

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