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Digest

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The Federal Antimonopoly Service

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IMPORTANT ISSUES OF ENFORCING THE ANTIMONOPOLY LAW AND THE LAW ON PROCUREMENT AT COURTS OF GENERAL JURISDICTION

A CASE EXAMINED BY ARKHANGELSK REGIONAL COURT

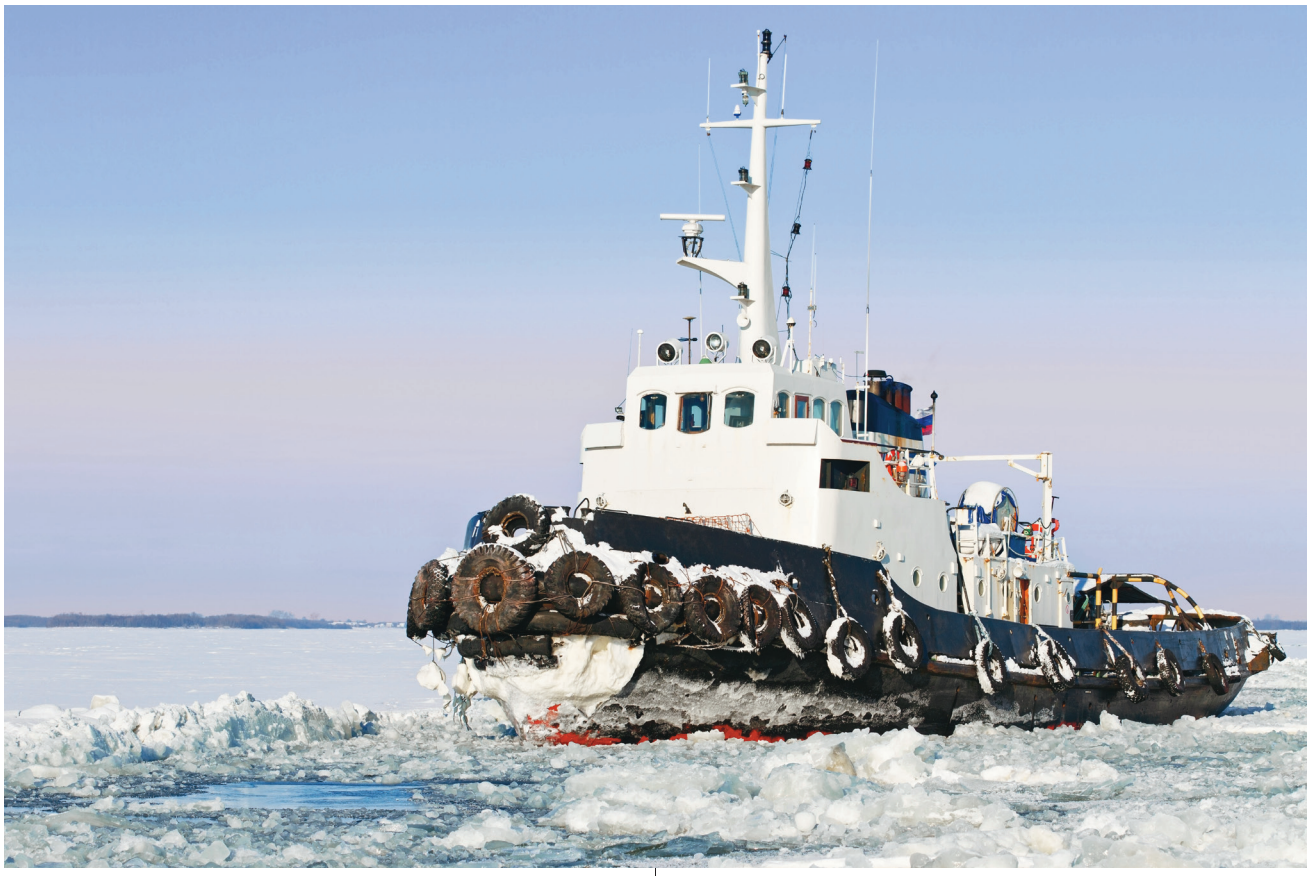
The analyzed civil-law case presents interesting empirical material for both courts of general jurisdictions and antimonopoly bodies, sine the latter are authorized to take part in court hearing of the cases associated with applying or violating the antimonopoly law.

CASE SUMMARY

Deputy Prosecutor of the Arkhangelsk Region lodged a lawsuit to Arkhangelsk District Court against a former Director of Arkhangelsk Regional Health Care Department seeking to protect the rights and legitimate interests of the Russian Federation in the person of the Ministry of Finances of Russian Federation and to recover damages (34,400,000 Rubles) caused by a crime under Part 1 Article 293 (neglect of duty) of the Criminal Code of the Russian Federation.

To justify the claim, Deputy Prosecutor indicated that the respondent organized auctions for concluding government contracts acting in his capacity as the Director of Arkhangelsk Regional Health Care Department authorized to purchase expensive medical equipment under agreements between Archangelsk Regional Authority and the Ministry of the Russian Federation for Health Care and Social Development to implement long-term specialized regional medical programmes ("Improving medical care for patients with cardiovascular diseases 2009-2011" and "Improving medical care associated with car accidents 2009-2010").

Medical equipment is included in the Government-approved List of goods (works, services) that must be procured through auctions. Arkhangelsk Regional Health Care Department formed a working group that in July 2009 drafted documentation for two auctions under each of the agreements for purchasing high-technology medical equipment.



The initial (maximum) price of the government contracts was based on the regional funds and subsidies from the federal budget as specified in the agreements.

The Regional Health Care Department applied to Arkhangelsk Regional Department on Competition Policy for approving the auction documentation and publishing auction notices. The documentation was approved on 27th July and on 28th July the information about the open auctions was published in the official print media and at the official web-site of the Arkhangelsk region.

On 14th August the ordering party informed the authorized body about introducing changes to the open auction documentation: combining all medical equipment in a single lot for each auctions and changing the technical parameters of the medical equipment (reducing the warranty period forom two to one year). The quantity and the original price remained unchanged. The changes were approved by the authorized body that published them in the official print media and at the official web-site on 20th August 2009. Four applications for taking part in the auctions were filed. No one challenged the auction documentation. On 15th September 2009 the Public Procurement Commission at Arkhangelsk Regional Department on Competition Policy declared the auctions void on the grounds that all bidders had not been allowed to take part in the auctions due to absence of licenses for assembling and commissioning ionizing radiation sources. Also the goods offered by two out of four bidders did not meet the requirements specified in the auction documentation to the functionalities and the quality of the goods.

On 24th September "Russian Medical Corporation" Ltd. informed Arkhangelsk Regional Health Care Department that due to obtaining the necessary license the company was prepared to enter into the governmental contracts for supplying high-technology medical equipment. Upon consent by the authorized body, the ordering party concluded the government contracts with the only supplier - "Russian Medical Corporation" Ltd. on 13th October 2009. Supplies were paid in full in December 2009.

The Prosecutor considered that the respondent decided to change the auction documentation – combine technologically and functionally not connected X-ray and ultrasound equipment in the same lot without analyzing the market value and specify particular models and detailed parameters of the medical equipment. Such changes of the technical assignment were based on technical characteristics of the medical equipment proposed by the Director of "Russian Medical Corporation" Ltd. who was known to the respondent. The claimant believed that making the decision the respondent could and must have foreseen that the changes could restrict the number of

bidders at the open auctions and lead to procuring the equipment at unreasonably high prices. Thus, actions of the Director restricted competition between entities operating on the markets of manufacturing and sale of X-ray and ultrasound equipment.

According to the Prosecutor, the respondent breached Part 3 Article 17 of the Federal Law "On Protection of Competition" which prohibits restricting competition between bidders by including products not connected technologically and functionally in the same lots. The respondent also violated Part 3.1 Article 34 of the Law on Procurement which prohibits specifying particular details of the goods in auction documentation (like patents, prototypes, place of origin, etc., if such specification can restrict the number of bidders).

Criminal proceedings against the respondent were terminated due to expiry of the period of limitation.

The claimant asked to recover damages inflicted upon the Russian Federation as the difference between the price for the equipment under the government contracts and the price for similar equipment sold to medical institutions in the Russian Federation.

A representative of the respondent disagreed with the claim and stated that the claim was made against an ineligible person; the size of the damages inflicted upon the Russian Federation was not confirmed and was based on assumptions; the evidence did not meet the requirements of relativity and validity. The representative asked to dismiss the claim referring to lack of proof for cause-and-effect relations between the actions of the respondent for changing the auction documentation and the consequences.

On 26th December 2011 the Court dismissed the claim. Cassation appeal was lodged on 30th December which was considered by the Judicial Division for Civil Cases of Arkhangelsk Regional Court governed by the cassation proceedings that were in effect prior to 1st January 2012 when procedural changes came into force.

The cassation appeal was dismissed and the judgment of the Court of First Instance upheld.

The case was not reopened in exercise of supervisory powers.

LEGAL ISSUES ON THE CASE THAT REQUIRE CLARIFICATION

1. Is the official the eligible respondent on the civil case in the relations regulated by the law on procurement and the antimonopoly law

The Prosecutor believed that the respondent to the case is directly responsible for the damages to the budget of the Russian Federation and is the eligible respondent because his actions were not instructed or directly supervised by his employer and related solely to the criminal intentions of the Director.

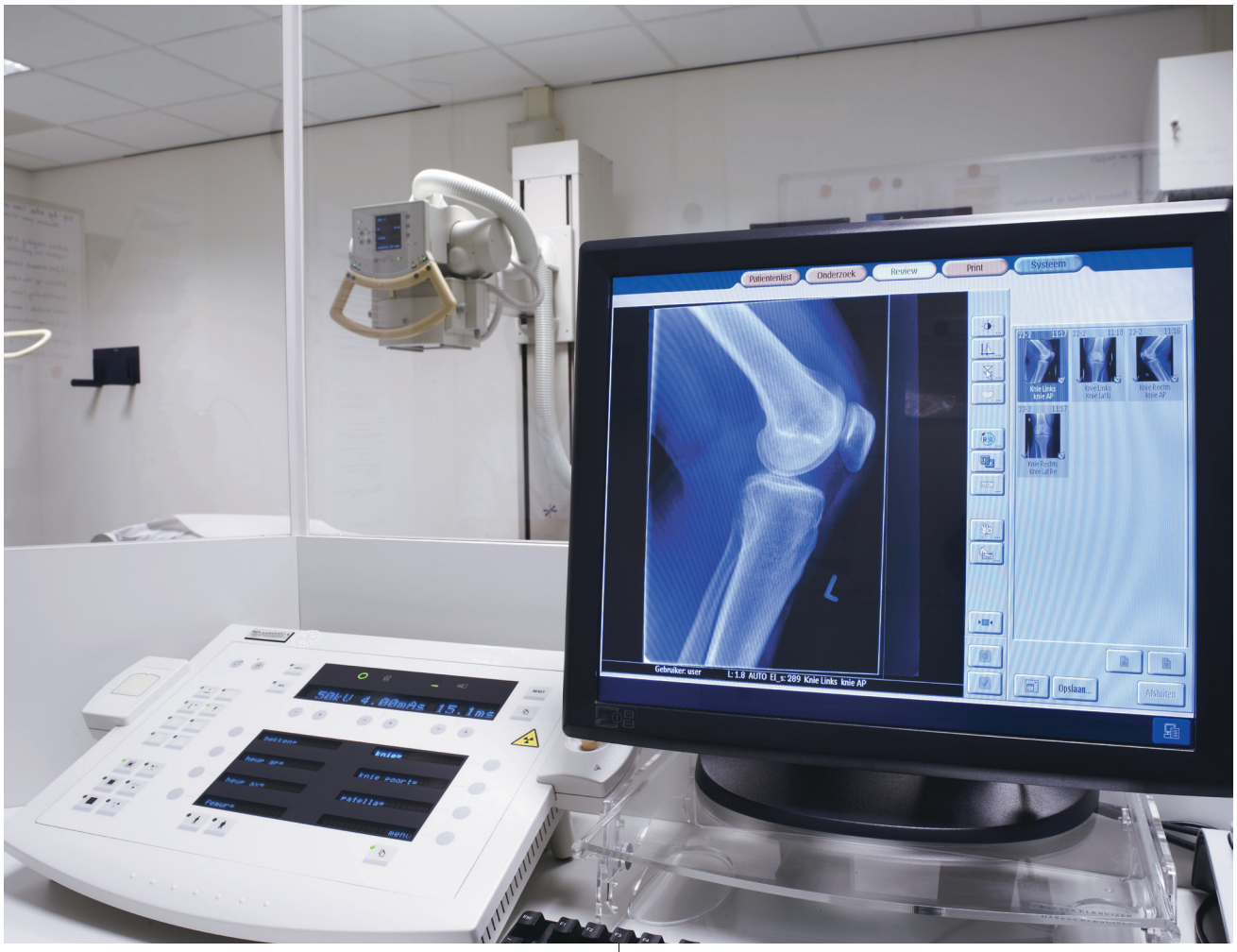
The Court of First Instance took the position that the illegible respondent must be the executive body of the Arkhangelsk region - the Ministry of Health Care and Social Development of the Arkhangelsk Region (the legal successor of the Arkhangelsk Regional Health Care Department) since the respondent to the case acted within the scope of his authority and on behalf of the Department he was responsible for. Damages must be compensated by the executive body while under the Labour Code an employee can be held responsible for compensating losses inflicted by actions of the respondent upon third parties.

Dismissing the claim, the Court stated that disagreement of the claimant with replacing the respondent to the case constitutes separate grounds for dismissing the claim against an ineligible respondent. At the same time, the Court did not rule on the merits of the case regarding the claim legitimacy.

The position described in the judgment issued by the Court seems to be very controversial.

The Cassation Court reasonably arrived to the following conclusions:

The Court of First Instance correctly stated that the Director of the Department was not the eligible respondent to the case. At the same time, the conclusion made by the Court of First Instance that the



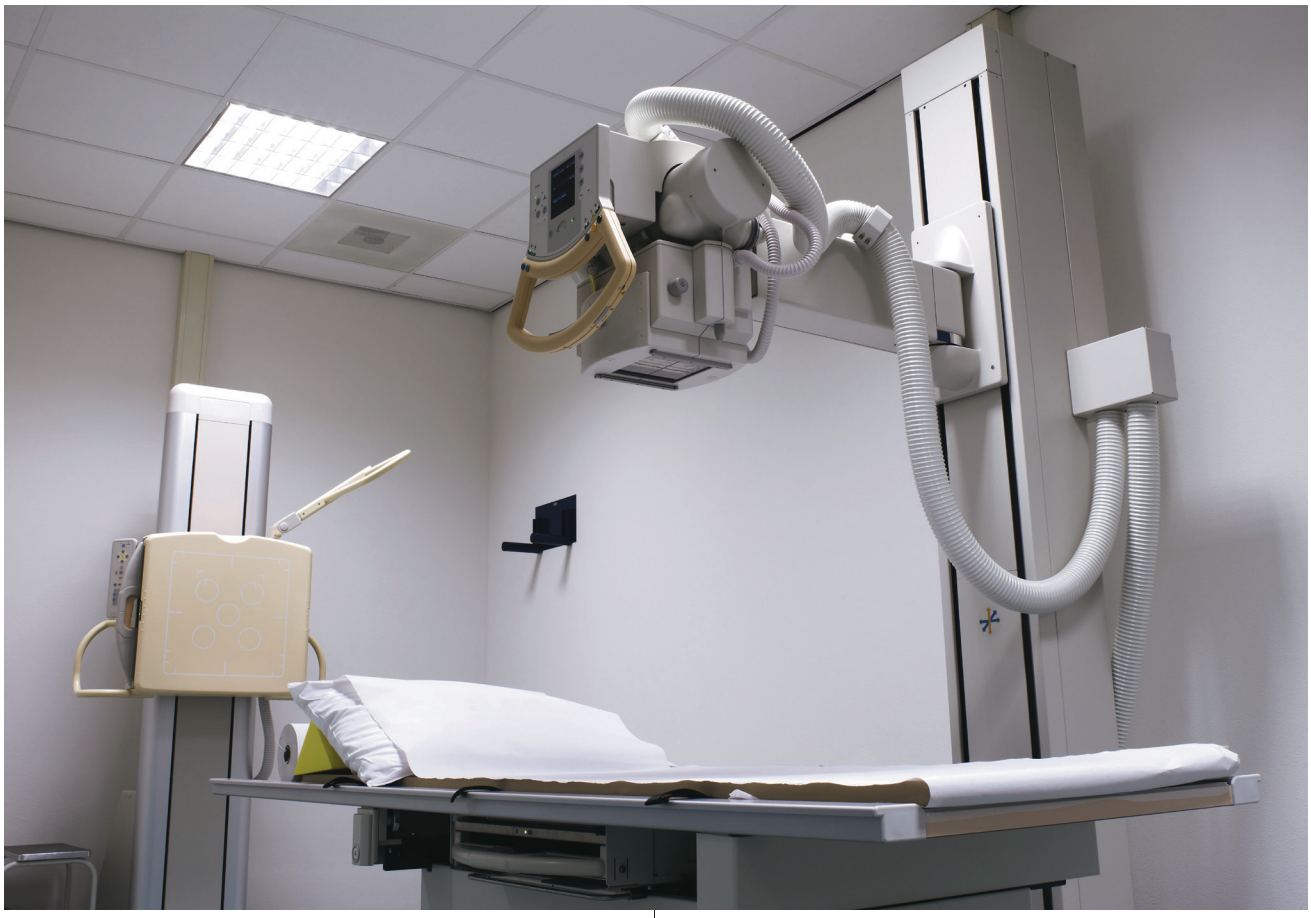
eligible respondent should be the Ministry of Health Care and Social Development of the Arkhangelsk Region as the legal successor of Arkhangelsk Regional Health Care Department was wrong. The Court also had no right to make a statement that the person was the eligible respondent because the Ministry was not brought into the case and was unable to express its attitude to the claim.

Based on the system-wide interpretation of the norms of law, to hold former Director of the Department financially liable the following conditions should be met: actions (omissions) by the Director should be unlawful; there should be a chain of causation between Director's behavior and the incurred losses; actions (omissions) by the Director must imply guilt. Also there should be an established legal acts of inflicting damages upon the legal entity. To hold a person acting on behalf of a legal entity financially liable due to his professional activity there should be a claim by the legal entity or a person authorized by the legal entity to compensate damage.

The government contracts for supplying medical equipment for the needs of medical institutions in the Arkhangelsk region were concluded by the respondent on behalf of Arkhangelsk Regional Health Care Department. The contracts do not include conditions that he acted to his benefit or on his own behalf (was a buyer or seller of the equipment). The government contracts were concluded upon consent by the authorized body with the single supplier because the open auctions were pronounced void. No claim was made by the Ministry (former Department) of Health Care of the Arkhangelsk region to the Director to compensate damage. There is no evidence that the health care executive body of the Arkhangelsk region incurred damage (losses).

The respondent is not sentenced under criminal proceedings and his actions did not have the nature of intentionally inflicting damages. Under such circumstances the respondent cannot be held fully financially responsible in accord with the current law.

Also, government bodies can act on behalf of the Russian Federation and the constituent territories of the Russian Federation and acquire and exercise property and personal non-property rights within their scope of competence, established by the acts that determine the status of such bodies.



In the case in question the Department (the Ministry) of Health Care of the Arkhangelsk region is the authorized executive government body in the Arkhangelsk region in the field of health care, exercising, in particular, the function of procurement of medicines and medical products for the public needs in the Archangelsk region.

Since the government contracts are concluded on behalf of a public-law entity, liability of the public entity under the government contract, the ordering party for which is an executive body, is not of subsidiary nature. The public-law entity is the principal to the obligations associated with the government contract. Legal qualification of the liability of the public-law entity shall not change if the direct goal of the government contract is to satisfy the needs of the government customer (ordering party) in particular goods.

2. Does combining medical equipment in the same lot and approving new parameters in the technical documentation for procurement of medical equipment constitute a violation of the Law "On Protection of Competition" and the Law "On Procurement…"?

Justifying the claim to compensate damage, the Prosecutor submitted as evidence an act drawn by Arkhangelsk OFAS Russia upon the findings of an unscheduled inspection of 19th March 2010.

The Head of the antimonopoly body issued an order to an inspection panel which inspected actions of the ordering party (the Department of Health Care of the Arkhangelsk region) and the authorized body (the Departments for Public Procurement and Competition Policy of the Arkhangelsk region) related to public procurement of the medical equipment. The inspection panel concluded that the ordering party violated Part 3 Article 17 of the Law "On Protection of Competition" (changing auction documentation to combine three lots into one), Part 5 Article 9 (changing the conditions of the government contract after it was concluded) and Part 3.1 Article 43 (changing technical parameters of the medical equipment) of the Law "On Procurement...". The inspection panel recommended forwarding the materials to an officer of the antimonopoly body to investigate an issue of holding the Director of the Department of Health Care of the Arkhangelsk region administratively liable. OFAS issued a determination that the Director committed an administrative violation under Part 4 Article 7.30 of the Code of the Russian Federation on Administrative Violations and should pay an administrative fine – 30,000 Rubles.

District Court upheld OFAS decision and dismissed the claim; Arkhangelsk Regional Court also supported the judgment issued by the District Court and again dismissed the claim to reverse it.

However, it seems that the position of the inspectorate panel was controversial with regard to establishing the facts of violating the antimonopoly law and the law on procurement, which formed the basis for criminal prosecution of the Director, finding him administratively liable and justifying civil law sanctions. No.379 Regulations of the Federal Antimonopoly Service for considering complaints about actions (omissions) of the ordering party, the authorized body, specialized organization, auction, tender or quotation in the course of procurement of goods, works, services for state and municipal needs commission establish the procedures for executing the state function and the procedures for informing about executing the state function.

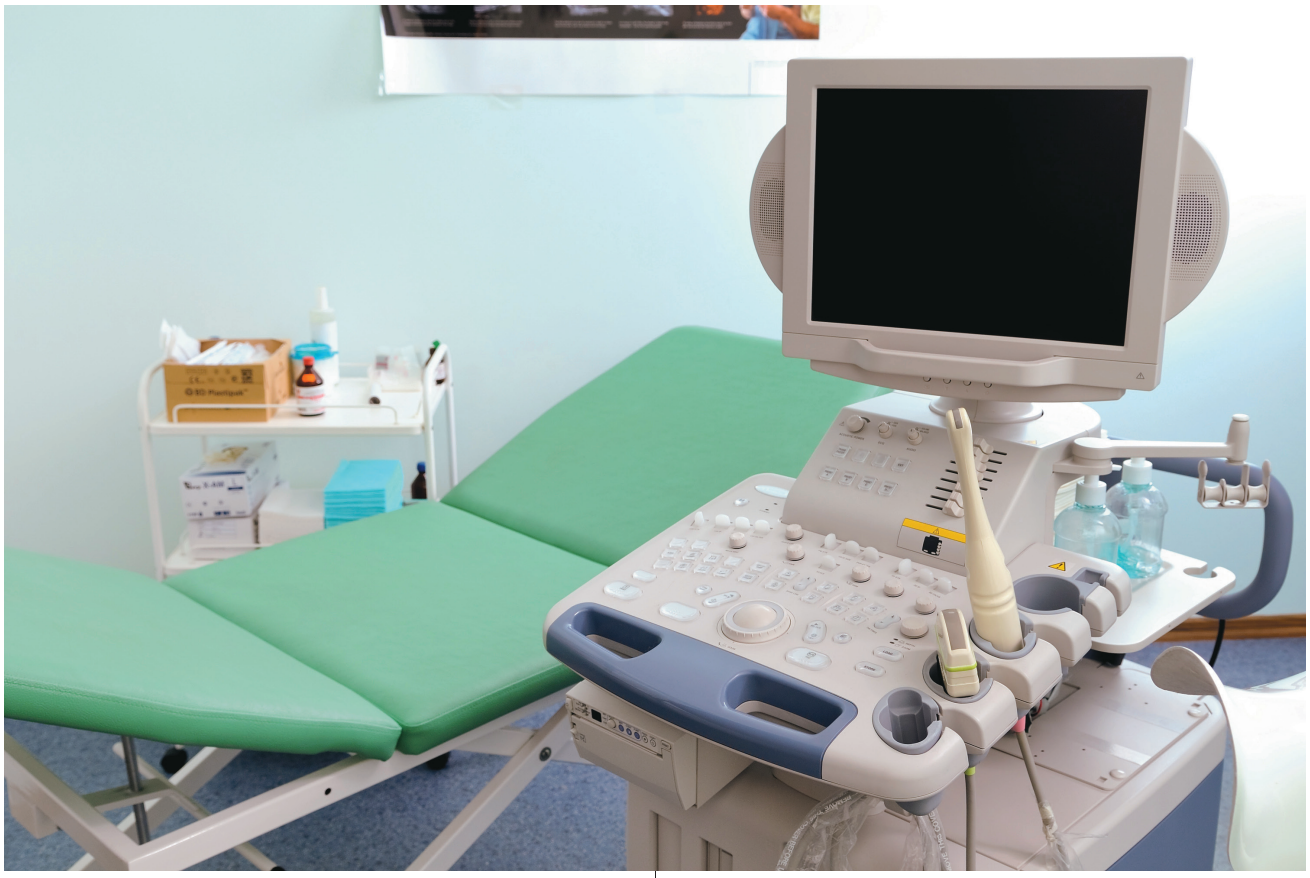
In the case in question, the antimonopoly body failed to observe the requirements for executing the government function for complaint consideration, which include such administrative procedures as notifying about the content of complaints, notifying the interested persons about the place and time of complaint consideration, forwarding complaint to the Commission for substantive consideration and drawing up a decision.

Also inspection panels of antimonopoly body do not have the authority to establish the facts of violating the law. Control over compliance with the law is exercised by the antimonopoly bodies. Such authority is granted to collegiate bodies – Commissions of an antimonopoly body. The materials of the case in question do not contain the relevant decisions of the antimonopoly body on establishing the facts of violating the antimonopoly law and the law on procurement.

Is seems that carrying out the unscheduled inspection Arkhangelsk OFAS was guided by the Guidelines on scheduled and unscheduled inspections in procurement of goods, works and services for state and municipal needs formulated in a FAS letter. However, the letter does not meet the requirements to normative acts, thus OFAS should have followed No.379 Regulations.

Therefore, the point of view described in the Court ruling on the criminal case and the judgment on administrative violation based on establishing by Arkhangelsk OFAS the fact of violating the law on procurement and the fact of violating the antimonopoly law is questionable because the act of unscheduled inspection cannot be recognized as acceptable evidence of violating the laws by the Director.

Overall, Arbitration Courts take a similar legal position on a number of cases, verifying the authority of antimonopoly bodies. The established legal mechanism of exercising powers of antimonopoly body in this aspect is based on No.379 Regulations and the rules given in the Law on procurement (Chapter 8).



The government control is exercised to restore public order and infringed civil rights, At the same time, unlimited control can prevent public relations protected by law. Therefore, possibilities of challenging actions of the persons specified in the Law on procurement by approaching the antimonopoly bodies are limited. After the contract is concluded, actions of such persons can be challenged only through judicial procedures and only Courts of Law are competent to evaluate all circumstances of procurement.

In the analyzed case, the Cassation Court effectively casted away the statement made by the inspection panel of the antimonopoly body made in the unscheduled inspection act of 19th March 2010 and emphasized reasonableness of the counterarguments put forward by the representative of the respondent that there is no evidence of inflicting actual direct damages by the respondent upon his employer caused by limited competition in procurement of medical equipment.

STANDPOINT OF THE COURT – SUBSTANTIATION

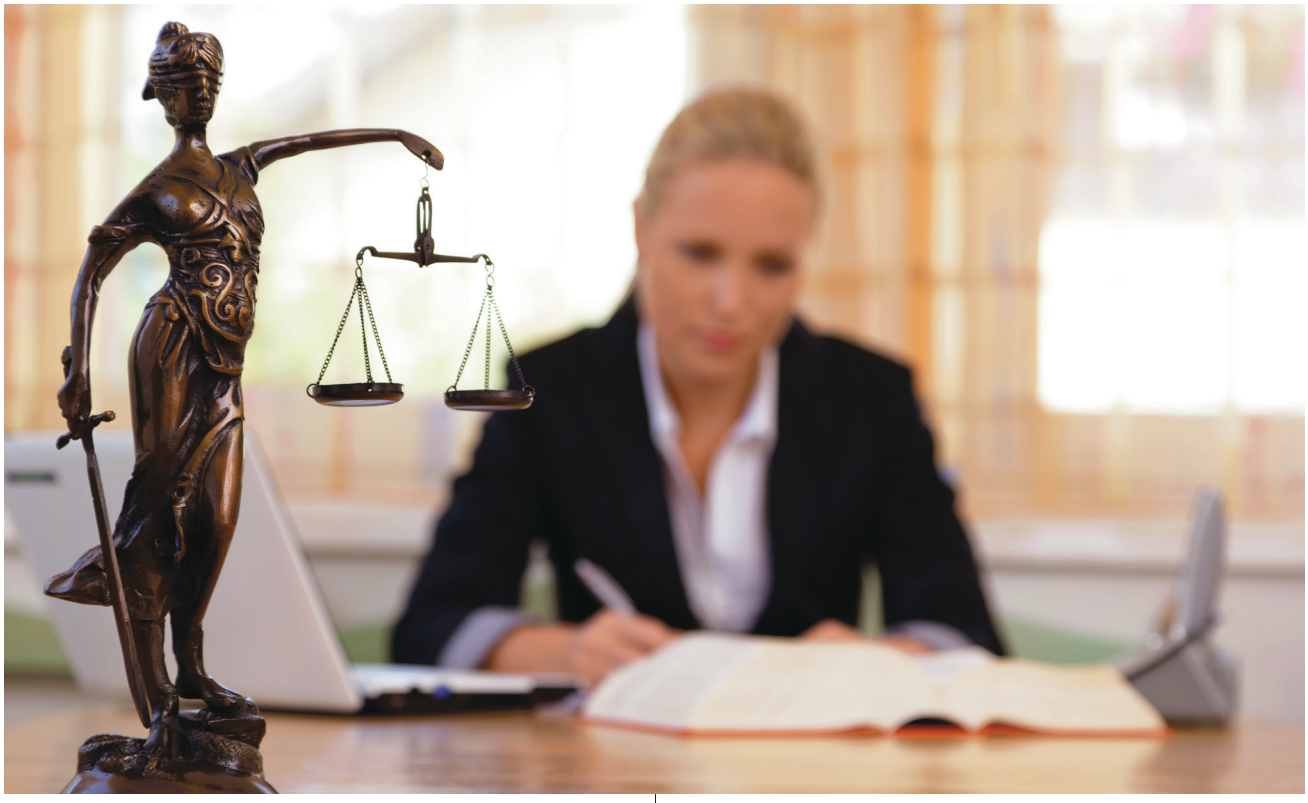
The Court position is as follows:

The Prosecutor did not present evidence confirming that actions of the respondents inflicted damages upon the employer as well as evidence of the size of damages. The case materials contain no indication that the employer of the respondent to the case incurred losses through actions of the respondent in his capacity as the Director in the form of payments to third persons or as decreased property.

At the same time Part 3 Article 17 of the Law "On Protection of Competition" prohibits restricting competition between auction bidders in public procurement by including products (goods, works, services) in lots that are not technologically or functionally linked to the goods, works, services that are the subject matter of the auction. Part 2 Article 1 of the Law formulated its goal as ensuring unity of economic space, free movement of goods, freedom of economic activity in the Russian Federation, protecting competition and creating conditions for effective market performance.

The Law on procurement established unified public procurement procedures. At the same time it sets no requirements to the procedures of compiling lots. The decision on the method of placing an order shall be made by the ordering party and the authorized body under Parts 2.1 and 3 Article 10 of the Law on procurement.

Certainly the ordering party must not ignore the goals of procurement regulation aimed at efficient use of budgetary funds and development of bona fide competition and must comply with Article 17 of the Law "On Protection of Competition" which prohibits any actions that lead or may lead to preventing, restricting, eliminating competition at auctions.



The Prosecutor simply failed to present to the Court uncontestable and acceptable evidence that the way the Department had compiled the lot prevented achieving the goals of rational and economically viable spending of budgetary funds. The case materials do not contain analysis of the state of competition on the market carried out in accordance with the established procedures and under No.108 FAS Order "On Approving the Procedures for Analyzing and Evaluating the State of Competition on the Market", which was valid at that period. Without such analysis it is impossible to determine the state of competition on the market of medical equipment or establish whether the initial (maximum) contract price was justified.

When the Director of the Department of Health Care of the Arkhangelsk region was making a decision to procure the equipment, Article 19.1 of the Law on procurement that obligates ordering parties to justify the initial (maximum) contract price (lot price) was not in effect. The rules for setting initial contact prices for certain types of medical equipment were adopted only in 2011.

There is no acceptable evidence confirming indisputably rather than on the basis of probability that a particular pattern of lots for medical equipment would save budgetary funds and enable acquiring the equipment at a better price. There is no evidence in the case that the changes to the technical assignment adversely affected a particular market. The criminal case also does not specify potential or actual bidders, their intentions due to the prospects of taking part (refusing to take part) in the auctions due to a particular initial and possible further configuration of the lot, specifics of activities of the economic entities interested in procurement, observing or infringing their rights (in view of revealing significant evidence under Clause 17 Article 4 and Part 3 Article 4 of the Law "On Protection of Competition" rather than abstract perception. Under such circumstances, the sum specified in the claim is assumed. On the basis of the information presented by the claimant it is impossible to calculate even assumed damage.

The case materials also do not contain evidence of inflicting harm exclusively upon the Russian Federation since Arkhangelsk Regional Authority and the Ministry of Health Care and Social Development of the Russian Federation together undertook obligations to finance the medical programmes. In particular, the Ministry granted subsidies to Arkhangelsk region for co-financing procurement of the equipment. The Prosecutor did not explain why the harm was inflicted specifically to the Russian Federation. Therefore, the circumstances, to which the Prosecutor refers in the Cassation appeal, cannot constitute the grounds for reversing the judgment of the Court of First Instance.

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ESTABLISHING THE INSTITUTION OF WARNINGS TO STOP ACTIONS (OMISSIONS) THAT HAVE SIGNS OF VIOLATING THE ANTIMONOPOLY LAW

THE CASE OF MOSCOW REGIONAL OFFICE OF FAS RUSSIA

In 2012 Moscow Regional OFAS exposed 49 facts of violating Article 10 of the Federal Law "On Protection of Competition" - abusing market dominance by economic entities. Most violations of Part 1 Article 10 took place in electric and heating power industries (73%, or 36 incidents); and housing & utilities sector (9%, or 4 incidents). Majority of violations in electric power industry related to failures of network companies to exercise technological connection of customers' receiving devices to electric power networks within the statutory period.

PREVENTIVE MEASURES

After the amendments to the Federal Law "On Protection of Competition" came into effect, the number of cases initiated upon signs of violating the antimonopoly law in the electric power industry has reduced considerably. In 2011 OFAS opened 78 antimonopoly proceedings, while in 2012 – only 48. The 40% reduction is a consequence of introducing Article 39 (1) in the Law on issuing warnings to stop actions (omissions) that have signs of violating the antimonopoly law (further on referred to as warnings).

Warnings can be issued under Clauses 3 and 5 Part 1 Article 10 of the Federal Law "On Protection of Competition". Clause 3 prohibits imposing disadvantageous contract conditions upon a counteragents or conditions irrelevant to the contract subject (economically or technologically unjustified and (or) not directly provided for directly by the federal laws, normative legal acts of the President of the Russian Federation, normative legal acts of the Government of the Russian Federation, normative legal acts of the authorized federal executive bodies or judicial acts, requirements for transferring financial assets, other property, including property rights, as well as consent to conclude a contract on conditions of including in it provisions, concerning the goods in which the counteragent is not interested and other requirements). Clause 5 prohibits economically or technologically unjustified refusals to conclude contracts or avoiding contracts with particular buyers (customers) when there are possibilities for production or supply goods as well as if such a refusal or avoidance are not directly provided for by the federal laws, normative legal acts of the President of the Russian Federation, the Government of the Russian Federation, authorized federal executive authorities or judicial acts.

The institution of warning is a measure preventing violations of the antimonopoly law. According to experts, preventive effect of warnings is that FAS cannot initiate a case without issuing a warning and before the deadline for its execution. The Head of FAS Legal Department Sergey Puzyrevsky points out that warnings form a new instrument of the antimonopoly enforcement aimed at eliminating the consequences of violations and the violation-enabling causes and conditions without opening antimonopoly proceedings. ***The positive simulative factor is that if a warning is executed the violator shall be relieved from administrative liability*** and shall not pay a fine. This approach, in particular, facilitates prompt restoration of the rights and interests of

the affected persons. Eliminating signs of violations following a warning constitutes separate grounds for the antimonopoly bodies to refuse initiating a case (Clause 7 Part 9 Article 44 of the Federal Law "On Protection of Competition").

To stop actions (omissions) that lead or can lead to preventing, restricting, eliminating competition and to enforce Article 39 (1) of the Law "On Protection of Competition", in 2012 Moscow Regional OFAS issued 93 warnings to economic entities whose actions (omissions) have signs of violating Part 1 Article 10 of the Law: Clause 3 – 46%, Clause 5 – 54%. In 2012 OFAS also issued warnings investigating cases opened under Article 10 in 2011, before the institutions of warnings was introduced. 25 warnings (27% of the total number of warnings) were issued in the course of investigating cases on violating Clause 3 (15 warnings, 16%) and Clause 5 (10 warnings, 11%).

Practice showed that warnings as the instrument of antimonopoly regulation prove to be efficient, encouraging market participants to eliminate violations before cases are opened (95% of the warnings issued by Moscow OFAS in 2012 were executed within the designated period or are being executed).

LEGAL VIEWS TAKEN BY COURTS

Prompt reaction of dominant market players to the issued warnings reduced the periods for restoring the rights of the persons whose interests were infringed and reduced the costs (timing, resources, financial) of the antimonopoly bodies.

Nevertheless, about 5% of warnings are appealed at Courts. Judicial practice in this field is only establishing and sometimes is controversial. So far the Supreme Arbitration Court has not formulated its position on possibility of appealing warnings.

In 2012, the 4th Arbitration Appeal Court ruled that a warning cannot be subject to separate claim and such proceedings must be terminated because warnings issued by antimonopoly bodies do not constitute non-regulatory instruments and cannot be considered as infringing the rights and legitimate interests of the claimant because the consequences of a failure to execute a warning is issuing a procedural act, which is not a subject-matter of a separate appeal. Warnings do not establish a fact of violating the antimonopoly law and do not determine sanctions. Failure to execute warnings does not incur any adverse consequences for a person to whom it was issued since it only constitutes the grounds for opening an antimonopoly case, which in its turn does not incur any adverse consequences and cannot be appealed.

However, in January 2013 the Federal Arbitration Court of the Provolzhie District ruled that a warning violates the rights and legitimate interests of a market participants and failure to execute it incurs adverse consequences for an economic entity while executing a warning means recognizing the fact of violating the antimonopoly law. The Court concluded that warnings are non-regulatory acts and, therefore, can be appealed.

OBJECTIVES AND RATIONALE

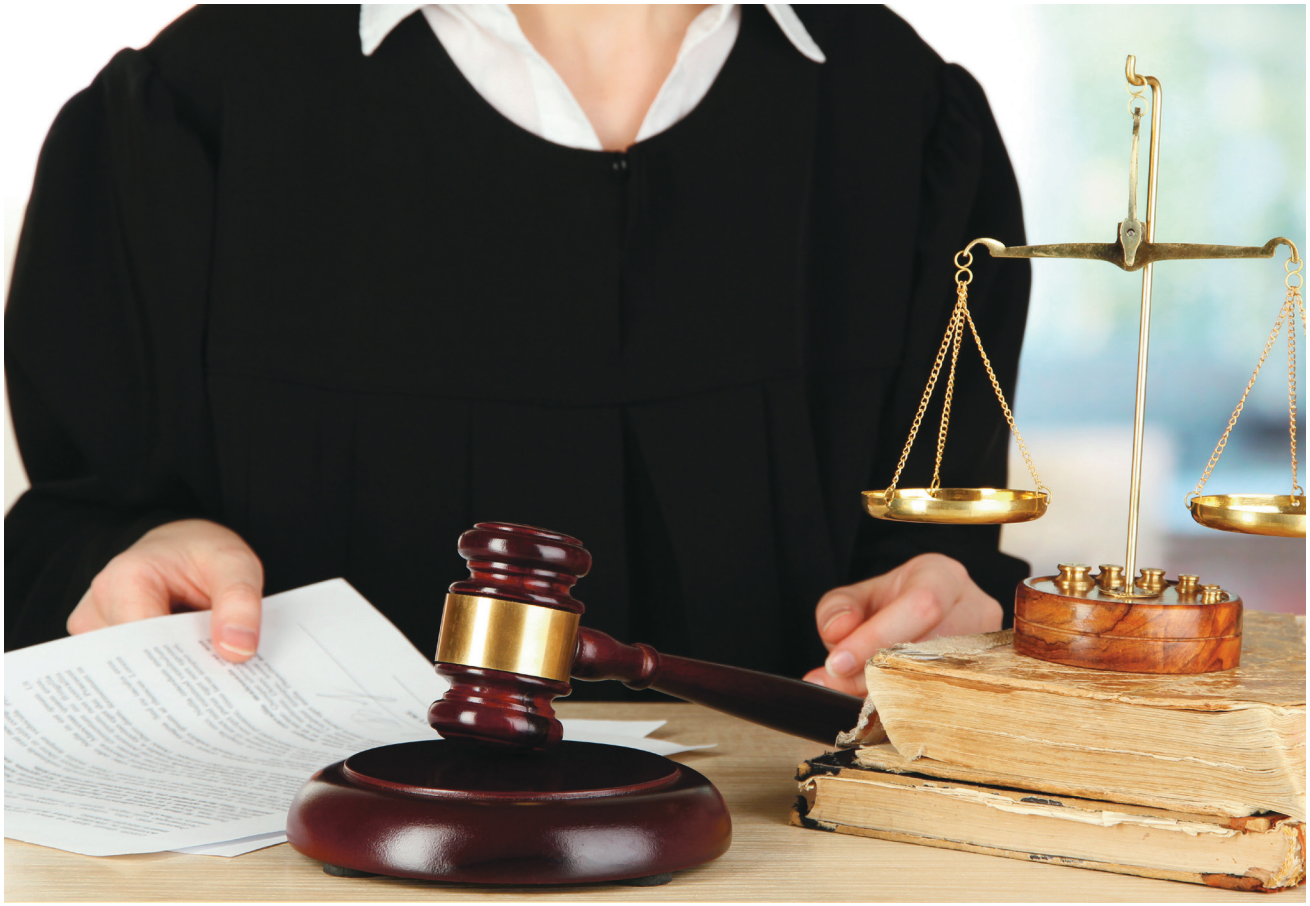
The issue with appealing warnings is incorrect interpretation ofrqualification of the institute of warnings by economic entities and Courts of Law.

The institution of warnings was introduced to encourage a positive behaviour pattern of economic entities that voluntary eliminated violations of the antimonopoly law in response to complaints by the interested persons and a reaction of the antimonopoly authority. However such positive pattern did not meet a reciprocal move by the regulator since the antimonopoly bodies did not have a possibility to relieve fines. Such a situation did not stimulate desirable behavour of bona fide market participants to voluntary eliminate antimonopoly violations and restore the rights and legitimate interests of the affected persons and, on the contrary, encouraged lawsuits to defend their standpoints at courts.

Thus, introduction of the institution of warnings seems to be quite promising: it establishes a model of interaction between the antimonopoly authority and market participants when the latter can be relieved from administrative liability if agree with the position of the antimonopoly body on signs of violating the antimonopoly law and a threat to the interests of other persons, and exercise actions towards eliminating the violations and their consequences. If a market participant disagreed with the position of the antimonopoly body and / or refuses to execute the warning, the procedure moves to a traditional stage of investigating an antimonopoly case. Refusals to execute warnings can be public (openly expressing disagreement including filing a lawsuit) or latent (omissions). In any case an antimonopoly investigation shall be initiated.

Based on a system-wide interpretation of Articles 39.1 and 44 of the Law "On Protection of Competition", the warning-issuing procedure is an additional procedure of offering a market participant to voluntary eliminate a violation, signs of which are exposed by the antimonopoly body, with a possibility to be relieved from administrative sanctions. If violations are not eliminated voluntarily the antimonopoly body continues the procedure of opening an antimonopoly case under Article 44.

Adverse consequences for market participants are caused by violating the antimonopoly law, which constitutes the grounds for issuing a warning or opening a case when warnings are not provided for, rather than by failure to execute a warning. Issuing a warning simply gives a market participant an option – to eliminate the signs of a violation or to move to the standard procedure of investigating an antimonopoly



case if the participant does not agree with the position taken by the antimonopoly authority.

Issuing warnings is not an administrative jurisdictional procedure, traditionally understood as efforts of executive bodies to resolve disputes between different entities and to exercise administrative enforcement in the form of administrative procedures. Thus, warnings do not infringe the rights of economic entities and can not be appealed.

There is no sense in judicial proceedings also because the issues of presence or absence of signs of violating the antimonopoly law cannot be the subject matter of appeals as violations of the antimonopoly law are to be recognized by the antimonopoly authority in the form of decisions made under Article 49 of the Law "On Protection of Competition".

Statistical data of Moscow OFAS give the following breakdown of cases investigated in 2012 under Part 1 Article 10 of the Law "On Protection of Competition":

- Fixing and maintaining monopolistically high prices (Clause 1) – 8% (4 incidents)
- Imposing disadvantageous contract conditions (Clause 3) – 2% (1 incident)
- Unreasonably reducing or terminating goods production (Clause 4) – 4% (2 incidents)
- Preventing market entry / exit (Clause 9) – 2% (1 incident)
- Violating pricing procedures (Clause 10) – 4% (8 incidents)
- Others – 76% (37 incidents).

It can be noticed that the institution of warnings is not applicable to quite a few elements of violations while they constitute the grounds for a considerable number of antimonopoly cases. Perhaps, extending the elements of violation to which warnings can be applicable would reduce the burden on bona fide business and accelerate restoration of the right and interests infringed by violating the antimonopoly law.

It also seems logical to extend a preventative institution of warnings to antimonopoly violations committed by the authorities. Such violations account for over half of the total number of violations of the antimonopoly law; therefore, warnings would certainly contribute to more efficient and prompt elimination of violations and restoration of the infringed rights.

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SUPPRESSING MONOPOLISTIC ACTIVITIES IN RAILWAY TRANSPORTATION

Violators of antimonopoly law can be service providers in both public and non-public railway systems

Violations in the **public** railway system are mostly related to the railways that are branches of "Russian Railways" OJSC, whose market power is determined on the one hand by its status of a holder of natural monopoly in use of the infrastructure (railway tracks), and on the other – the company's dominant position as a carrier.

Contractual regulation of transportation

Under Part 1 Article 4 of the Federal Law "On Natural Monopolies", railway transportation is included in the list of natural monopolies. "Russian Railways" OJSC is a holder of natural monopoly included in the Register of the holders of transport natural monopolies in railway transportation services and services for using the infrastructure of public railway transportation.

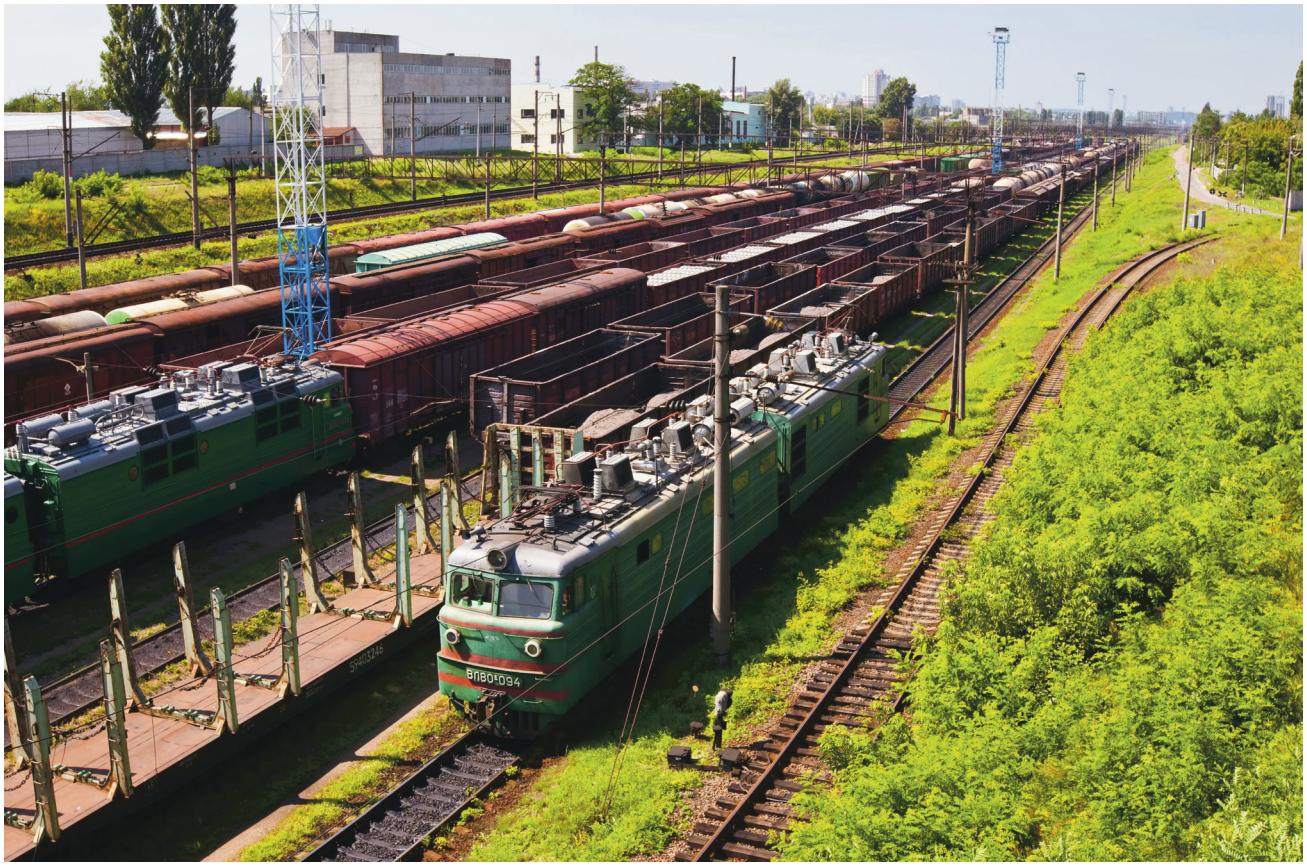
Article 10 of the Federal Law "On Protection of Competition" prohibits dominant companies to restrict competition and infringe the interests of their counteragents; the list of prohibited actions is not exhaustive. Some of the most frequent violations exposed through investigating cases on rail transportation include: refusals to conclude contracts with particular counteragents without any economic or technological justification; imposing disadvantageous contract conditions upon a counteragent; including services in the contract that a counteragent does not need; breaching pricing procedures, etc.

Disputes between railways and counteragents subject to investigation by the antimonopoly authority most frequently concern transportation contracts. Contractual regulation of transportation is not limited to contracts for just transportation services. Transporting goods starts with operations for supplying the means of transport for loading and presenting cargo by consignors for shipment. Delivery to a consignee also requires railways to complete a number of operations (works), for instance, it may include customs clearance. When shipments take place on a regular basis, consignors would like to have guarantees that railways shall provide all necessary services in the course of each shipment.

To this purpose railways propose consignors to enter in a so-called *integrated transportation services agreement*, which is different from a transportation arrangements agreement or an agreement for transport and forwarding services. It includes all possible services that a railway can provide to consignors, including customs goods transportation. The list of all services (works, operations) includes up to 50 items. It is not easy for customers to understand what they are paying for and at what rates.

Practices of the Office of the Federal Antimonopoly Service in the Sverdlovsk Region (Sverdlovsk OFAS) on exposing violations

A violation takes place when a railway unlawfully requires a counteragent to pay for works (operations, services) not provided for by the law for two reasons: 1) due to the public responsibilities of a railway as a carrier; 2) the costs of the works are included in the rates for terminal operations, for instance, preparing cars for spotting, notifying about cargo arrivals, etc. Most frequently railway customers complain to the



antimonopoly bodies about excessive rates for the services provided in the course of freight transportation, keeping goods in the customs controlled zone or supplying cars to non-public sidetracks.

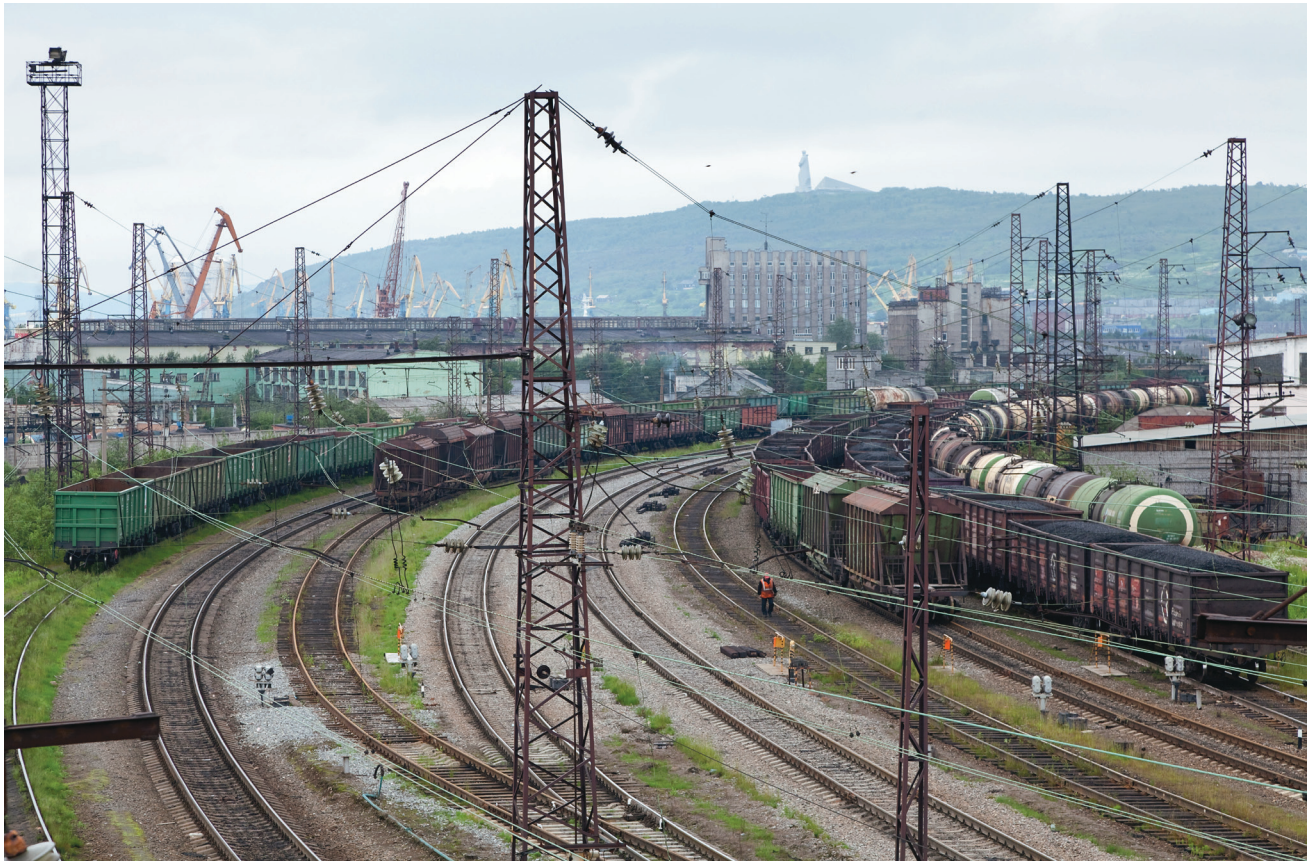
Below is a summary of some examples when Sverdlovsk OFAS exposed violations committed by "Russian Railways" OJSC in the person of Sverdlovsk Railway that unlawfully requested payments for works (services).

In the first case, "Russian Railways" OJSC violated Part 1 Article 10 of the Federal Law "On Protection of Competition" demanding a consignee to pay for the "services" allegedly provided when the goods were in the customs controlled zone. The Railway attempted to execute its public responsibilities (deliver the goods, place the goods in the customs controlled zone and exercise inner customs transit, protect and register the goods) and its obligations (payment for storage and protection of the goods in the customs control zone) at the expense of the third person (the counteragent under a goods transportation contract). The Railway also tried to impose disadvantageous contract conditions irrelevant to the subject of the contract for integrated transportation services (for instance, drawing up certain documents).

In the second case, "Russian Railways" OJSC unreasonably requested an industrial railway transport enterprise to pay for "inspecting the technical condition of the locomotives prepared for shipment in the non-operational state", classifying it as a separate service. However, the antimonopoly body established that the carrier's labour costs for exercising these works are included in the tariffs for terminal operations.

In the third case, "Russian Railways" OJSC violated pricing procedures wrongly applying regulated tariffs for supplying cars to non-public sidetracks – the company overestimated the distance for which it charged the counteragent (Clause 10 Part 1 Article 10 of the Federal Law "On Protection of Competition"). The Railway's obligations were to supply cars to non-public sidetracks approaching the receiving station for the goods delivered to the owner of the sidetrack. The Railway, however, included a clause in the contracts that cars were supplied from a railway yard located 15 km away from the receiving station and charged the counteragent for supplying and removing cars 15 km both ways.

In the forth case, Sverdlovsk OFAS revealed that "Russian Railways" OJSC breached Clauses 4 and 5 Part 1 Article 10 of the Federal Law "On Protection of Competition". Reducing production of goods when there is demand for such goods or refusing to enter in a contract, the Railway must prove that it was technologically impossible and economically inexpedient. An individual entrepreneur owns a container site on a non-public sidetrack to a station



of the Railway. The Railway did not allow an individual entrepreneur to open a station for accepting and delivering goods in universal containers and at the same time opened a neighbouring station where exercised the same operation (loading / unloading containers to/ from cars). Enjoying its monopolistic position on the market of railway transportation and being the infrastructure owner, the Railway effectively eliminated its competitor – the individual entrepreneur from the market of transportation and forwarding services. He had to stop operations and was unable to change the type of activity he was engaged in because of considerable investments in construction of the container site. However, OFAS did not have to issue a determination because the Railway understood unlawfulness of its actions and undertook efforts to open the station.

A similar case was related to container terminals in Yekaterinburg, the capital city of the province. The main railway container terminal is owned by a subsidiary of "Russian Railways" OJSC. It is located in the northern part of the city which creates considerable logistical issues associated with entering/ exiting the terminal by vehicles from other directions. In the southern part of the city a commercial organization owns a container site on non-public sidetracks approaching public rail tracks of Koltsovo station. The site met all technical requirements necessary to carry out operations with universal containers. However, the Railway decided that it could manage cargo traffic without competitors and did not allow opening a railway station for works with universal containers. As a result of the efforts undertaken by the antimonopoly body the station is now opened.

Widespread violations of the antimonopoly law in **non-public** railway transport are when the owners of sidetracks unreasonably refuse to use them for passing freight cars to warehouses of consignors / consignees. Since the owners of sidetracks have dominant position on the market of car supplying services within the geographic boundaries of sidetracks approaching a particular railway station, their actions are also subject to regulation under Article 10 of the Federal Law "On Protection of Competition".

In conclusion, the current railway transport reform generates new relations between participants of transportation by rail. However, cases investigated by Sverdlovsk OFAS show that the number of legal issues has not decreased so far. The enforcement practice is aimed at achieving the balance of interests in relations between railways and its customers.

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PROBLEMS OF DETERMINING THE DOMINANT POSITION OF ECONOMIC ENTITIES ON ADJACENT MARKETS

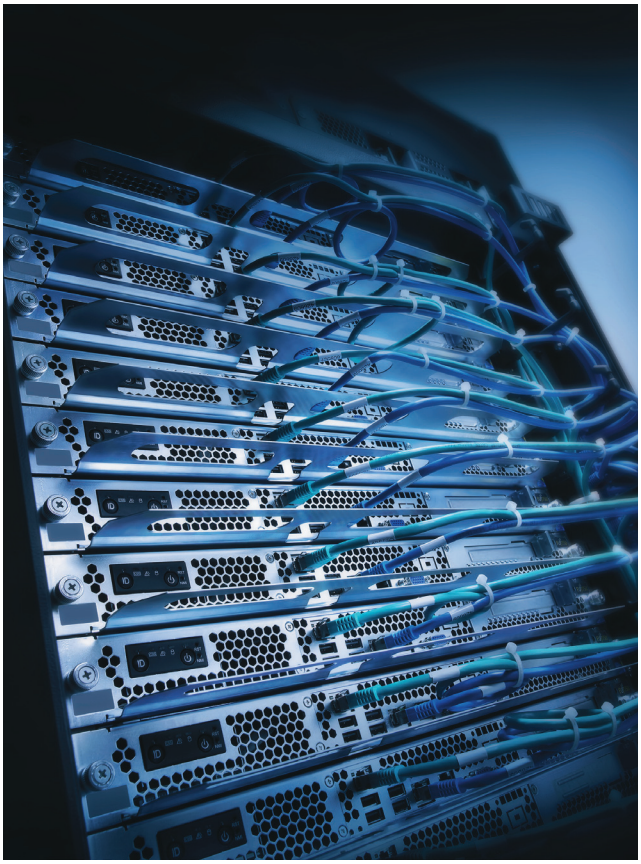
THE CASE OF TRAFFIC TRANSMISSION SERVICES

Due to the specifics of Russian economy, preventing and constraining monopolistic activities, including abusing market dominance, is one of the main avenues for supporting competition. Perhaps, the most important but also the most difficult stage is to determine whether an economic entity has dominant position on a particular market and prove it in the course of judicial proceedings.

Theory

Markets of natural monopolies are subject to strict government regulation (pricing, additional reporting and control, information disclosure, etc.) Thus, possibilities to increase profitability are limited and holders of natural monopolies tend to commit violations of the antimonopoly law on the markets adjacent to the markets of natural monopolies. At the first glance, such adjacent markets seem to be competitive with much less or no government regulation; however, there is a tendency for economic entities to abuse their dominant position, which infringes the interests of both their competitors and end consumers of goods (services).

Dealing with violations on the markets adjacent to natural monopolies, the antimonopoly bodies often have to analyze the state of competitive environment. Such analysis, however, would be pretty much a "by-the-book" approach since the outcome is practically predetermined. No.135-FZ Federal Law "On Protection of Competition" a priori states that a holder of natural monopoly has dominant position on a naturally monopolistic market. Part 1 Article 4 of the Law "On Natural Monopolies" contains a non-exhaustive list of activities classified as natural monopolies. The range of naturally monopolistic markets is wider than the list provided for by the Law. A conclusive evidence is that until 6th January 2012 water supply services were not listed in Part 1 Article 4 of the Law "On Natural Monopolies" although by nature they are identical to heating energy transmission, which the Law describes as natural monopolistic activity. Thus, in reality markets in the state of natural monopoly may include not only the fields specified in Part 1 Article 4 of the Law



"On Natural Monopolies" but also the markets where holders of natural monopolies operate and that have signs of natural monopoly under Article 3 of the Law. Typically, such markets are adjacent to the markets of natural monopolies listed in Part 1 Article 4 of the Law.

Practice

In 2011 over 70% of the cases on abusing market dominance in the Voronezh region took place on the markets in the state of natural monopoly.

A perfect example of an adjacent market analyzed by the Office of the Federal Antimonopoly Service in the Voronezh region (Voronezh OFAS Russia) is

the market of traffic transmission through pointes of interconnect at the local level in a case against "Centre Telecom" OJSC. The company renders public telecommunications services and is a holder of natural monopoly under Part 1 Article 4 of the Law "On Natural Monopolies".

The Government of the Russian Federation approved the list of public telecommunications and postal services the rates for which are subject to regulation by the Federal Tariff Service. Traffic transmission through pointes of interconnect at the local level is not included in the list.

Voronezh OFAS Russia discovered that traffic transmission is secondary to the main type of communications activity in which a particular operator is involved: it establishes interaction between telecommunications networks and transmit traffic enabling connections and information transfer between users of interacting networks, and due to inseparable technological linkage with public telecommunications services offered by providers it cannot be rendered independently.

Traffic transmission at the local level is inseparably connected to local telephone services as a necessary condition. The volume of traffic mutually depends on the number of subscribers to the local telephone network of the operator. Transmitting traffic through pointes of interconnect at the local level is a naturally monopolistic activity as it is technically impossible to end a call to a subscriber by-passing the operator ("Centre Telecom" OJSC), to which local telephone network a subscriber is connected. Thus, the end call services (traffic transmission) provided by "Centre Telecom" OJSC cannot be replaced with any other service or end call service (traffic transmission) provided by other operators.

"Naturally monopolistic" character of traffic transmission through pointes of interconnect at the local level (local end call service) corresponds to the concept of "natural monopoly" and the actual state of the market in question but does not indicate that this activity is directly regulated by the Law "On Natural monopolies". It simply characterized the market with the single market participant - "Centre Telecom" OJSC. The boundaries of the traffic transmission market match the boundaries of the market of public telecommunication services provided by the operator ("Centre Telecom" OJSC).

Voronezh OFAS Russia arrived to the conclusion that "Centre Telecom" OJSC has dominant position on the market traffic transmission through pointes of interconnect at the local level. The antimonopoly body did not specially analyze the state of competitive environment on the market in question.

This approach - establishing dominant position of an economic entity on a market adjacent to the market of natural monopoly without conducting market analysis - is rather complex and often is

not supported by Courts of Law due to absence of specialized technical knowledge and reluctance of judges to carefully look into technological specifics of markets. For instance, Cassation Court twice forwarded the case of "Centre Telecom" for reconsideration indicating that the antimonopoly body had been unable to prove the company's dominant position, particularly, because OFAS failed to analyze the state of competition on the market according to the established procedures. "Centre Telecom" OJSC insisted that it did not have the dominant position on the market of traffic transmission arguing that traffic transmission and public telecommunications services are not linked technologically and constitute independent service.

However, the Supreme Arbitration Court of the Russian Federation drew a line on the case, explicitly stating that public telecommunications services and traffic transmission have inseparable technological connection, and concluded that the state of competition on both markets was identical – the state of natural monopoly. The Supreme Arbitration Court fully supported OFAS decision that "Centre Telecom" OJSC as a holder of natural monopoly had dominant position on the market of public telecommunications services as well as on the adjacent market of traffic transmission at the local level.

It shows that the approach to determine dominant position on a market adjacent to the natural monopoly without analyzing in detail the state of competition on the market is logical and justified since such adjacent markets are not independent due to their technological specifics. Often this is the only possible approach enabling prompt and effective response of antimonopoly bodies to violations committed by natural monopolies (proper analysis of the state of competition typically is time-consuming as it takes around two months). Ultimately its helps avoid irreparable consequences for consumers, competitors and competition in general.

To establish unified practice accepted by Courts, the antimonopoly bodies should study in detail interconnection between the markets and then describe the findings in decisions on antimonopoly cases.

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REGULATING INSTALLATION AND DISMANTLING ADVERTISING STRUCTURES

The Federal Law "On Advertising" regulates mostly the content of advertisements and the disseminating procedures in advertising. Article 19 of the Law, however, specially focuses on the issues associated with installing advertising carriers rather than on the process of placing advertised information on a carrier.

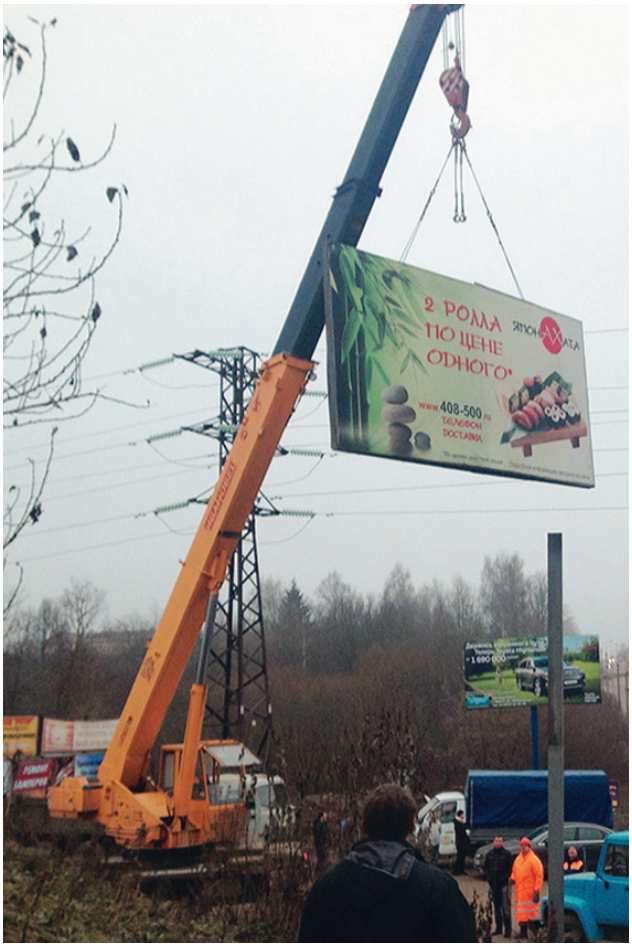
Approaches to regulating installment of advertising structures are similar to those applied in antimonopoly regulation. For instance, advertising structures should be placed on state or municipal property as an outcome of competitive bidding; shares controlled by market participants should be identified and the threshold is set at 35%.

Procedures regulating some aspects of installing, operating and dismantling advertising structures are beyond the competence of the antimonopoly bodies. At the same time, the Antimonopoly Service is responsible for enforcing compliance with the law on advertising and must monitor and evaluate actions of the authorities and market participants in this field.

FAS is often approached by representatives of the authorities or local self-government bodies seeking explanations which actions shall be considered legitimate under the current law as well as by economic entities unhappy with particular decisions made by local self-government bodies on outdoor advertising. The obligation to explain controversial or unclear issues of Article 19 of the Federal Law "On Advertising" is assigned solely to the Central FAS Office. FAS responds to individual enquiries and on a regular basis and also prepares summaries of explanations to the most frequent questions, which are then forwarded to the regional FAS offices.

Under Article 19 installing an advertising structure requires a contract between its owner and the owner of immovable property where it is intended to arrange the installation (unless owned by the same person). The Law specifies contract procedures only for the cases of installing an advertising structure on state or municipal property. Specifics of such procedures is determined by the above-mentioned approaches to regulating installment of advertising structures, which are similar to the approaches used in antimonopoly regulation.

Apart from a contract with the owner of immovable property, lawful installation of advertising structures in



a municipality requires permission from a local self-government body because advertising structures are installed within municipalities each of which has a unique architectural look and land-use planning. The procedures for issues permission to install advertising structures are determined by each local self-government body independently as follows from the

standpoint taken by the Constitutional Court of the Russian Federation: local self-government bodies make such decisions independently if the issue of installing advertising structures concerns municipal property. Issuing permission, a local-self-government body shall obtain consent of other various authorized bodies on possibility to install structures with particular technical characteristics in a particular location.

In the absence of a contract with the owner of immovable property or permission from a local self-government body legitimacy of the installed advertising structure is questionable. Part 10 Article 19 of the Federal Law "On Advertising" prohibits unauthorized installations. Such advertising structures should be demolished on the basis of a determination issued by a local self-government body.

However, judicial practice recognized as unauthorized only those advertising structures, for which local-self-government bodies have never issued permission in principle (installed without permission). To demolish such structures there is no need to approach a Court of Law and under Part 10 Article 19 a determination issued by a local self-government body shall suffice.

Advertising structures for which permission was issued and then later withdrawn or pronounced void cannot be considered originally unauthorized, and under Parts 22 and 22.1 Article 19 to demolish the structures without valid permission local-self-government bodies must file a lawsuit requesting forced demolition.

The antimonopoly bodies do not have powers to issue determinations to demolish unauthorized advertising structured and can only file lawsuits seeking their invalidation.

In view of the widespread intentions of municipalities to put installation of advertising structures in their areas to order, the State Duma of the Russian Federation is considering amendments to Article 19 of the Federal Law "On Advertising". The amendments, in particular, streamline the procedures for demolishing invalid advertising structures. Thus, adopting the amendments will considerably change regulation of outdoor advertising.

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ANTIMONOPOLY CONTROL OVER CABLE TV

The market of rebroadcasting TV programmes through cable networks is very dynamic and diverse, its active development and emerging new adjacent markets such as digital or "interactive" TV pushes the antimonopoly bodies to constantly study the market specifics and refine antimonopoly regulation of cable television.

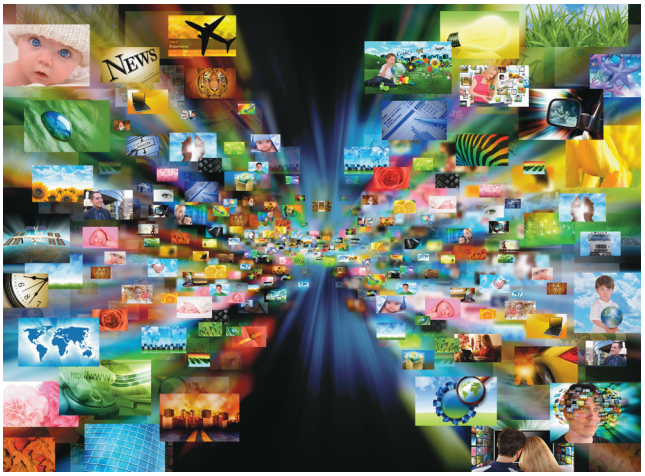
The paper outlines the most interesting cases investigated by the Office of the Federal Antimonopoly Service in the Vladimir region (Vladimir OFAS) in the field of retranslating services through cable TV networks.

The market in the Vladimir region is highly concentrated, with a small number of market participants, whose operations due to technological specifics are limited to the networks available in a particular area.

In 2011, Vladimir OFAS investigated a case against a cable TV operator in Kovrov – "Ekran" Ltd., which had dominant position in the communications market and provides services to a broadcasting company for delivering TV channel signal to the subscribers. Without any economic or technological justification the operator refused to sign a protocol (an agreement) with a company on intentions to obtain a broadcasting license and then further refused to conclude a contract in spite of technical possibility to render services. OFAS instructed the operator to stop violating the antimonopoly law.

An interesting case was initiated against "Zhanr" CJSC (Part 1 Article 14 of the Federal Law "On Protection of Competition"). Communications services were provided using a reconstructed communication structure before it was commissioned, and agreements for such services were concluded with subscribers. As a result, a competitor of "Zhanr" CJSC that could have lawfully provided similar services to subscribers received less income than it was due. Vladimir Regional Arbitration Court dismissed the company's claim to invalidate OFAS decision.

The most representative, however, is a case opened against "Navigator" Ltd. under Clause 6 Part 1 Article 10 of the Federal Law "On Protection of Competition". The respondent increased the fee for using cable TV for the residents of an apartment house; although the fee for other houses serviced by the respondent remained the same. The respondent explained that that the owners of residential premises in the house charged "Navigator" Ltd. a rental fee for using engineering structures in the building. Under



the Federal Law "On Communications" operators can conclude contracts with owners and possessors of buildings and operate communications means and constructions located in these buildings; while the owners or possessors of the immovable property can charge an adequate fee for using their property. A representative of the apartment house explained to OFAS that the fee for using constructive elements of the house had been determined on the basis of market prices for renting identical property and customary practices. The antimonopoly body established that in the section in question "Navigator" Ltd. had a trunk line which serviced 10,000 subscribers; therefore the costs of operating and maintaining the line were included in the overall subscribers' fee. Vladimir OFAS requested "Navigator" Ltd. to eliminate the violation by recalculating the fee for the subscribers residing in the apartment block who paid a higher fee for the cable TV in January-March 2012 in comparison with the regular fee (175 instead of 160 Rubles / month). The determination was executed.

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