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CJEU examines Article 101 application in a Latvian software distribution case

On 18 November 2021, the Court of Justice of European Union (CJEU) delivered a preliminary ruling in a case C-306/20 *Visma Enterprise*. This case concerns a software distribution setup that provides for a client reservation system between distributors of the same software program. The preliminary ruling sheds light on criteria which need to be assessed when analyzing compliance of such systems with competition rules, as well as clarifies that the assessment and process of fines for a competition law violation has no bearing on whether the violation took place.

Fine imposed by Latvian Competition Council

Back in December 2013, the Latvian Competition Council (LCC) fined a software supplier SIA Visma Enterprise (previously – FMS Software) with a 45 000 LVL (64 476 EUR) fine for a clause in its accounting software distribution agreements that, the LCC found, restricted competition between Visma's distributors.

The notorious clause required the distributors of Visma's accounting software to register potential transactions between the distributor and the end-user at the start of the selling process in a database developed by Visma. The clause provided that the sale would be prioritized on a first come first served basis, where a distributor who registered the client first would enjoy a priority with the particular client for six months, unless the client objected.

The competition watchdog found that while setting such a database with end-users is not prohibited, the client reservation clause constituted an "advantage in the sales process" which is a "by object" restriction that hinders distributors of Visma's accounting programs to compete for clients prior to closing the sale, and is comparable to market division in the form of allocating clients. With this, the LCC found a violation of national equivalent to TFEU 101(1) and considered no need for further analysis of the real effects of this agreement on the market. At the same time, the authority did not penalize the distributors.

Legal proceedings and request for preliminary ruling

Visma challenged the LCC's decision in national courts, where the case was reviewed in total four times, twice being rejected by the Regional Administrative Court, twice going up to the Supreme Court and each time being sent back again to the Regional Administrative Court for a repeated review, until in 2020 the Regional Administrative Court decided to stop the proceedings and send multiple questions to the CJEU for a preliminary ruling.

First, the referring court asked whether an agreement between a supplier and a distributor which provides for the specific priority clause (six months "advantage in the sale process" to the distributor that is first to register a potential transaction, unless the end-user objects) is a prohibited agreement under TFEU Article 101(1), and if so, whether it is prohibited as such or its effects must be analyzed to find a violation (that is, whether it is a prohibition "by object" or "by effect"). The national court also inquired whether such a clause constitutes a violation if the market share of the supplier is below 30% (i.e., the market share threshold that allows certain vertical agreements to benefit from a safe harbor of a vertical block exemption and thus not subject to prohibition).

To this, the European judges noted that the facts of the case are not set because there is no understanding what was the purpose of the contested clause and how the "advantage in the sale process" manifested. Since the LCC claimed that only the distributor that has first registered the user in Visma's database could proceed with the transaction, but Visma contested this allegation, the CJEU stated that to find a violation, first the aim of this clause had to be determined and the specific legal and economic context evaluated.

It follows from the judgement that the contested clause (a system whereby a software distributor upon registering a potential transaction with the supplier enjoys priority in closing this transaction, unless the end-user objects it) cannot be automatically found prohibited as such ("by object") unless sound legal and economic analysis demonstrates sufficiently appreciable level of distortion of competition for such a finding.

When assessing such clauses, national authorities should analyze the structure of the relevant market, characteristics and availability of the products or services, position of the market players (such as the below 30% market share) and the effect of the clause on competition, including, by modelling a counterfactual scenario.

In general, the European court noted that a restriction of competition between distributors of the same product or services brand (*intra-brand competition*) usually only raises competition concerns if competitors between different

brands of the relevant product (*inter-brand competition*) is weakened.

Second, the national court asked whether the specific clause, if found to be prohibited, may be justified by individual exemption as provided in TFEU Article 101(3). Here, the CJEU relied on its previous jurisprudence, concluding that agreements falling under the prohibition of TFEU 101(1) may still be justified if they cumulatively fulfil the four conditions under TFEU 101(3) proving that benefits of the restriction outweigh any anticompetitive effects.

Lastly, the Latvian court made a question raised by Visma in its appeal, namely, whether because the national competition authority only fined the supplier, and not the distributors, this excludes existence of a prohibited agreement and thus violation of TFEU Article 101(1).

Here CJEU judges found that a competition law violation (agreement prohibited under Article TFEU 101) and a penalty for this violation (attributing liability to participants of the prohibited agreement) are two distinct issues, and that the finding of a TFEU 101 violation cannot be reversed on the basis that the competition authority made a differentiated assessment of liability of the parties to this prohibited agreement.