

CORPORATE LAW

Challenging Sham Litigation

A Brazilian regulatory agency takes on Germany's Siemens in a case of alleged anti-competitive practices that is likely to set an important precedent for regulators and the courts in protecting free market competition.

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Brazil's Economic Defense Council (CADE), a Justice Ministry agency responsible for monitoring market competition, released an opinion earlier this year related to a legal dispute between German giant Siemens VDO Automotive and Brazilian firm Seva Engenharia Eletrônica ongoing since 2005. It is the first time that CADE has interjected in a case involving alleged abuse of dominant market power to block the market entry of a competitor through the use of legal challenges to regulatory measures. This kind of uncompetitive behavior is known in the US and other jurisdictions as sham litigation.



Fernando Furlan, the author of the CADE opinion, charged that Siemens had engaged in abusive legal action against Seva, requiring that the Brazilian company include certain provisions in its contracts that Siemens, itself, does not. In addition, Siemens questioned the competence of government agencies -- such as Contran, a transportation regulatory body, and Inmetro, The National Institute of Metrology, Standardization and Industrial Quality -- to regulate the new digital tacograph introduced by its competitor. Tacographs are electronic systems for recording driving times and rest times for drivers of commercial vehicles. In 2005, Siemens VDO Automotive had an 85% share of Brazil's analog tacograph market and was challenged by the entry of a new player offering a digital alternative.

The case is still far from decided, as the other members of the CADE council must vote on the ruling, but the extensive nature of the evidence reviewed in this case suggests it could set an important precedent for future anti-competition cases. CADE's judgment will signal to the market that any kind of anti-competitive practices will be subject to official sanction.

Legal remedies against anti-competitive practices are spelled out in Paragraph V, Article 21 of the Law 8,884/94, which defines them as "obstacles to the establishment, the functioning or the development of a competitive firm or of a supplier, buyer or financier of goods or services." Legislation within the Civil Code already provided for penalties for bad-faith legal proceedings. Law 5,869/73 provides for the application of sanctions against those who use the legal system for suspect or sinister purpose (Article 17), or who initiate judicial proceedings without legal merit.

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While Article 17 of the Civil Code relates to specific cases, a ruling by CADE based on an infraction against the economic order, whether it involves an administrative or judicial sanction, has a much broader impact and serves as a warning to the entire marketplace.

If Siemens is convicted by CADE, meaning that the company will be subject to penalties under Law 8,884, the company will still have an opportunity to argue its case in court. Weighing against it, however, will be a significant body of evidence and argument put forth by experienced CADE regulators charged with defending market competition.

While we await the final administrative ruling by CADE, as well as the result of the court battle to follow, the big question that remains is whether Brazil is sufficiently prepared to deal with the technical and legal complexities of regulatory conflicts.

Regardless of the final outcome in this case, clearly Brazil's regulatory apparatus is maturing. It is essential that it maintain its independence. In this respect, it would appear that CADE is well ahead of other regulatory agencies, which have shown scant willingness to challenge similar predatory practices.

It is worth noting in this case that CADE took upon itself the task of analyzing the obstacles to free competition, with the understanding that these bad business practices ultimately hurt the final consumer. Many companies refuse to accept competition or to give up market share. Instead, they use their economic muscle to annihilate their competitors; if necessary, using unfounded legal action to achieve that end. Tough action by CADE in the Siemens case will ensure that similar cases of abuse are brought to the attention of CADE and the courts, thus strengthening the competitive and regulatory environment.

In order for CADE and other regulators to be successful, they must have a profound understanding of the peculiarities of each market sector where a competitive dispute arises. In addition, they must be conscious of the fact that the business environment is competitive by nature and be able to determine what constitutes – what we, in the legal profession, might call -- “reasonable” competition.

At the same time, it is important that CADE not shy away from taking a tough stance when there is a clear case of coordinated effort to strangle competition, a clear abuse of power. In the great majority of cases, tactics adopted by companies to create artificial barriers to competition are subtle, which often makes them difficult to detect by anyone without plenty of market knowledge and legal experience.

When the judgment in the Siemens VDO Automotive vs Seva Engenharia Eletrônica case is handed down, we will have an important precedent which will help guide future judgments related to protecting market competition by CADE and perhaps even by the courts.

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