COMMISSION

COMMISSION DECISION

of 17 June 1998

relating to a proceeding pursuant to Article 86 of the EC Treaty

(IV/36.010-F3 — Amministrazione Autonoma dei Monopoli di Stato)

(notified under document number C(1998) 1437)

(Only the Italian text is authentic)

(Text with EEA relevance)

(98/538/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community,

Having regard to Council Regulation No 17 of 6 February 1962, first Regulation implementing Articles 85 and 86 of the Treaty [1], as last amended by the Act of Accession of Austria, Finland and Sweden, and in particular Articles 3(1) and 15(2) thereof,

Having regard to the applications submitted pursuant to Article 3 of Regulation No 17 by R. J. Reynolds Tobacco GmbH and R. J. Reynolds Tobacco Company SAE, Rothmans International BV and International Tobacco Company for a finding that Amministrazione Autonoma dei Monopoli di Stato has infringed Article 86 of the EC Treaty,

Having regard to the Commission decision of 27 February 1997 to initiate proceedings in this case,

Having given the firm concerned the opportunity to make known its views on the objections raised by the Commission in accordance with Article 19(1) of Regulation No 17 and with Commission Regulation (EEC) No 99/63 of 25 July 1963 on the hearings provided for in Article 19(1) and (2) of Regulation No 17 [2],

After consulting the Advisory Committee on Restrictive Practices and Dominant Positions,

Whereas:

PART I

THE FACTS

I. AAMS

(1) Amministrazione Autonoma dei Monopoli di Stato (hereinafter referred to as 'AAMS') is a body forming part of the financial administration of the Italian State which, in addition to carrying out various administrative activities, also engages in the production, import, export and wholesale distribution of manufactured tobaccos.

(2) Article 45 of Law No 907 of 17 July 1942 [3] gives AAMS the exclusive right to produce manufactured tobacco on national territory.

AAMS currently exercises that right through 21 production plants employing some 7 500 persons. In those plants, AAMS produces not only the cigarette brands it owns but also brands owned by Philip Morris. To that end, it has over several decades concluded licensing agreements with Philip Morris

[1] OJ 13, 21. 2. 1962, p. 204/62.
[2] OJ 127, 20. 8. 1963, p. 2268/63.
[3] Law on the salt and tobacco monopoly, GURI (Gazzetta Officiale della Repubblica Italiana) No 199, 28. 5. 1942.

to manufacture the Marlboro, Muratti Ambassador, Mercedes and Diana brands in particular. In 1995 AAMS manufactured some 54 million kilograms of cigarettes, of which 40 million kilograms were of its own brand and 14 million were branded as Philip Morris.

(3) In addition, AAMS engages in the import, introduction into the country by way of intra-Community acquisition, distribution and sale of manufactured tobaccos. It has a distribution capacity of some 102 million kilograms of cigarettes per annum.

II. **The products and their distribution in Italy**

1. *The products*

(4) The products concerned by these proceedings are cigarettes (and not, therefore, other tobacco products such as cigars, cigarillos, cut tobacco and snuff).

In 1995 legal sales of cigarettes in Italy totalled 90 million kilograms. The cigarettes were manufactured, variously, in Italy (about 54 million) by AAMS and in other Member States (about 36 million).

In recent years the market shares held by the various producers have been as follows:

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
AAMS	62,2	61,9	61,1	58,4	56,0	51,5	48,5	48,5	45,1	43,6	42,1
Philip Morris	30,4	30,9	31,8	34,1	36,3	40,1	42,6	42,9	46,9	49,9	51,6
BAT	2,9	2,9	2,6	2,7	2,7	2,9	3,1	2,9	2,7	2,2	2,0
Rothmans	1,1	1,1	1,2	1,3	1,6	2,0	2,4	2,4	2,4	2,1	1,9
Reynolds	1,5	1,6	1,8	2,0	2,1	2,3	2,3	2,2	1,9	1,4	1,5
Others	1,9	1,6	1,5	1,5	1,3	1,2	1,1	1,0	1,0	0,8	0,9

2. *Distribution of the products in Italy*

(5) The importation into Italy of cigarettes from other Member States and their wholesale distribution were 'authorized' — that is to say liberalised — by Article 1 of Law No 724 of 10 December 1975 [4], which provided that, by way of derogation from Article 45 of Law No 907/42 referred to above, imports were authorised through distribution warehouses other than those of AAMS provided, however, that the warehouses had been authorised by the financial administration and that the imports were already contained in the table listing the selling prices of cigarettes. Subsequent decrees of the Finance Ministry, and in particular the Ministerial Decree of 26 July 1983, laid down the criteria and arrangements for obtaining authorisation to set up warehouses and the rules governing the movement of the imports.

However, until now all Community cigarettes have been imported into Italy by AAMS, which also handles their wholesale distribution on the basis of agreements concluded by it with the foreign manufacturers wishing to sell their cigarettes in Italy.

(6) Law No 1293 of 22 December 1957 [5] provides for the organisation of the services for the distribution and sale of articles subject to monopoly and, therefore, cigarettes. Under that Law, the services are provided by:

(a) departmental inspectorates;

(b) warehouses;

(c) warehouse outlets;

(d) 'magazzini';

(e) retailers.

(7) The departmental inspectorates (hereinafter referred to as the 'inspectorates') supervise the distribution and sale of the monopoly goods. In accordance with the rules laid down by the AAMS Executive Board, they organise the said services and ensure their smooth operation (Article 2 of Law No 1293/57). The inspectorates are part of AAMS and are headed by AAMS officials having disciplinary authority over the staff of the inspectorate and dependent bodies, and over 'magazzini' staff and retailers.

(8) The warehouses for monopoly goods (also referred to as primary distribution units — hereinafter referred to as 'warehouses') are responsible for receiving the monopoly goods, storing

[4] GURI 1 4, 7. 1. 1976.

[5] GURI No 9, 13. 1. 1958.

them and distributing them for sale (Article 3(1) of Law No 1293/57). The warehouses collect the tax on sales of monopoly goods and all revenue accruing to AAMS and pay them to the Treasury (Article 3(2) of Law No 1293/57). They form part of AAMS and are run by AAMS officials. There are currently 21 warehouses.

The warehouse sales outlets remove the monopoly goods from the warehouses against payment of the appropriate amount and sell them to the authorised retailers. Exceptionally, they may also supply, on behalf of the warehouses, the 'magazzini' (Article 4(1) of Law No 1293/57). In order to carry out their tasks, the sales outlets receive an allocation of 'sale or return' goods (Article 4(2) of Law No 1293/57).

(9) The 'magazzini' (also referred to as secondary distribution units, but referred to hereinafter as 'magazzini') collect the monopoly goods from the warehouses and sales outlets against payment of the corresponding amount and sell them to authorized retailers. The 'magazzini' are managed under contract by private individuals who receive an allocation of 'sale or return' goods and are required to provide a guarantee (Article 5(1) and (2) of Law No 1293/57). The subcontractor is remunerated on the basis of the agreed weight of the goods sold (Article 5(3) of Law No 1293/57). Management of the 'magazzini' is governed by Decree No 1074 of 14 October 1958 [6], by a detailed list of specifications and by instructions from AAMS. There are currently some 600 'magazzini'.

(10) The retailers of monopoly goods (hereinafter referred to as 'retailers') purchase their cigarette supplies from the 'magazzini' and stock them with a view to selling them to the public.

The retailers are divided into ordinary and special retail stores. State retail stores were abolished by Law No 198 of 13 May 1993.

The ordinary retail stores are run by private-sector managers under contracts of not more than nine years' duration (Article 19 of Law No 1293/57). They are set up as and when AAMS deems it necessary and useful in the interests of the service (Article 21 of Law No 1293/57) and are classified as first- or second-category stores, depending on the revenue yielded by the premiums on tobacco and tobacco products.

[6] GURI No 308, 22. 12. 1958.

The special retail stores were set up to satisfy particular requirements of the retail sales service and may be temporary in cases where it is not possible to establish an ordinary store (Article 22 of Law No 1293/57).

AAMS may also authorise sales of monopoly goods in public commercial concerns, community centres and cooperatives. Such special authorisation is granted in the form of a 'temporary licence' (Article 23 of Law No 1293/57).

All retailers are required to pay AAMS an annual fee in proportion to their income and an additional flat-rate annual fee (Article 26 of Law No 1293/57). They are paid through a system of 'premiums', which means a fixed amount determined by decree of the Finance Ministry in agreement with the Treasury and in the light of the opinion of the AAMS Administrative Board (Article 24 of Law No 1293/57). When the retailer collects the monopoly goods, he pays an amount corresponding to their price, less the amount of the premium. Management of the retail outlets is governed by Decree No 1074/1958, by a detailed list of specifications and by instructions issued by AAMS.

There are at present some 58 000 retailers and some 18 000 public retail outlets with a 'temporary licence'.

(11) Even if Community cigarettes were brought direct into Italy by operators other than AAMS and were therefore sent to wholesale warehouses other than those controlled by the latter, sales to the public would nevertheless continue to be subject to the monopoly. As a result, other importers would in any event have to use the retailers referred to above in order to sell cigarettes to the public.

III. **Behaviour of AAMS**

(12) The behaviour of AAMS at issue here relates to:

— the standard distribution contract concluded by AAMS with certain cigarette manufacturers under which the latter entrust AAMS with the introduction and wholesale distribution of cigarettes manufactured in another Member State,

— certain unilateral decisions taken by AAMS concerning cigarettes manufactured in another Member State and subsequently brought into Italy.

1. *Distribution contracts*

(13) AAMS has developed a model contract (hereinafter referred to as the 'distribution contract') for the wholesale distribution in Italy of cigarettes manufactured in any other Member State by another producer (hereinafter referred to as 'foreign firm'). In that context, AAMS sends the distribution contract for signature by the foreign firm that plans to entrust AAMS with the distribution of its cigarettes in Italy. AAMS uses the same contract for all foreign firms. The latest version of the contract was produced at the end of 1993. It has a five-year duration and ends on 31 December 1998.

(14) The text of the distribution contract is unilaterally laid down by AAMS, foreign firms having no option but to sign it as submitted.

The facts relating to the renewal of the most recent distribution contract (end 1993/early 1994) show that foreign firms have no opportunity to negotiate any of the contract clauses or to suggest changes that take account of their views and interests.

It is pointed out in this connection that, by letter dated 10 November 1993, R. J. Reynolds Tobacco Company SAE (hereinafter referred to as 'Reynolds') sent AAMS a 'list of more specific observations we should like to discuss with you with a view to their subsequent incorporation in the contract in the form of clauses'. AAMS did not follow up the letter and simply presented Reynolds, by letter dated 28 December 1993, with a new distribution contract which did not take account of Reynolds' proposals contained in its letter of 10 November. Then, on 7 January 1994, AAMS informed Reynolds that, if it did not receive formal approval of the distribution contract, it would suspend distribution and sales of its cigarettes.

Similarly, the letters sent by British American Tobacco (Deutschland) Export GmbH (hereinafter referred to as 'BAT')) containing proposals relating to renewal of the contract received no reply.

Finally, a request made by Rothmans International BV (hereinafter referred to as 'Rothmans') for discussions on the possibility of amending the distribution contract met with the same response. In reply to the request for discussions made by Rothmans in its letter of 12 November 1993, AAMS simply forwarded on 21 December 1993 the text of the new contract, which took no account at all of the proposals by Rothmans, which 'wished to reach ... agreement to distribute [Rothmans] products in accordance with the provisions of the draft contract ... to avoid an interruption of continuity in distribution ...'. On 7 January 1994 AAMS informed Rothmans that it had 'studied with care the said request' adding that 'despite the best will in the world, it has not been possible to integrate them in the provisions of the contract already sent to your company, a contract already approved, moreover, by our administrative board. The draft contract submitted for approval by your company must, therefore, be regarded as definitive ... We await receipt of your copy of the contract, duly signed ... failing which AAMS will be compelled to suspend the distribution and sale of your company's products.' Faced with this stance, Rothmans informed AAMS by letter of 10 January 1994 that it would sign the new contract but added, 'We do, however, want to express our regrets that it has not been possible to include in the contract or even discuss with you the points we mentioned in our letter of 12 November 1993'.

(15) The most important clauses of the distribution contract may be summarised as follows:

(a) the foreign firm entrusts AAMS with the wholesale and retail distribution in Italy of the brands of processed tobacco listed in the appendix to the contract (first paragraph of Article 1);

(b) the list of tobacco brands in the appendix to the contract is updated directly by AAMS in consequence of and in conformity with administrative provisions issued by the competent government authority concerning any new additions to the price-list of brands (second paragraph of Article 1);

(c) once a brand has been added to the price list, AAMS allows the foreign firm, twice a year, to introduce new brands in its distribution system (third subparagraph of Article 1);

(d) the foreign firm pays AAMS an amount calculated, in respect of each brand, on the basis of parameters which take account of quantities sold (Article 7 and Appendix C). The payment for cigarettes is based on every kilogram sold in accordance with the annual scale of sales laid down for each brand:

— up to 100 000 kg and new brands:	ITL 4 430/kg
— from 100 001 kg to 500 000 kg:	ITL 3 800/kg
— from 5 001 kg to 1 million kg:	ITL 3 600/kg
— from 1 000 001 kg to 3 000 000 kg:	ITL 3 400/kg
— over 3 000 000 kg:	ITL 2 900/kg

(e) payment for products is subject to presentation by the foreign firm of a monthly invoice in respect of the quantities transferred during the same period from the warehouses to the 'magazzini'. To that end, AAMS makes available within the first 10 days, and in any case not later than the first 15 days of the following month, for each brand, a list showing the status in respect of each warehouse. AAMS then issues the order of payment to the State Accounting Department *(Contabile del Portafoglio dello Stato)* within 25 days of the date of receipt of the invoice from the foreign firm (Article 9);

(f) for the initial introduction of new brands, the quantities of cigarettes to be imported or acquired by way of intra-Community acquisition may not exceed 5 000 kg (fifth subparagraph of Appendix B). As regards subsequent imports and for the 12 months following the first order, orders presented by AAMS will correspond to sales for the previous month (sixth paragraph of Appendix B);

(g) AAMS undertakes to order from the foreign firm the quantities of products necessary to ensure that uninterrupted supplies are available to the primary and secondary distribution units, according to actual market demand (first subparagraph of Article 2);

(h) the monthly quantities necessary to ensure that those aims are achieved are determined as follows:

— the stock at the warehouses at the starting date of the contract and at the beginning of each subsequent calendar year is based on the average monthly sales of the previous year, commensurate with the number of months, as follows: two months for brands whose monthly sales do not exceed 500 000 kg and one month for the others (first paragraph of Appendix B),

— the foreign firm supplies monthly orders commensurate with the quantities sold during the preceding month (second paragraph of Appendix B),

— if the foreign firm intends to introduce extra supplies of products in excess of those defined above but not exceeding 30 % of the monthly order allowed for each brand, then the amount of such extra supplies must be agreed with ARMS, taking account of the latter's actual handling capacity and foreseeable demand (fifth subparagraph of Article 2),

— should the foreign firm introduce extra supplies of cigarettes, the payment due to AAMS is increased by ITL 600 per kg, calculated on the basis of the total quantity supplied during the month in question (sixth subparagraph of Article 2);

(i) the quantities of cigarettes ordered by AAMS are to be supplied by the foreign firm on the basis of monthly plans for distribution among the warehouses, agreed on each individual occasion by the two firms (second subparagraph of Article 2);

(j) the foreign firm supplies cigarettes packaged in accordance with current regulations. In addition, the cigarettes must have the word 'Monital' printed on them lengthways (first subparagraph of Article 4);

(k) AAMS may carry out inspections and qualitative analyses on samples of imported cigarettes (first subparagraph of Article 5). To that end, the foreign firm is required to pay a fixed annual amount for each brand (second subparagraph of Article 5);

(l) the foreign firm is entitled to appoint its own representative in Italy, who may visit warehouses, 'magazzini' and retailers (first and second subparagraphs of Article 10). In order to carry out these tasks, the representative may employ staff (fourth subparagraph of Article 10). The appointment of the representative and of staff must be notified to AAMS (fifth subparagraph of Article 10);

(m) both the foreign firm and AAMS agree to desist from any form of cigarette promotion or the granting of incentives to wholesalers and retailers. In the event of repeated breach and proven liability of the foreign firm or one of its representatives, the foreign firm may not undertake the abovementioned visit without having previously replaced the representative concerned (sixth subparagraph of Article 10);

(n) the foreign firm undertakes to supply to AAMS cigarettes that do not conflict with the relevant laws in force in Italy. In the event of any breach of this obligation, the foreign firm must withdraw the product and bear all expenses connected with the withdrawal, accepting all responsibility stemming from the marketing of the product (Article 11);

(o) AAMS is entitled to return to the foreign firm cigarettes that are no longer in perfect condition on account of lengthy storage or accident. In such cases, any expenses connected with returned goods are borne by the foreign firm (fifth and sixth subparagraphs of Article 13);

(p) AAMS undertakes to observe impartiality in its distribution network, at any time and at any level thereof, with regard to all products distributed, whether Italian or foreign, however well known or important, ensuring that such products are distributed at the various sales outlets in accordance with market requirements (Article 12);

(q) the distribution contract runs for five years (first subparagraph of Article 15). However, if the foreign firm decides to distribute its own cigarettes, directly or indirectly, to wholesalers in Italy, the distribution contract may be terminated by either party subject to notice of three months (second subparagraph of Article 15).

2. *Unilateral decisions concerning imported cigarettes*

(16) In recent years AAMS has acted in a manner which has had a direct effect on the position in Italy of cigarettes manufactured in another Member State and then brought into Italy. Its actions may be summarised under the following headings:

(a) refusal by AAMS to increase the quantities imported and distributed under the distribution contract;

(b) measures taken by AAMS in respect of the 'magazzini' in order to favour its own brands to the detriment of competing brands;

(c) action taken by AAMS in respect of retailers in order to favour its own brands to the detriment of competing brands.

(17) As was stated (point 15(h), third and fourth indents), foreign firms may apply to AAMS for an increase in the quantities allowed onto the Italian market up to a maximum of 30 % of the monthly order. However, such an increase is subject to approval by AAMS.

On the basis of the documents listed in and appended to the statement of objections, it is clear that AAMS refused to give approval in several cases without adequate justification.

In 1995 AAMS refused on four occasions to allow increases requested by Reynolds of up to 30 % in quantities of Amadis cigarettes.

In April 1996 it refused to grant increases requested by Rothmans of up to 30 % in quantities of Lord cigarettes. In August 1996 it refused to grant increases of up to 30 % in the cigarette brands listed by Rothmans.

In August 1996 AAMS refused to grant increases of up to 30 % in quantities of Barclay, Barclay UL, Kim Menthol and Lucky Strike 10s cigarettes requested by BAT. The refusals caused stocks to fall below the levels provided for in the distribution contract.

(18) AAMS constantly coordinates and supervises the distribution activities of the 'magazzini'. According to AAMS, the purpose of the monitoring is to allow it to assess real market requirements and supply flows.

However, on several occasions, AAMS instructed the 'magazzini' to reduce orders for introduced cigarettes and/or increase orders for AAMS cigarettes, threatening them with proceedings if they failed to comply.

There are a number of examples of such behaviour:

— in January 1990 Reynolds informed AAMS that a number of warehouses had repeatedly cut supplies of certain brands of cigarettes intended for the 'magazzini',

— in October 1993 an inspectorate sent a letter to the 'magazzini' on its territory informing them that, as far as some foreign brands and, in certain cases, all foreign brands were concerned, it had identified 'excessive stocks in relation to market requirements'. It therefore instructed the local warehouse 'to specifically check requests for supplies in order to improve the balance of stocks and rationalise the management of allocations' granted to the 'magazzini',

— on an unspecified date another inspectorate sent a letter to the 'magazzini' on its territory with almost exactly the same content as that referred to above,

— in January 1994 an AAMS inspectorate sent a letter to the 'magazzini' on its territory requiring them 'to comply with the abovementioned sales quota ... in order to maintain if not improve, where possible, the market shares of AAMS brands'. The inspectorate also added that 'it goes without saying that an increase in

sales of foreign products must go hand in hand with a proportional increase in the sales of domestic products. Exceptional sales of non-domestic products will in any case have to be offset within the next two months so that the "magazzino" in question obtains at the end of 1994, in relation to the market share referred to above, the following result. . .',

— in March 1994 an inspectorate sent a letter to the 'magazzini' on its territory requesting them to take action to achieve the market shares (domestic products/foreign products) laid down by the inspectorate in an earlier letter,

— in February 1995 an AAMS inspectorate sent a letter to a 'magazzino' stating that a retailer had received a consignment of foreign cigarettes which appeared to be high in relation to the total consignment of all products and higher even than the quantities of consumer goods taken. The inspectorate therefore decided that, in future, foreign cigarettes would be supplied only in quantities corresponding to the percentage of sales achieved by the 'magazzino' in question,

— in July 1995 an AAMS inspectorate sent a letter to a 'magazzino' informing it that, according to the checks it had carried out, the 'magazzino' had on several occasions requested a warehouse to supply quantities of foreign products which were 'normally purchased in smaller quantities, based far more closely on sales',

— in November 1995 an AAMS inspectorate sent a letter to a 'magazzino' inviting it to reduce its stocks of foreign products 'to bring them to the level essential to overall operating requirements'.

(19) AAMS also constantly monitors the trading activities of retailers as it is kept informed, by means of a system of standardised forms, of the choices of the retailers in question concerning their cigarette orders.

Various examples show that AAMS has pursued its monitoring activities with a view to favouring the cigarettes it produces itself. To that end, it should be noted that:

— in March 1995 an AAMS inspectorate reprimanded several retailers for having obtained, as from November 1994, quantities of foreign cigarettes which were comparable to the monthly sales of virtually the whole sector. For that reason, it considered that those retailers were favouring the cigarettes in question and had infringed the principle of impartiality in the distribution of products,

— in February 1995 an AAMS inspectorate informed a retailer that 'the minimum quantity of monopoly goods which must be kept permanently in stock in the shop you manage . . . has been fixed',

— in February 1995 an AAMS inspectorate informed a retailer that it had ordered an abnormally high quantity of foreign cigarettes compared with its total orders and with the quantities of products having a higher turnover,

— in April 1996 an AAMS inspectorate suspended supplies of cigarettes to a retailer because the latter had not only failed to promote the sale of domestic cigarettes but had also culpably favoured the distribution of a competitor's cigarettes.

PART II

LEGAL ASSESSMENT

A. *ARTICLE 86 OF THE TREATY*

(20) Article 86 of the Treaty prohibits as incompatible with the common market any abuse by one or more undertakings of a dominant position within the common market, or in a substantial part of it, in so far as it may affect trade between Member States. In order to determine the applicability of Article 86 to the present case, it is necessary to decide whether the conditions set out in the Article have been met.

I. **The undertaking**

(21) AAMS is an entity engaged in economic activities that are both industrial (production of manufactured tobacco) and commercial (wholesale distributor of processed tobaccos) in nature. According to the case-law of the Court of Justice [7], it therefore constitutes an undertaking within the meaning of Articles 85 to 90 of the Treaty. The fact that AAMS does not have a separate legal personality from that of the State does not affect this conclusion.

[7] Case 118/85 of 16 June 1987, Commission v. Italy [1987] ECR, p. 2599.

Although the State has a single legal personality, Italian law recognises that each ministry and each autonomous administration has its own legal personality and, therefore, the capacity to be a party to legal proceedings independently *(legitimatio ad causam)*. In order to achieve its ends, an autonomous administration may make use of an administrative system which, although continuing to belong to the State, nevertheless enjoys considerable organisational autonomy (autonomy with regard to management, decision-making, assets and budget).

The fact that the Italian State has delegated certain public authority powers to AAMS does not mean that the Community competition rules do not apply to the behaviour of AAMS in its business activities (production of goods and supply of services) ([8]).

II. **The relevant markets**

(22) In order to determine whether AAMS holds a dominant position within the meaning of Article 86 of the Treaty, it is necessary to define the relevant market — that is, the economic sectors and geographic areas forming the background to an assessment of the economic strength of AAMS with regard to its competitors and customers.

1. *The markets for products and services*

(23) From the standpoint of products and services, it is necessary to distinguish three markets. The first consists of a group of products, whilst the other two correspond to the supply of services.

(24) First, there is the market for cigarettes produced in Italy or in other Member States of the Community for distribution and sale on Italian territory in order to satisfy smokers' demand (hereinafter referred to as the 'cigarette market'). There are various competing cigarette manufacturers on this market which endeavour to attract the largest possible number of consumers to their own brands and ensure that existing customers remain loyal.

(25) Secondly, there is the market for services relating to the distribution and wholesale of the abovementioned cigarettes (hereinafter referred to as the 'wholesale distribution market'). On this market, AAMS collects the cigarettes from the place of manufacture (or, in the case of cigarettes manufactured abroad, at the frontier), stores them in its own warehouses and distributes them to 'magazzini' or, through the warehouse outlets, to retailers. The 'magazzini' stock the cigarettes and sell them on to authorised retailers.

(26) Lastly, there is the market for services relating to the retailing of the cigarettes (hereinafter referred to as the 'retail distribution market'). There are some 58 000 authorised retailers of monopoly goods and 18 000 public outlets with a 'temporary licence'.

(27) Although the markets in question are separate, they are clearly highly interdependent, so that any action taken in one of them can have an appreciable effect on the others. This is particularly so with the cigarette market, as the competitiveness of economic operators is considerably influenced by the way in which their products are affected by activities in the wholesale and retail distribution markets.

2. *The geographic markets*

(28) From a geographic point of view, the markets outlined at points 24, 25 and 26 are located on Italian territory. In the light of the Commission notice on the definition of relevant market for the purposes of Community competition law ([9]), that territory must be regarded as separate from the territories of the other Member States for the following reasons:

— the preferences of Italian smokers are different from those of smokers in other Member States; see point 46 of the Commission notice. The brands produced by AAMS have a very high market share in Italy (42,1 %), although they are virtually non-existent in other Member States. In addition, the Philip Morris brands have a much higher market share in Italy than in the other Member States,

— the retail prices for cigarettes differ considerably from those in other Member States,

— in order to meet the requirements of the prevailing Italian regulations, all foreign manufacturers wishing to sell their products in Italy are required to label their cigarette packages with appropriate warnings (such as: 'tobacco seriously damages your health') in Italian. Such differences in the market should be taken into account even if they stem from legal texts (see point 50 of the Commission notice),

([8]) Judgment of the Court of Justice of 20 March 1985 in Case 41/83 Italy v. Commission [1985] ECR, p. 873.

([9]) OJ C 372, 9. 12. 1997, p. 5.

— there are no imports and/or exports by entities other than the producers (in other words, there are no parallel imports of cigarettes).

3. *Conclusions concerning the relevant markets*

(29) On the basis of the foregoing, it must be concluded that the relevant markets for the purposes of the present proceedings are as follows:

— the Italian market for cigarettes,

— the Italian wholesale distribution market,

— the Italian retail distribution market.

III. **The position of AAMS on the relevant markets**

1. *The position of AAMS on the Italian market for cigarettes*

(30) The Italian cigarette market consists of a duopoly made up of Philip Morris and AAMS (together, they hold some 94 % of the market), while other firms have only a marginal share of the market although they occupy stronger positions in other Member States. This situation has existed for at least 10 years. It should, however, be pointed out that, although the combined market share of the duopoly has remained virtually unchanged (over 90 % in any event), the share held by Philip Morris has risen consistently and markedly in the last few years whilst that of AAMS has fallen by roughly the same amount. Philip Morris is therefore the only firm to benefit from AAMS's regular loss of market share, the other firms having generally retained the same share.

2. *The position of AAMS on the Italian wholesale distribution market*

(31) With regard to the wholesale market, it should first be noted that Italy has adopted legislation liberalizing the import and wholesale distribution of cigarettes ([10]). As a result, any firm satisfying the requirements of the laws in force may engage in the wholesale distribution of cigarettes on Italian territory. A Community cigarette manufacturer could create its own distribution network or use the services of a wholesale distributor already operating in Italy. However, until now no producers have taken advantage of the possibility, preferring to continue to use the AAMS network to distribute their products in Italy. It must be borne in mind when analysing this choice that foreign firms have considerable financial difficulty in setting up a sufficiently extensive independent distribution network. Furthermore, no firms (other than AAMS) are at present engaged in wholesale distribution which could possibly be used for such activities, nor is the economic climate likely to encourage Italian firms to seize the opportunities afforded by the rules in force in order to enter the market. Lastly, there are the very specific characteristics of the Italian distribution system in the cigarette sector (very strict control by AAMS of the activities of the 'magazzini' and retailers, the deeply ingrained habit of the 'magazzini' and retailers of having AAMS as their sole commercial interlocutor, etc.). It must therefore be concluded that foreign manufacturers have not had (and still do not have) a viable alternative enabling them to choose differently and that, therefore, AAMS is a 'mandatory partner' for such firms.

AAMS is thus the only operator present on the Italian market for the wholesale distribution of cigarettes and it therefore has a *de facto* monopoly.

In the course of these proceedings, AAMS argued that since 1 January 1993 foreign firms have been able to entrust the wholesale distribution of cigarettes to a number of traders with bonded warehouses currently used to market other products liable to excise duty (and are therefore subject to a similar administrative and accounting regime as cigarettes) ([11]).

In considering these arguments, it must be borne in mind that bonded warehouse operators wishing to distribute cigarettes under the relevant legislation would encounter insurmountable financial obstacles. First and foremost, Italian regulations require manufactured tobaccos to be kept on separate premises from other bonded goods (such as alcohol), and this would entail substantial investment by the economic operators concerned.

([10]) Article 1 of Law No 724/1975.

([11]) The Decree Law of 31 December 1992, converted into Law No 427 of 29 October 1993, transposes into Italian law Council Directive 92/12/EEC on the intra-Community movement of products subject to excise duty (OJ L 76, 23. 3. 1992, p. 1), as last amended by Directive 96/99/EC (OJ L 8, 11. 1. 1997, p. 12).

Furthermore, the potential purchasers of cigarettes (essentially the retailers) are very different from the customers for other excise goods (such as retailers in the food distribution sector, in respect of alcohol). This would involve setting up a new transport and distribution structure without the chance to benefit from operational synergies with the existing distribution structure.

Finally, it should be borne in mind that the market share held by foreign manufacturers (excluding Philip Morris, which is tied to AAMS by licensing contracts) is extremely small (about 7 %) and does not, therefore, provide a sufficient financial incentive for firms wishing to compete against AAMS in the wholesale distribution of tobacco. It is clear that it would not be in the interests of retailers to obtain supplies from a different wholesaler if the latter could supply them only with a small proportion of the cigarettes they required.

It must be concluded from the foregoing that AAMS holds a dominant position within the meaning of Article 86 of the Treaty on the Italian market for the wholesale distribution of cigarettes.

3. *The position of AAMS on the Italian retail distribution market*

(32) With regard to the retail market, the Italian State has prohibited AAMS from engaging in the direct retailing of cigarettes. On the other hand, AAMS retains sole administrative authority to issue the licences to operate as a retailer. The licences do not, however, constitute a business activity because:

— they represent an exercise of public authority consisting in the issue of administrative acts in the form of concessions granting authorisation to engage in the retailing of cigarettes,

— the fact that retail sales are subject to the issue of licences by AAMS is not sufficient evidence that the latter exercises economic control over retailers. As a result, AAMS does not exercise *de facto* control over retailers such as would deprive them of their independence on the market. Retailers are therefore independent firms in relation to AAMS, both legally and commercially, and compete against each other.

It must therefore be concluded that AAMS is not present on the market for retail sales of cigarettes ([12]).

IV. **Abuses of a dominant position**

(33) The Court of Justice has consistently held ([13]) that the concept of abuse is an objective concept relating to the behaviour of an undertaking in a dominant position which is such as to influence the structure of a market where, as a result of the very presence of the undertaking in question, the degree of competition is weakened and which, through recourse to methods different from those which condition normal competition in products or services on the basis of the transactions of commercial operators, has the effect of hindering the maintenance of the degree of competition still existing in the market or the growth of that competition.

1. *The distribution contracts*

(34) As is stated at paragraph 31, AAMS holds a dominant position on the market for the wholesale distribution of cigarettes, where it is the only operator present. As a result, foreign manufacturers have invariably decided to use AAMS to distribute their cigarettes in Italy.

In view of the factors described in point 31 above, it would be reasonable to conclude that the decision of the foreign firms to use AAMS to distribute their cigarettes in Italy and to sign a distribution contract to that end is based on understandable economic and commercial reasons.

However, scrutiny of the current distribution contract reveals that some clauses give AAMS an actual right of control and, whenever it considers it expedient, a right to intervene in the many choices facing a foreign firm which must be regarded as essential to the firm's competitive freedom. On the basis of the clauses in question, AAMS is able to limit the competitive initiatives of foreign firms on the Italian market and thus protect the sale of its own brands.

The clauses were imposed by AAMS since it unilaterally drafted the text of the distribution contract: the foreign firms had the choice of signing it, as drafted by AAMS, or dispensing with the latter's services for distributing their products in Italy. In view of their very close dependence on AAMS, the foreign firms were compelled to accept the clauses imposed by AAMS in full, after expressing their dissatisfaction.

([12]) See the judgment of 14 December 1995 in Case C-387/93 Banchero [1995] ECR I, p. 4663.
([13]) See the judgment of 13 February 1979 in Case 85/76 Hoffmann-La Roche v. Commission [1979] ECR, p. 461.

It can therefore be concluded that AAMS exploited its dominant position on the market for the wholesale distribution of cigarettes in order to incorporate in the distribution contract clauses allowing it to control and even veto the competitive initiatives of the foreign firms, in order to protect its own sales.

1.1. The clauses concerning the introduction of new cigarette brands onto the market

1.1.1. The clause relating to the time limit for the introduction of new cigarette brands onto the market

(35) Under the third subparagraph of Article 1 of the distribution contract, AAMS allows foreign firms to introduce new brands twice a year.

The clause limits the opportunities for a foreign firm to launch new cigarette brands on the Italian market at the moment it considers best. It must be borne in mind that the seasons have a considerable influence on certain brands of cigarettes. It may therefore genuinely be in the interests of the foreign firm to introduce a brand on a given date without being compelled to wait until AAMS has decided to rule on the matter in accordance with the abovementioned provision. In addition, if a manufacturer wishes to launch a new brand simultaneously throughout the Community, the delayed introduction in Italy will compel it, for no reason whatsoever, to modify its strategy and may harm its competitiveness.

It must therefore be concluded that the imposition of the clause limiting the introduction of new brands onto the Italian market to twice a year restricts the competitiveness of the foreign firm and thus constitutes an abuse of a dominant position within the meaning of Article 86 of the Treaty.

1.1.2. The clause relating to the maximum quantities of new cigarette brands allowed on the market

(36) The fifth paragraph of Appendix B of the distribution contract provides that the quantities of new brands may not exceed 5 000 kg, while the sixth paragraph of the Appendix provides that, in the first year, orders from AAMS must be the same as in the preceding month.

It should be noted that a producer must be free to decide the conditions and arrangements for the launch of a new product, including the quantity to be marketed at the time of the launch. The relevant provision of the contract deprives the foreign firm of this facility.

(37) In addition, the quantity in question is totally inadequate in relation to the requirements for launching a new product in Italy. Since the minimum order that can be placed by a retailer is one carton, only one third of retailers (or 25 000 out of 75 000 retailers) will be able to obtain the new product at the time of the launch. However, AAMS cigarettes and those manufactured under licence are not subject to the abovementioned quantitative ceiling ([14]). As a result, the cigarettes of foreign firms are discriminated against, compared with AAMS brands, for no valid reason ([15]).

In fact, the purpose of such a provision is to impede the marketing of new foreign cigarettes or, at the very least, to reduce their impact on the market. This affects the competitiveness of the foreign firm, as the clause arbitrarily fixes at a very low level the quantities that may be marketed when a new product is launched.

Such a provision must be regarded as having a particularly restrictive effect in the event of a foreign firm deciding to launch a new version (such as 'light' or 'ultra light') of a widely marketed brand, since it is likely in such a case that consumer demand will be strong.

For these reasons it must be concluded that the provision limiting the quantities of new products to be placed on the market at the time of the launch and in the following year constitutes a serious restriction of the competitiveness of the foreign firm and is accordingly an abuse within the meaning of Article 86 of the Treaty.

1.2. The clauses relating to the monthly quantities of cigarettes allowed on the market

1.2.1. The clause relating to the maximum monthly quantities of cigarettes allowed on the market

(38) The second paragraph of Appendix B of the distribution contract provides that the quantities of cigarettes of the foreign firm to be marketed in Italy must be commensurate with the quantities sold during the previous month.

([14]) In the course of the proceedings, examples were provided of recent launches of new brands by AAMS: in June 1996, the first month of the launch, AAMS sold 33 217 kilograms of MS E. Slim cigarettes and, in July 1996, also in the first month, it sold 35 543 kilograms of MS Personal cigarettes. These quantities are some seven times greater than the maximum allowed for foreign cigarettes.

([15]) It was stressed in the course of the proceedings that AAMS cigarettes are automatically distributed, from the first month of being launched, to all 'magazzini' and retailers.

The clause restricts the freedom of foreign firms to decide on the volume of goods to be sold. The foreign firm is thus deprived of the chance of competing on the Italian market and taking full advantage of the opportunities available. It must therefore be concluded that the clause is designed to protect the market position of AAMS cigarettes and is indeed capable of doing so.

(39) The clause in question does not appear to be justified by any objective need to protect any legitimate financial and/or commercial interests of AAMS.

First, AAMS has distribution capacities of some 102 million kilograms of cigarettes a year, which is considerably in excess of actual market requirements in Italy (about 90 million kilograms). As a result, it has far too much capacity, allowing it to respond favourably to any requests from foreign firms to increase the quantities distributed without strengthening its distribution structures.

Furthermore, the clause in question does not appear to be justified by any need for the quantities of foreign cigarettes distributed by AAMS to correspond to actual market demand, as was argued by AAMS in the course of the proceedings. It is not in the interests of foreign firms to make available through the AAMS distribution network more cigarettes than the market can actually absorb since, after a given time, they are required to withdraw all unsold cigarettes stocked in AAMS warehouses at their own expense (Article 10 of the distribution contract). In addition, if cigarettes remain in storage in the warehouses for a long time, the foreign firm must replace them with other, more recent products.

Lastly, the cigarettes produced by AAMS, whether as its own brand or under licence, are not subject to any comparable limitation and hence enjoy a considerable competitive edge compared with cigarettes manufactured abroad.

(40) For these reasons it must be concluded that the imposition of the said clause constitutes an abuse of a dominant position within the meaning of Article 86 of the EC Treaty, despite the fact that it allows for possible and partial derogation.

1.2.2. The clause relating to the increase in the monthly quantities of cigarettes allowed on the market

(41) The fifth subparagraph of Article 2 of the distribution contract provides that the foreign firm may ask AAMS to increase the quantities of cigarettes to be placed on the Italian market. This possibility, however, is subject to a threefold limitation. First, the agreement of AAMS is required. Second, any increases must not exceed 30 % of the 'monthly order allowed' (which must itself be commensurate with sales in the previous months). Third, AAMS approval of such increases gives rise to an obligation on the part of the foreign firm to pay a higher distribution fee calculated not on the basis of the 'additional' quantities, but on the basis of the entire quantity supplied (sixth subparagraph of Article 2 of the distribution contract).

These provisions seriously jeopardise the competitive freedom of the foreign firms. A manufacturer must be free to determine the quantities of products to be marketed. The need for AAMS approval in order to increase quantities clearly has the object of restricting the sales of foreign cigarettes. Limiting increases to 30 % of the 'monthly order allowed' seriously jeopardises the competitiveness of the firm concerned by preventing it from responding in full to existing demand on the Italian market. This has particularly serious effects in the case of cigarette sales, which are strongly affected by the seasons. Thus, for example, a foreign firm might be unable to meet the demand for a particularly popular brand of cigarettes during the summer months and might have to content itself with increasing the average quantities sold in off peak months by 30 %. Lastly, the obligation to pay AAMS an additional amount calculated on the basis of total quantities in the event of an increase in quantities does not appear to be in any way justified. The distribution fee is structured in such a way that its amount gradually diminishes as the quantities sold increase (thus the fee for annual sales in the 1 to 3 million kilogram range is ITL 3 400 per kilogram, whereas the fee for sales in excess of 3 million kg is ITL 2 900 per kilogram). Accordingly, an increase in quantities sold should lead to a reduction in the distribution fee and not to an increase as provided for in the contract.

It thus seems clear both that the sole aim of the provisions is to prevent foreign firms from increasing in response to market demand the quantities sold on the Italian market, and that the provisions are capable of achieving that aim.

(42) According to AAMS, the clause in question is justified in the first instance by the need to avoid excessive financial risk in the form of the payment made for quantities of foreign cigarettes exceeding market requirements. AAMS points out that the distribution contract requires it, no later than the 15th day of each month, to inform the foreign firm of the quantities of cigarettes that have left its warehouses and, within 25 days of the date of the receipt of the invoice from the foreign firm, to issue the order of payment. In practice, therefore, AAMS is required under the contract to arrange payment within some 50 days of removal of the foreign cigarettes from the warehouses. AAMS also claims that, in view of the fact it is paid only when the retailer purchases the cigarettes from the warehouse, it runs the risk of having to advance sums for a considerable period.

AAMS has not provided any information concerning the average time spent by cigarette stocks in the warehouses; it has referred only to a general risk of excessive periods of storage ([16]). On the other hand, Rothmans stated at the hearings that the average stock turnover rate was 20 days and that, therefore, AAMS would not in general incur any financial exposure but would, on the contrary, benefit from a financial advantage of 30 days (as it waits 20 days to receive payment and about 50 to pay).

It can also be assumed that the 'magazzini' operate a rational commercial policy and do not therefore usually acquire foreign cigarettes liable to stay in stock for a long time. On the contrary, it can reasonably be assumed that the 'magazzini' purchase their stock from the warehouses on the basis of actual demand from retailers, thus generally ruling out the risk of excessive storage periods (and the associated financial risk for AAMS).

([16]) AAMS states only that 'products may remain in stock for a long time in the distribution circuit (i.e. in the warehouses themselves) before reaching the retailer, in other words before the moment at which [AAMS] receives from the tobacco retailers the price for the sale of the products'.

(43) Secondly, AAMS claims that the clause in question is justified by the need to avoid a number of negative economic consequences. It claims that the fact that a foreign firm withdraws at its own expense cigarettes which have remained too long in warehouse storage is not sufficient to prevent AAMS from having to bear certain financial costs, e.g. expenditure on rail transport from the Italian frontier to the warehouse, for unloading the wagons, for storage and for stock management. However, AAMS has not given any figures on the extent of the financial charges.

The clause appears to be disproportionate to the objective. The parties could instead operate under other non-restrictive measures designed to take account of actual expenditure incurred by AAMS on cigarettes which have remained unsold in its warehouses and have therefore been removed by the foreign firm.

Lastly, the parties could incorporate into the contract similar measures aimed at reimbursing actual expenditure incurred by AAMS in connection with unsold cigarettes in 'magazzini' (a hypothetical situation that is unlikely to occur frequently, for the reasons stated in point 42).

(44) It is clear from the foregoing that the relevant clause in the distribution contract concerning the possibility of increasing the quantities of foreign cigarettes distributed on the Italian market considerably restricts the competitive scope of foreign manufacturers and, therefore, constitutes an abuse of a dominant position under Article 86 of the Treaty.

1.3. The clauses concerning packaging and quality control

1.3.1. The clause concerning the printing of the word 'Monital' on the cigarettes

(45) Article 4 of the distribution contract requires the foreign firm to print the word 'Monital' (an abbreviation of 'Italian monopolies') on each cigarette intended for sale on the Italian market.

The obligation does not appear to be justified by the need to distinguish legally marketed cigarettes from contraband cigarettes, since it would suffice simply to affix to each packet of cigarettes the mark provided for by Article 4 of Law No 724/975, as cigarettes cannot be sold singly.

In addition, the obligation is a means of promoting AAMS through a competing product. Lastly, the obligation may create doubt on the part of consumers as to the identity of the cigarette manufacturer in question.

It must therefore be concluded that the imposition of the clause in question constitutes an abuse of a dominant position under Article 86 of the Treaty.

1.3.2. The clause relating to quality control

(46) The quality controls provided for in Article 5 of the distribution contract cannot be regarded as necessary to enforce compliance with the rules in force; as a result, their imposition by AAMS is not justified. Consequently, AAMS cannot require a foreign firm to pay an annual amount for each packaging of each brand as payment for such inspections and analyses.

Article 11 of the distribution contract requires the foreign firm to supply to AAMS products that do not conflict with the relevant legislation in force in Italy. The legislation gives effect to Council Directive 89/662/EEC [17], as amended by Directive 92/41/EEC [18] on the labelling of tobacco products, and Council Directive 90/239/EEC [19] on the maximum tar yield of cigarettes, which aim *inter alia* at eliminating obstacles to intra-Community trade and hence the need for controls.

Furthermore, such controls cannot be justified by the need to protect AAMS from possible liability for having distributed cigarettes that fail to conform to the rules in force. Under Italian Law No 224 of 24 May 1988 giving effect to Council Directive 85/374/EEC [20] on liability for defective products, a distributor is liable only if the manufacturer cannot be identified.

It thus seems that, in practice, the controls had the effect of unjustifiably delaying the launch of new brands of foreign cigarettes on the Italian market, as no new brands can be marketed until AAMS has completed its checks.

The clause requiring the foreign firm to allow AAMS to check its products and pay a fixed amount in that connection is therefore an abuse of a dominant position under Article 86 of the Treaty.

2. *Unilateral action with regard to imported cigarettes*

2.1. Refusal to authorise increases in cigarette imports

(47) AAMS on several occasions refused to allow foreign firms to increase quantities of imported cigarettes (see point 17). Its behaviour had the effect of preventing foreign firms from marketing in Italy the quantities of cigarettes they considered desirable and hence weakened their competitiveness.

Under the distribution contract, AAMS has the right to reject requests for increases of more than 30 % in the monthly order allowed, whilst below that threshold (that is, for increases of 0,1 % to 30 %) it can approve or reject requests for increases. The AAMS refusals referred to above concern requests for increases complying with the contract (see point 17).

In its observations on the statement of objections, AAMS stated that the abovementioned refusals were not unjustified because: (a) as regards Reynolds, on 30 June of 1983, 1984, 1985 and 1986, in relation to a market share of 1,9 %, 1,4 %, 1,5 % and 1,6 % respectively, stocks in AAMS warehouses amounted to 3,47 %, 1,78 %, 1,60 % and 1,79 %; (b) as regards Rothmans, on 30 June of 1983, 1984, 1985 and 1986, in relation to a market share of 2,4 %, 2,1 %, 1,9 % and 1,8 % respectively, stocks in AAMS warehouses were 3,7 %, 2,87 %, 2,95 % and 3,06 % of total cigarettes in AAMS warehouses.

The comparison between the market shares of the foreign firm and the percentage of that firm's products in relation to total stocks in the warehouses is entirely without relevance as a justification for the behaviour of AAMS. A valid point would have been to check whether the stocks in AAMS warehouses could satisfy actual market demand for a specific brand of cigarette (and not for all the brands of a given foreign firm) at a specific time of year. AAMS has not provided any data to allow such an assessment to be made.

[17] OJ L 359, 8. 12. 1989, p. 1.
[18] OJ L 151, 11. 6. 1992, p. 30.
[19] OJ L 137, 30. 5. 1990, p. 36.
[20] OJ L 210, 7. 8. 1985, p. 29.

It is worth noting, however, that the distribution contract itself provides that cigarettes stocks (of a given brand with monthly sales of under 500 000 kilograms) in warehouses must be equal to double the average monthly sales (of that brand) in the previous year (Appendix B of the distribution contract). Such a clause (not called into question by this Decision) is consistent with normal commercial policy as regards stock management and could serve as a parameter for assessing requests for increases presented by foreign manufacturers.

The data provided by AAMS do not distinguish between the various brands of each foreign firm. However, the data for all brands show that warehouse stocks were lower than those provided for in the distribution contract and that consequently the requests for increases were justified.

Accordingly, the refusal to grant the increases requested by the foreign firms constitutes an abuse of a dominant position under Article 86 of the Treaty.

2.2. Behaviour with regard to the 'magazzini'

(48) AAMS supervises the activities of the 'magazzini' through its own inspectorates. On various occasions, AAMS inspectors did not confine themselves to exercising the supervisory powers conferred on AAMS by the legislation in force but took action aimed specifically at favouring domestic cigarettes and limiting sales of imported cigarettes (see point 18). As such behaviour does not form part of the public supervisory powers entrusted to AAMS, it constitutes an action of an undertaking. The fact that the behaviour constitutes an administrative act would tend, if anything, to aggravate the abuse.

(49) The restrictive effect of such behaviour was particularly severe in the cases where AAMS required 'magazzini' to comply with effective sales quotas applicable both to AAMS cigarettes and to foreign cigarettes.

Such behaviour is not required by any current legislation or by any contractual provision. On the contrary, it is clearly in breach of Article 12 of the distribution contract, which establishes the principle of an impartial distribution system.

(50) Accordingly, such behaviour in respect of 'magazzini' constitutes an abuse of a dominant position under Article 86 of the Treaty.

2.3. Behaviour with regard to retailers

(51) AAMS supervises the activities of retailers through its own inspectors. On various occasions, AAMS inspectors did not confine themselves to exercising the powers conferred on AAMS by the legislation in force but took action aimed specifically at favouring AAMS cigarettes and limiting sales of imported cigarettes (see point 19). On those occasions, the AAMS inspectors did not confine themselves to their power to supervise retailers ([21]) but acted with the sole aim of specifically favouring the business activities of AAMS to the detriment of its competitors. Such behaviour is manifestly unrelated to the public powers conferred on AAMS and therefore constitutes an act of an undertaking aimed at increasing the sales of AAMS cigarettes in relation to those of foreign firms. The fact that the behaviour in question is in the form of an administrative act does not alter that conclusion.

(52) The anti-competitive effect of such behaviour is particularly severe in the case of AAMS, which required retailers to purchase minimum quantities of domestic cigarettes or, without reason, ruled that the quantities of foreign cigarettes requested by retailers were excessive.

Such behaviour is not required by any rules currently in force or by any contract provisions. On the contrary, it is clearly in breach of Article 12 of the distribution contract, which establishes the principle of an impartial distribution system.

(53) Accordingly, such behaviour with regard to retailers constitutes an abuse of a dominant position within the meaning of Article 86 of the Treaty.

([21]) According to AAMS, the supervisory power 'is a power consisting exclusively in checking that the activity of retailing complies with the requirement of the act granting such powers'.

3. *Conclusions on the abuses of dominant position*

(54) It is clear from the foregoing that AAMS, benefiting from its dominant position on the market for the wholesale distribution of cigarettes, implemented a number of abusive measures aimed at protecting and strengthening its position on the market for cigarettes, having recourse to means other than those on which normal competition is based.

V. **The effect on trade between Member States**

(55) The behaviour referred to above is specifically aimed at hampering the introduction, distribution and sale in Italy of cigarettes manufactured in other Member States and therefore clearly satisfies the requirements relating to trade between Member States.

B. ***ARTICLE 3 OF REGULATION No 17***

(56) Article 3 of Regulation No 17 provides that, where the Commission finds that there is an infringement of Article 86 of the Treaty, it may require the undertakings concerned to bring such infringement to an end.

There are therefore grounds for requiring AAMS to put an end to the infringements that are continuing and to take the necessary steps to prevent the continuation or repetition of the infringements in question ([22]).

I. **Termination of the ongoing infringements**

(57) In order to determine which infringements are still taking place, it is necessary to consider the measures taken by AAMS while the case was under examination and after the initiation of proceedings.

AAMS informed the Commission by letter dated 10 October 1997 of an amendment to the model distribution contract consisting in the deletion of the clause limiting the possibility of introducing new cigarette brands to twice a year (third paragraph of Article 1 of the contract — see point 15(b) of this Decision) and the clause requiring the word 'Monital' to be printed on the cigarettes (first paragraph of Article 4 of the contract — see point 15(j) of this Decision). The foreign firms were informed of the amendment on 22 September 1997.

(58) On the basis of the foregoing, AAMS should modify the other abusive clauses of the distribution contract, namely, the clauses referred to in point 15(f), (h) and (k), in order to eliminate the abusive aspects referred to in points 36 to 44 and point 46.

II. **Measures to prevent the continuation and repetition of the infringements**

(59) In order to allow the Commission to ascertain whether the infringement has been terminated and cannot be repeated, AAMS should be asked to communicate to the Commission the new distribution contracts, amended in accordance with the information referred to in point 58.

(60) With regard to the unilateral behaviour referred to in point 17, it is necessary to require AAMS to refrain from taking, in respect of foreign firms, measures having an equivalent effect to such behaviour.

Accordingly, for a period of three years from the date of notification of this Decision, AAMS should present to the Commission, within two months of the end of the calendar year, a report indicating for the preceding year the quantities of foreign cigarettes distributed by AAMS and any refusals (total or partial) on its part to distribute such cigarettes.

(61) As regards the unilateral behaviour referred to in points 18 and 19, it is necessary to take account of certain measures taken by AAMS during the examination phase of the case and following the initiation of proceedings.

First, in its letter of 25 July 1997, AAMS provided the Commission with a copy of the circular sent on 16 June 1997 by its executive board to all its inspectorates. In that letter, AAMS first invited all the inspectors 'to refrain from initiatives which may constitute an infringement of the principle of impartiality... both in respect of tobacco produced domestically and foreign tobacco'. In addition, AAMS prohibited 'all initiatives aimed in any way whatsoever at influencing retailers' requests, even by fixing in advance the level for stock turnover, a practice which is incompatible with the obligation

([22]) In its judgment of 6 March 1974 in Joined Cases 6 and 7/73 Commercial Solvents v. Commission ([1974] ECR, p. 223), the Court of Justice held that the Commission had discretionary power to order measures to ensure its decision was effective, by requiring undertakings to do certain acts (paragraph 45).

on retailers to base their orders on consumer demand'. Lastly, AAMS required all its inspectorates to inform the AAMS executive board of all measures 'concerning the marketing of manufactured tobacco which they intended to notify to the "magazzini" and the retailers of monopoly goods'.

Secondly, it should be noted that, by letters dated 25 July and 10 October 1997, AAMS informed the Commission that, by circular of 18 April 1997, it had abolished the obligation on retailers to contribute to the development of domestic tobacco sales previously provided for in Article 15 of the general terms and conditions applicable to contracts for State monopoly goods shops ([23]). The obligation was replaced by the following provision: 'retailers shall ensure that they observe impartiality in the sale of tobacco, whether domestic or foreign, and in their display and presentation, which must comply with normal commercial practice' (Article 14(4) of the new terms and conditions). The new provision was referred to in the abovementioned circular of 16 June 1997. By circular of 24 September 1997, the AAMS executive board sent to all its inspectorates the text of the new terms and conditions for public contracts to operate monopoly goods shops, comprising several amendments, including the one referred to above. The circular also provides that 'to ensure that all retailers of monopoly goods are informed of the new text appended, the inspectors will make as many copies as there are outlets supplied by the "magazzini" within their jurisdiction, and will require the said "magazzini" to give a copy to each retailer and obtain acknowledgment of receipt'. Furthermore, in another circular dated 24 September 1997, AAMS provided the inspectorates with the text of the new terms and conditions for public contracts to manage 'magazzini' for the sale of monopoly goods ([24]). The new text abolishes the obligation to promote domestic tobacco previously imposed on the 'magazzini' and enshrines the principle of impartial distribution. The circular also requires inspectors to send the new text to the 'magazzini' located on their territory.

In view of the foregoing, it does not seem necessary to impose specific measures on AAMS to ensure that the abuses referred to in points 18 and 19 of this Decision are not repeated.

([23]) The terms and conditions for public contracts to manage State monopoly goods shops are State measures and are not covered by these proceedings. However, the amendment to the specifications is taken into account here as relevant to the assessment of the need to impose specific measures on AAMS to ensure that the abuses in question are not repeated.

([24]) See footnote 23.

C. ***ARTICLE 15 OF REGULATION No 17***

(62) Where, intentionally or negligently, undertakings infringe Article 86 of the Treaty, the Commission may, under Article 15(2) of Regulation No 17, impose fines on them of from ECU 1 000 to ECU 1 million, or a sum in excess thereof but not exceeding 10 % of the turnover in the preceding business year of the undertaking in question. In order to determine the amount of the fine, regard is had both to the gravity and the duration of the infringement.

The infringement was perpetrated by AAMS, which, whilst not having a legal personality as such, is an undertaking within the meaning of Article 86 of the Treaty. AAMS also enjoys organisational autonomy (in particular as regards asset management) and has its own capacity *ad litem* (see point 21).

In this case, it is appropriate to impose a fine on AAMS in view of its behaviour. In order to determine the amount of the fine, account should be taken of the gravity and duration of the infringement and of any aggravating and/or attenuating circumstances.

I. **Gravity of the infringement**

(63) In determining the gravity of the infringement, consideration must be given to the nature of the infringement, its actual impact on the market and the extent of the relevant geographic market.

1. *Nature of the infringement*

(64) The infringements of Article 86 of the Treaty committed by AAMS form part of a policy specifically aimed at obstructing, systematically and severely, access to the Italian cigarette market for competing producers, and at restricting their opportunities for increasing their share of that market.

(65) The breaches of Article 86 of the Treaty were committed intentionally by AAMS, which was specifically aiming, through such behaviour, severely to hinder access to the Italian cigarette market for competing producers.

It should be pointed out in this connection that, on several occasions, certain foreign firms expressly drew the attention of AAMS to the fact that many clauses of the distribution contract appeared to be incompatible with the Community competition rules.

2. *Actual impact on the market*

(66) In assessing the actual impact which the infringement has had on the market, two factors must be taken into consideration: the existence of restrictive State measures and the evolution of the Italian cigarette market.

(67) First, the difficulties encountered by foreign firms in gaining access to (and developing their activities on) the Italian market must to a large extent be ascribed to the measures adopted by the Italian State during the period concerned. It should be stressed here that:

— the Finance Ministry repeatedly omitted to adopt decrees adding new cigarette brands to the price list, despite being requested to do so by foreign firms (no decree adding foreign cigarette brands to the price list was adopted between 1992 and 1997), with the result that the new brands could not be placed on the Italian market ([25]). Such failure to act on the part of the State authorities meant that the clauses on the placing on the market of new cigarette brands (see point 15(c) and (f) of this Decision) were rendered inapplicable and without practical effect during the periods concerned,

— during the whole of the period in which the infringements were committed, retailers were required, under Article 15 of the general terms and conditions, to contribute to the development of domestic tobacco sales ([26]). The view should therefore be taken, here too, that the adverse effect of this State measure on the development of foreign cigarette sales partly neutralised the effect of the contractual clauses,

— up to August 1993, Italy had not brought its legislation into line with the Community rules on determination of the retail selling prices of imported manufactured tobacco ([27]). Before that date, Italian legislation had not allowed foreign firms freely to determine the retail selling prices of their cigarettes and was therefore a factor limiting the ability of those firms to compete. It was therefore also likely to hinder the development of sales of imported cigarettes on the Italian market, since foreign firms were denied the freedom to set the prices of their cigarettes in line with their own marketing strategies.

(68) Secondly, during the currency of the infringement, AAMS' market shares declined constantly and very considerably. Despite the existence of the infringement and of the above restrictive State measures, AAMS did not therefore succeed in reversing the downward trend in the sales of its own cigarettes on the Italian market. The infringement may, at the very most, have had the effect of slowing down a decline in AAMS' market share which could otherwise have been even more significant.

([25]) It should be noted here that Italian law requires, as an absolute precondition for placing a new brand of cigarettes on the Italian market, publication in the Official Gazette of the Italian Republic of a decree of the Minister for Finance adding the brand to certain schedules (Article 2 of Law No 825 of 13 July 1965 on the tax rules for products covered by the State monopoly, as amended by Article 27 of Decree-Law No 331 of 30 August 1993, converted by Law No 427 of 29 October 1993 (GURI No 225, 29.10.1993), and by Article 9 of Law No 76 of 7 March 1985. (GURI No 65, 16.3.1985)). The completion of this procedure is therefore to be regarded, to all intents and purposes, as a pre-condition to the placing on the market of new cigarette brands.

([26]) See point 61 and footnote 23.

([27]) Article 5 of Council Directive 72/464/EEC of 12 December 1972 on taxes other than turnover taxes which affect the consumption of manufactured tobacco (OJ L 303, 31.12.1972, p. 1). (This matter is currently governed by Article 9 of Council Directive 95/59/EC (OJ L 291, 6.12.1995, p. 40).) Up to August 1993, Italian legislation (Article 2 of Law 825/65) stipulated that 'the inclusion of each product subject to the State monopoly in the tariffs (...) and changes in that regard shall be effected by decree of the Minister for Finance in relation to the prices requested by suppliers for imported goods, after obtaining the opinion of the Administrative Board for State Monopolies, and in relation to the prices proposed by the said Board for other goods'. The Court of Justice of the European Communities declared that Italy had failed to fulfil its obligations under Article 5 of Directive 72/464/EEC by retaining legislation which did not expressly indicate and did not clearly entail an obligation on the part of the competent administrative authority to observe, under the conditions and within the limits laid down by the Directive, the principle that manufacturers and importers are free to determine the maximum prices of manufactured tobacco imported into Italy (judgment of 28 April 1993 in Case C-306/91 [1993] ECR I, p. 2133). In order to bring its legislation into line with that judgment, Italy adopted Decree-Law No 331/93, Article 27 of which, amending Article 2 of Law No 825/65, provides that 'retail selling prices and changes in those prices shall be established in line with the requests of manufacturers and importers'.

3. *Extent of the relevant geographic market*

(69) It should be borne in mind that the anti-competitive effects of the infringement are limited to a single Member State, Italy.

4. *Conclusion regarding the gravity of the infringement*

(70) In the light of the foregoing, the behaviour in question can be regarded, on the one hand, as constituting infringements of a nature and with a purpose that are markedly anti-competitive and, on the other hand, as having had effects on the market that are in practical terms relatively minor and limited to a single Member State.

In view of the concurrence of the above factors, it must be concluded that the behaviour in question constitutes a serious infringement.

(71) Since the amount of the fine must be determined, according to the gravity of the infringement, in such a way that it constitutes a sufficiently strong deterrent to any repetition of the infringement, an amount of ECU 3 000 000 is appropriate.

II. **Duration of the infringement**

(72) The current model distribution contracts came into effect on 1 January 1995 and are to expire on 31 December 1998. The abusive clauses in these contracts are identical in content to the corresponding clauses in the previous model distribution contracts, which were concluded at the beginning of 1985 and expired on 31 December 1993. The 1985 model distribution contracts in turn reproduced the corresponding clauses of the earlier model contracts (which are not, however, taken into consideration). On the basis of the information in the Commission's possession, the infringement appears to have been pursued for at least 13 years (namely since 1985).

Furthermore, the unilateral abusive behaviour (see points 16 to 19) extends over seven years (from 1990 to 1996).

(73) In the light of the foregoing, it is clear that the infringement has been in existence for a long time. It is therefore appropriate to increase the amount of the fine determined on the basis of the gravity of the infringement by 100 % (or ECU 3 000 000).

III. **Basic amount of the fine**

(74) In the light of the foregoing, the basic amount of the fine should be fixed at ECU 6 000 000.

IV. **Aggravating and attenuating circumstances**

(75) There are no aggravating or attenuating circumstances that would justify increasing or reducing the above basic amount.

V. **Amount of the fine**

(76) For the above reasons, the amount of the fine should be fixed at ECU 6 000 000.

HAS ADOPTED THIS DECISION:

Article 1

Taking advantage of its dominant position on the Italian market for the wholesale distribution of cigarettes, Amministrazione Autonoma dei Monopoli di Stato (hereinafter 'AAMS') has engaged in improper behaviour in order to protect its position on the Italian market for cigarettes, in breach of Article 86 of the EC Treaty, through the use of clauses compulsorily inserted in distribution contracts as set out in Article 2, and through unilateral practices as set out in Article 3.

Article 2

The compulsory clauses improperly inserted by AAMS in the distribution contracts are as follows:

(a) the clause relating to the time limit for the introduction of new cigarette brands onto the market (third paragraph of Article 1);

(b) the clause relating to the maximum quantities of cigarettes allowed on the market (Appendix B, fifth and sixth paragraph);

(c) the clause relating to the maximum monthly quantities of cigarettes allowed on the market (Appendix B, second paragraph);

(d) the clause relating to increases in the monthly quantities of cigarettes allowed on the market (fifth and sixth paragraph of Article 2);

(e) the clause relating to the printing of 'Monital' on the cigarettes (Article 4);

(f) the clause relating to inspection and analysis of the cigarettes (Article 5).

Article 3

The improper unilateral practices pursued by AAMS are as follows:

(a) refusal to authorise increases in the monthly quantities of foreign cigarette imports requested by foreign undertakings in conformity with the distribution contracts;

(b) behaviour with regard to 'magazzini' and retailers, designed to promote national cigarettes and to limit sales of foreign cigarettes.

Article 4

AAMS shall forthwith put an end to the infringements referred to in Articles 2 and 3, in so far as it has not already done so. In particular, AAMS shall amend the clauses of the distribution contracts referred to in Article 2 which are still in force, in such a way as to eliminate the abuses found by this Decision to have occurred. The new distribution contracts shall be submitted to the Commission.

Article 5

AAMS shall refrain from continuing or repeating the behaviour referred to in Articles 2 and 3 and from all activities having an equivalent effect.

To that end, AAMS shall, for a period of three years from the date of notification of this Decision, forward to the Commission within two months of the end of each calendar year, a report on the preceding year describing the quantities of foreign cigarettes distributed by AAMS as well as any refusal (total or partial) to distribute such cigarettes.

Article 6

A fine of ECU 6 000 000 is hereby imposed on AAMS in respect of the abuses referred to in Articles 2 and 3.

The above fine shall be paid, in ecus, within three months of notification of this Decision. The amount shall be transferred in ecus to the account of the Commission of the European Communities No 310-0933000-43, Banque Bruxelles Lambert, Agence Européenne, 5 Rond Point Schuman, B-1040 Brussels.

On expiry of that period, interest shall automatically be payable at the rate charged by the European Central Bank on the first working day of the month in which this Decision was adopted, plus 3,5 percentage points, that is to say 7,75 %.

Article 7

This Decision is addressed to Amministrazione Autonoma dei Monopoli di Stato, Piazza Mastai, 11, I-00153 Rome.

This Decision shall be enforceable pursuant to Article 192 of the Treaty.

Done at Brussels, 17 June 1998.

For the Commission

Karel VAN MIERT

Member of the Commission