

Chapter 3: Some outstanding issues from the European Commission's Guidance on Article 102: Not-so-faint echoes of Ordoliberalism

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Monopolisation is treated rather differently on either side of the Atlantic. You don't need to be an international antitrust expert to sense that. The press is rather hard to miss:

- EC takes on Microsoft where US authorities failed¹
- *Reviving Old Fight, Regulators Accuse Software Giant of Harming Competitors by 'Tying' Web Browser to Windows*²
- MSFT: EU would force users to pick browser³
- Is Microsoft ruling an example of European protectionism?⁴

The last headline, at least, is odd. The European Commission isn't using competition law to protect European companies from American rivals. The transatlantic divide is not caused by protectionism, but by different views on how antitrust should protect the market. This chapter examines how that fundamental difference still motivates much of European Commission policy with respect to the enforcement of Article 102.

My reference point will be the recent Guidance on Article 102 EC⁵ issued by DG Competition, European Commission in December 2008, and finalised in Spring 2009.⁶

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¹Warwick Ashford, <<http://www.computerweekly.com/Articles/2009/01/19/234297/ec-takes-on-microsoft-where-us-authorities-failed.htm>>

²<http://online.wsj.com/article/SB123213711567091269.html?mod=googlenews_ws>

³Richard Koman, <<http://government.zdnet.com/?p=4306>>

⁴<<http://www.europeanvoice.com/article/imported/is-microsoft-ruling-an-example-of-european-protectionism-/63776.aspx>>

This Guidance reveals the extent to which European competition law in this area has moved towards something with which American advisors will be more familiar: the maximisation of consumer welfare.

The European Commission has made some great strides towards limiting enforcement activity to situations where consumer harm is likely. DG Competition, in particular, must be commended for this movement. To my mind, however, more needs to be done. European law on abuse of dominance still operates within a legal and political framework that asks only whether a dominant firm is excluding its rivals. The case law simply does not allow much room for a new focus on economic effects and proof of likely harm to consumers. The politics of EU policymaking explain the law: some powerful European Member States still cling to the theories of harm that don't ask that second stage question of whether foreclosure will be likely to harm consumer welfare.⁷ As a result, European competition law on abuse is still guided by an 'Ordoliberal' concern with promoting rivalry and this acts as a proxy for consumer benefits.⁸ The Ordoliberal concern in question does not involve over-reliance on formalistic prohibitions of conduct by 'category'; Europe has largely moved on from that. It does require economic evidence to identify whether conduct is harmful. Its focus however is not on proving likely harm to *consumers*. Commission policy is still focussed on proving that dominant firm conduct may harm *rivals* - this in turn is assumed to reduce the competitive constraints on the dominant firm and thereby to allow it to harm consumers. The Ordoliberal theory of harm is obvious; it is just difficult to prove – and the Commission doesn't propose to try. European case law is even clearer: the Commission doesn't have to prove that consumer harm is likely – such can be assumed.⁹

⁵ European Commission, *Guidance on the Commission's Enforcement Priorities in Applying Article 82 EC Treaty to Abusive Exclusionary Conduct by Dominant Undertakings*, Brussels, 9 February 2009, COM(2009)864final, (O.J.E.U. C 83, 7 April 2009) (hereafter the 'Guidance').

⁶ See also Chapter 7 by Art and Ibáñez Colomo in this Volume for an evaluation of the Guidance Paper.

⁷ P Marsden, 'A Bundeskartellamt/Competition Law Forum Debate on Reform of Article 82: A "Dialectic" on Competing Approaches' (2006) in *European Competition Journal* 211 <http://www.biiicl.org/files/1183_bkarta-clf82.pdf>

⁸ On Ordoliberalism, see generally W Möschel, 'The Proper Scope of Government Viewed from an Ordoliberal Perspective: The Example of Competition Policy' [2001] 157 in *Journal of Institutional and Theoretical Economics* 3; and D J Gerber, 'Constitutionalizing the Economy: German Neo-Liberalism, Competition Law and the "New Europe"' [1994] 42 in *American Journal of Comparative Law* 25; and W Möschel, 'Competition Policy from an Ordo Point of View' in A Peacock and H Willgerodt (eds), *German Neo-Liberals and the Social Market Economics* (MacMillan, 1989).

⁹ See *British Airways*, n. 12 below

This paper will examine the assumptions that the European Commission still makes with respect to

- first, the existence of dominance, and
- second, the motivating theory of harm (‘anticompetitive foreclosure’).

In particular, it will examine how these assumptions are evident in the Guidance’s approach to various abuses, including exclusive purchasing, rebates, bundling and tying, predation, and refusal to deal.

European Assumptions of Harm

The Commission’s Guidance reveals that the great strides it has made towards a introducing a consumer welfare-based test of harm from abuse of dominance are still hampered by two key assumptions.

The first assumption is that if a firm achieves success leading to ‘dominance’ then the competitive structure of the market has already been harmed. This is not the same as saying that bigness is in itself ‘bad’. What it means in Europe, though, is that the market leader that attains ‘dominance’— whether by superior skill, foresight, industry or not — ‘has a special responsibility not to allow its conduct to impair genuine undistorted competition on the common market’.¹⁰ This is a very different fundamental starting point from the ethic of freedom of contract which prevails in US antitrust law and which leads to less imposition on dominant firms of a ‘duty to deal’ with their rivals.¹¹

This assumption about dominance, and the related ‘special responsibility’, are so well established in European law that they were never likely to be altered by policy guidance from even the ‘central’ competition agency in Europe. However, the Commission’s new economic approach could have tried to define better how and when the competitive ‘structure’ would be harmed. It could have also set out what benefit a ‘special responsibility’ might offer, over and above the obvious ‘order’ it imposes on competition between the dominant firm and its rivals, and the obvious resultant chill on the dominant firm’s incentives to innovate. The Guidance is silent on these issues, and merely restates the case law. Nor does the essential theory offer any analysis of whether, as a direct

¹⁰ Case C-322/81 *NV Nederlandsche Banden-Industrie Michelin v. Commission* [1983] ECR 3461, para. 57.

¹¹ See e.g. *United States v. Colgate & Co.*, 250 U.S. 300 (1919).

result of the firm's dominance, its rivals actually exert less competitive constraint on its conduct. That 'harm' is taken for granted.

The second assumption made in the Guidance is that foreclosure itself is anticompetitive. According to the Guidance, the Commission is concerned about the dominant firm creating what is termed 'anticompetitive foreclosure'. The Commission implies that the adjective modifies the noun, and indeed that is what most people would expect: the foreclosure must be proven to be anti-competitive in order to become an agency priority. Foreclosure of rivals can't be enough, one would think. Indeed, the Guidance frequently states that 'anticompetitive' means some form of likely harm to the welfare of consumers. Unfortunately however, as the examples of individual abuses listed in the Guidance reveal, no separate proof of any likely harm to consumers is required. Foreclosure appears to be sufficient. Even then, proof of foreclosure isn't necessary: it being likely is enough. Throughout the Guidance there is a self-referencing circularity of argument that assumes that likely foreclosure will be likely to harm consumers. As a result, it isn't necessary to prove that consumer harm is likely to evidence 'antitrust injury' under EU law.

The focus on foreclosure is founded in Ordoliberal reasoning: when a dominant firm does something that may make it difficult for a rival to expand, or when it offers a new product bundle with which a rival cannot compete, then this is somehow seen as a problem that requires a government order to fix. Economic analysis is used to identify how likely the foreclosure may be; but no evidence is required to identify whether consumers are in fact likely to be harmed by the conduct. Nor is there a clear examination of whether the dominant firm is actually pushing its rivals out of the race, or simply pulling away from its competition.

Regrettably even this is not the end of the concern. While the Guidance is the most important policy document within the EU on this subject, as a matter of European law, it admits that it merely 'sets out the enforcement priorities that will guide the Commission's action' and is 'without prejudice to the interpretation of Article 102 by the European Court of Justice or the Court of First Instance'.¹² This is an important limitation, since

¹² Guidance, paras. 2 and 3

the Court has resisted even the economic approach pressed for by the Commission; its cases adopt a much more formalistic approach which deems unnecessary any evidence of consumer harm, whether likely or actual.¹³ Some cases even go so far as to say that proof of harm to rivals is unnecessary: the European Court has rejected countervailing evidence of rivals' market share actually growing during the period of the 'abuse', holding that 'but for' the 'abuse' the share would have been likely to have grown more.¹⁴

This focus on rivalry and consequent concern with foreclosure itself is where European law on abuse most differs from American monopolisation law. While economic reasoning is certainly being used more and more in European antitrust cases, it is used to prove the theoretical likelihood of foreclosure. The inevitable next question – 'is this likely to harm consumers?' – is never considered; an affirmative answer is assumed.

In sum, then, European law on abuse still contains too many inferences and not enough proof. This is why no one can assert with any credibility that competition law on both sides of the Atlantic shares the same focus on consumer harm.

Examining the assumptions in detail

The Guidance on Article 102 starts with some strong intentions regarding battling conduct that harms consumers. This rhetoric isn't matched in reality. The Commission states emphatically that: 'In applying Article 102 to exclusionary conduct by dominant undertakings, the Commission will focus on those types of conduct that are most harmful to consumers' (Guidance, para. 5). As this Guidance took years to craft, and is a product of consultation with innumerable expert economists and lawyers, as well as negotiations among the Member States, it is worth looking at all of its wording carefully. When you

¹³ In *British Airways v. Commission*, for example, it was stated by the Advocate General that an 'indirect detriment to consumers' can be assumed where 'it is shown that the conduct of a dominant undertaking is likely adversely to affect the structure of competition, unless there is an objective economic justification for it': Opinion of A G Kokott in Case C-95/04 P *British Airways v. Commission* [2007] ECR I-2331, para. 89.

¹⁴ *British Airways v. Commission*, para. 33: 'the growth in the market shares of some of BA's airline competitors ... did not mean that BA's practices had no effect, since, in the absence of those practices, "it may legitimately be considered that the market shares of those competitors would have been able to grow more significantly"' (citing CFI judgment para. 298)

do that, it becomes clear that the Guidance contains too many assumptions – and not enough actual guidance - regarding what causes consumer welfare harm.

Assumption 1: dominance may not be an abuse; but it is a ‘problem’ that needs correcting

In its Guidance, the Commission first explains that:

Dominance has been defined under Community law as a position of economic strength enjoyed by an undertaking, which enables it to prevent effective competition being maintained on a relevant market, by affording it the power to behave to an appreciable extent independently of its competitors, its customers and ultimately of consumers¹⁵.

This notion of independence is related to the degree of competitive constraint exerted on the undertaking in question. Dominance entails that these competitive constraints are not sufficiently effective and hence that the undertaking in question enjoys substantial market power over a period of time. This means that the undertaking's decisions are largely insensitive to the actions and reactions of competitors, customers and, ultimately, consumers.

The Commission may consider that effective competitive constraints are absent even if some actual or potential competition remains¹⁶. (Guidance, para. 10)

Economists may question whether any firm can truly be ‘independent’ from its rivals and consumers, even when it exercises a degree of market power. Presumably, even monopolists cannot ramp prices up without inducing entry from rivals. Nevertheless, the

¹⁵ See Case 27/76 *United Brands Company and United Brands Continentaal v. Commission* [1978] ECR 207, para. 65; Case 85/76 *Hoffmann-La Roche & Co. v. Commission* [1979] ECR 461, para. 38.

¹⁶ See Case 27/76 *United Brands Company and United Brands Continentaal v. Commission* [1978] ECR 207, paras. 113-121; Case T-395/94 *Atlantic Container Line and Others v. Commission* [2002] ECR II-875, para. 330.

seemingly impossible test of ‘independence’ has been met relatively easily in European cases.¹⁷ Firms have been held to be dominant at market shares less than 40% and with reasonably low entry barriers, and where their rivals are actually growing and in particular taking share from the dominant firm itself.¹⁸ Consequently, one should not place too much weight on this ‘independence’ requirement in European competition law.

Fortunately, the Commission’s Guidance provides more clarity as to the actual concern at hand, *viz.* an absence of effective competitive constraints on the dominant firm:

The Commission considers that an undertaking which is capable of *profitably increasing prices above the competitive level for a significant period of time* does not face sufficiently effective competitive constraints and can thus generally be regarded as dominant. (Guidance, para. 11, emphasis added.)

This statement is remarkable, and a first for European competition law. Don’t assume that Robert Bork is at the helm of DG COMP just yet though. Prices matter, but they are not the only concern in competition policy, especially in Europe. The Commission makes clear that:

... the expression ‘increase prices’ includes the power to maintain prices above the competitive level and is used as *shorthand* for the various ways in which the parameters of competition - such as *prices, output, innovation, the variety or quality of goods or services* - can be influenced to the advantage of the dominant undertaking and to the detriment of consumers. (Guidance, para. 11, emphasis added.)

¹⁷ See e.g. Case 6-7/73 *Istituto Chemioterapico Italiano Spa and Commercial Solvents Corporation v. Commission* [1974] ECR 223; Case 85/76 *Hoffmann La Roche v. Commission* [1979] ECR 461; Case 27/76 *United Brands v. Commission* [1978] ECR 207; Case 322/81 *Nederlandsche Banden-Industrie Michelin NV v. Commission* [1983] 3461.

¹⁸ See Case T-219/99 *British Airways v. Commission* [2003] ECR II-5917 (CFI); and Case C-95/04 P *British Airways v. Commission* [2007] ECR I-2331 (ECJ): ‘Th[e] evidence showed that, in the United Kingdom, the market share of competing airlines grew during the period of the alleged infringement and that the proportion of BA tickets in travel agents’ sales diminished.’

The term ‘increasing prices’, then, is only being used as shorthand; not as a proxy or as determinative proof of harm.

The Commission is obviously concerned about consumer harm then; there is no question about that. It has set out the various harms to prices, output, innovation, and the variety or quality of goods or services that might result from exclusionary abuses. How might these harms come about through exclusion though? For the Commission, the touchstone – the defining ‘theory of harm’ if you will – is to ‘ensure that dominant undertakings do not impair effective competition by foreclosing their competitors in an anticompetitive way and thus having an adverse impact on consumer welfare, whether in the form of higher price levels than would have otherwise prevailed or in some other form such as limiting quality or reducing consumer choice’ (Guidance, para. 19). It is in relation to *how* the Commission *actually tests* for these consumer harms that the absence of any real analytical rigour is revealed. Its theory of harm resulting from anticompetitive foreclosure doesn’t go far enough.

Assumption 2: harmful abuse: foreclosure leading to consumer harm ("anticompetitive foreclosure")

The Commission explains that the term "anticompetitive foreclosure" is used to describe:

a situation where effective access of actual or potential competitors to supplies or markets is hampered or eliminated as a result of the conduct of the dominant undertaking whereby the dominant undertaking is likely to be in a position to profitably increase prices to the detriment of consumers.
(Guidance, para. 19)

Recall that ‘prices’ is but shorthand for all manner of depredations on competition. Note also that ‘consumers’ includes intermediate and final consumers.¹⁹

The Commission considers the following factors²⁰ to be generally relevant to an assessment of ‘anticompetitive foreclosure’:

¹⁹ Guidance, para. 19.

- *the position of the dominant undertaking.* In general, the stronger the dominant position, the higher the likelihood that conduct protecting that position leads to anticompetitive foreclosure;
- *the conditions on the relevant market.* ...Economies of scale mean that competitors are less likely to enter or stay in the market if the dominant undertaking forecloses a significant part of the relevant market. Similarly, the conduct may allow the dominant undertaking to "tip" a market characterised by network effects in its favour or to further entrench its position on such a market. Likewise, if entry barriers in the upstream and/or downstream market are significant, this means that it may be costly for competitors to overcome possible foreclosure through vertical integration;
- *the position of the dominant undertaking's competitors.* ...A specific competitor may play a significant competitive role even if it only holds a small market share compared to other competitors. It may, for example be the closest competitor to the dominant firm, be a particularly innovative competitor, or have the reputation of systematically cutting prices...;
- *the position of the customers or input suppliers.* This may include consideration of the possible selectivity of the conduct in question. The dominant undertaking may apply the practice only to selected customers or input suppliers who may be of particular importance for the entry or expansion of competitors, thereby enhancing the likelihood of anticompetitive foreclosure²¹;
- *the extent of the allegedly abusive conduct.* In general, the higher the percentage of total sales in the relevant market affected by the conduct, the longer its duration, and the more regularly it has been applied, the greater is the likely foreclosure effect;

²⁰ Set out from the Guidance, at para. 20.

²¹ Case T-228/97 *Irish Sugar v. Commission* [1999] ECR II-2969, para. 188.

- *possible evidence of actual foreclosure.* If the conduct has been in place for a sufficient period of time, the market performance of the dominant undertaking and its competitors may provide direct evidence of anticompetitive foreclosure. For reasons attributable to the allegedly abusive conduct, the market share of the dominant firm may have risen or a decline in market share may have been slowed. For similar reasons, actual competitors may have been marginalised or may have exited, or potential competitors may have tried to enter and failed;
- *direct evidence of any exclusionary strategy.* This includes internal documents which contain direct evidence of a strategy to exclude competitors, such as a detailed plan to engage in certain conduct in order to exclude a competitor, to prevent entry or to pre-empt the emergence of a market, or evidence of concrete threats of exclusionary action. Such direct evidence may be helpful in interpreting the dominant undertaking's conduct.

Effects analysis has clearly come to the fore: all of these factors - save the final element of 'intent' – involve a laudable consideration of the effects of the practice. They all focus on the effects that a practice may have on rivals. This is an obvious concern for a paper on exclusionary abuse, which is obviously about rivals. That is accepted. If the case prioritisation is supposed to be constrained by a concern to prevent conduct that is 'most harmful to consumers' though then something more is needed. Focussing on foreclosure alone is still too broad; it doesn't examine whether consumers are indeed likely to be harmed by such conduct, or to what degree.

This divergence in approach is due to one fundamental difference between American Monopolisation law and European abuse of dominance provisions: in Europe an Ordoliberal concern with 'rivalry' over efficiency, and its focus on controlling dominance before it actually causes harm to consumers, militates towards less proof - and more assumptions and inferences - of harm. In particular, Ordoliberalism is most concerned

about harm to competitors. It shares the aim of protecting consumers but does not require proof of harm to them in order to authorise intervention. Harm to consumers will be assumed if likely harm to rivalry can be established. In contrast, the logic of putting the word ‘anticompetitive’ in front of ‘foreclosure’ in the Guidance, was – one would have thought – to limit Commission intervention to cases of foreclosure ‘whereby the dominant undertaking is likely to be in a position to profitably increase prices to the detriment of consumers’.²² That limitation has been left out of the analysis though.

Whether this approach is correct or not, rather depends on what a regime chooses to prioritise, how much evidence it decides that it needs to prove its case, and where it chooses to place itself along the spectrum of Type 1 to Type 2 enforcement errors that it believes it can tolerate. If an authority states it will accept some under-enforcement so that it does not risk chilling some pro-competitive activity, then it will not intervene without proof of likely or actual harm to consumers. If on the other hand an authority is worried about letting too much possibly anti-competitive conduct slip through its net, it will be satisfied with less proof - and more assumptions - of harm, regardless of the consequences for pro-competitive activity.²³

The fact that the European Commission’s Guidance takes the latter approach is obvious when we look at some specific examples.

Examples of assumptions 1 and 2:

1. The link between dominance and abuse

In contradiction with the general insights of a proper economic approach,²⁴ the Guidance is inherently suspicious of dominance. That is clear. The Commission does not find dominance itself to be an offence,²⁵ but dominance certainly is a factor that bleeds across to the abuse analysis itself. Thus the Commission relies on case law to state that:

²² Guidance, at para 19.

²³ On this issue, see Chapter 4 by Katsoulacos and Ulph in this Volume.

²⁴ See Chapter 1 by Etro and Kokkoris in this Volume.

²⁵ Indeed, it is prevented from doing so by the words of the EC Treaty: only an ‘abuse’ of a ‘dominant position’ is prohibited under Article 82 EC.

Experience suggests that the higher the market share and the longer the period of time over which it is held, the more likely it is that it constitutes an important preliminary indication of the existence of a dominant position and, in certain circumstances, of possible serious effects of abusive conduct, justifying an intervention by the Commission under Article 82²⁶. (Guidance, para. 15)

To some eyes most of this paragraph may seem intuitively correct. To others, it may be surprising, particularly the point about a relatively stable dominant position being an ‘important preliminary indication ... of possible serious effects of abusive conduct’. Dominance, after all, can also be attributed to success. Market share relates to sales, and thus, presumably to demand for the product. It seems rather chilling for an authority to suggest that the longer that you attract more customers and more sales from your rivals the more likely it is a ‘preliminary indication’ that you are abusing a dominant position. Surely that can’t be what is intended. Yet there it is in black and white.

2. a) Exclusive purchasing

The Commission’s approach to exclusive purchasing commitments is set out as follows:

The Commission will focus its attention on those cases where it is likely that consumers as a whole will not benefit. *This will in particular be the case if there are many customers and the exclusive purchasing obligations of the dominant undertaking, taken together, have the effect of preventing the entry or expansion of competing undertakings.* (Guidance, para. 34, emphasis added)

The capacity for exclusive purchasing obligations to result in anticompetitive foreclosure arises in particular where, without the obligations, an important competitive constraint is exercised by competitors who either are not yet present in the market at the time the

²⁶ The Guidance notes that, as to the relationship between the degree of dominance and the finding of abuse, see Joined Cases C-395/96 P and C-396/96 P *Compagnie Maritime Belge Transports, Compagnie Maritime Belge and Dafra-Lines v. Commission* [2000] ECR I-1365, para. 119; Case T-228/97 *Irish Sugar v. Commission* [1999] ECR II-2969, para. 186.

obligations are concluded, or who are not in a position to compete for the full supply of the customers.

Rivals may not be able to compete for an individual customer's entire demand because the dominant undertaking is an unavoidable trading partner at least for part of the demand on the market, for instance because its brand is a 'must stock item' preferred by many final consumers or because the capacity constraints on the other suppliers are such that a part of demand can only be provided for by the dominant supplier²⁷.

If competitors can compete on equal terms for each individual customer's entire demand, exclusive purchasing obligations are generally unlikely to hamper effective competition unless the switching of supplier by customers is rendered difficult due to the duration of the exclusive purchasing obligation.

In general, the longer the duration of the obligation, the greater the likely foreclosure effect. However, if the dominant undertaking is an unavoidable trading partner for all or most customers, even an exclusive purchasing obligation of short duration can lead to anticompetitive foreclosure. (Guidance, para. 36, emphasis added.)

It is rather appropriate that this, the first, 'abuse' considered by the Commission's Guidance contains echoes of the 'dominance as abuse' approach described directly above. Here we see that the fact that customers want the dominant firm's wares is itself inherently suspect. There is no suggestion the 'must stock' nature of a product is due to any coercion by the dominant firm. It simply reflects past consumer demand and future expectations of that demand. Even then, the dominant firm's wholesale or retail customers are not tied to it irrevocably, even by 'must stock' items. There are simply some products that a wholesale or retail customer knows that its consumers will want; and thus is more likely to order. Of course rival suppliers have difficulty supplying that part

²⁷ Case T-65/98 *Van den Bergh Foods v. Commission* [2003] ECR II-4653, paras. 104 and 156.

of the customer's demand; they don't supply that particular product or brand. Viewing this as somehow nefarious, when it is the normal result of competition, is most peculiar. The fact that the dominant firm may seem 'unavoidable' for some parts of the customer's requirements is just business reality, but is not necessarily harmful. The purchaser can always not stock the items, after all. If the unavoidability is due to pure commercial rationality on the part of the retailer, it seems a rather odd concern for an enforcement authority to have. This is even apart from the additional efficiencies, certainty, savings, and payment that come with the exclusivity.

Obviously, it is not the customer that the Commission is concerned about but the dominant firm's competitors, who will thus have less 'shelf space' for which to compete when more of demand is tied up with exclusivity arrangements. This may in turn harm the customer, and lead it to accept terms from the dominant firm that it would rather not. Still, these indirect effects are not expressly considered or examined in the Guidance. Nor is there any analysis of what consumers want (other than the obvious point that they want some of the 'must stock' items). What actually succeeds in getting onto a given retailer's shelves is affected by advertising, brand, price and ultimately the quality and perceived value of the product to the end-user. These factors are not considered in the Guidance. It just seems odd and rather chilling to normal business operations to cast exclusive purchasing in such a pejorative light. Of course, one shouldn't be naïve: exclusive purchasing commitments can and do exclude rivals for the length of the contract. However, a policy document that supposedly prioritises abuses that most harm consumers should actually set out and apply some test for consumer harm, rather than assume that such harm is likely when retailers and their largest suppliers agree exclusive deals.

2. b) Rebates

Where exclusive purchasing supposedly guarantees exclusivity *ex ante*, rebate systems are much looser arrangements and reward loyalty *ex post*. The Commission sees little difference between the two: either way, rivals are assumed to be incapable of matching a dominant firm's offer.

When considering rebate systems, the Commission supplements its analysis of anticompetitive foreclosure with some extra factors:

- ... the likelihood of anticompetitive foreclosure is higher where competitors are not able to compete on equal terms for the entire demand of each individual customer. (Guidance, para. 39)²⁸
- ... retroactive rebates may foreclose the market significantly, as they may make it less attractive for customers to switch small amounts of demand to an alternative supplier, if this would lead to loss of the retroactive rebates²⁹. The potential foreclosing effect of retroactive rebates is in principle strongest on the last purchased unit of the product before the threshold is exceeded. However, what is in the Commission's view relevant for an assessment of the loyalty enhancing effect of a rebate is not simply the effect on competition to provide the last individual unit, but the foreclosing effect of the rebate system on (actual or potential) competitors of the dominant supplier. The higher the rebate as a percentage of the total price and the higher the threshold, the greater the inducement below the threshold and, therefore, the stronger the likely foreclosure of actual or potential competitors. (Guidance, para. 40)

There then follows a detailed examination of costs tests. Throughout, the overriding concern is clear: potential foreclosure of rivals of the dominant firm, who may not be able to offer sufficient financial incentives to prevent customers from accepting the dominant firm's offer. Rivals have it worst, argues the Commission, when the dominant firm offers retroactive rebates – which apply over all units supplied to the customer during the relevant period, and are based on the customer beating certain sales targets, for example, year on year. These rebates are looked at particularly negatively in Europe. As with exclusive purchasing, we see the rival-based concern with a dominant firm supposedly benefiting from its past success, effectively locking-in customers, and making

²⁸ See Case T-203/01 *Michelin v. Commission (Michelin II)* [2003] ECR II-4071, paras. 162-163. See also Case T-219/99 *British Airways v Commission* [2003] ECR II-5917, paras. 277 and 278.

²⁹ Case 322/81 *Nederlandsche Banden Industrie Michelin v. Commission (Michelin I)* [1983] ECR 3461, paras. 70-73.

it financially irresponsible for them to tear themselves away from the rebate programme to accept a rival's more expensive offer. The Commission's position on rebates is based on a theory of 'suction effect' that has driven case law in this area in Europe: the greater the rebate offered by the dominant firm, and the more products over which it is offered, the more and more expensive it becomes for rivals to contest that part of the customer's requirements and induce it to switch over from the dominant firm.³⁰

The message from Brussels: since the customer can't be expected to act in its own longer term interests by saying 'No' once in a while to the dominant firm's better offer, the Commission has to step in to ensure that the customer has some choice of supply. The rationale: the Commission has to think about the customer's longer term interests and prevent it from being made 'an offer it can't refuse' so that alternative suppliers are able to still exert some competitive constraint on the dominant firm. This is presumably so that the dominant firm is not left free to start charging whatever it likes - but it is also for the various non-price benefits the customer receives from simply having a choice of supplier.

There are several arguments against this reasoning: should competition law be so paternalistic, and deprive the customer of its interest in a rebate? Should government assume that customers are so unsophisticated that they can't maintain a balance between having only one cheap supplier and having several and so keep the former on its toes? Isn't there a natural dynamic where the customer will want choice anyway because that is what its own customers will want too? Isn't the Commission ignoring the dynamic nature of competition among suppliers themselves whereby they all watch each other and contest various offers all of the time? If a smaller supplier can't compete with what the dominant firm is offering over a whole range of products, it can at least make targeted pricing - or other offers to preserve its position, or even to grow.

Even if the Commission's theory of anticompetitive foreclosure were sound, though, its new 'economic approach' should mean that it is at least tested. Instead there is no examination of whether the rebate would lead rivals to exit, or reduce their competitive

³⁰ See generally, Case 322/81 *NV Nederlandsche Banden Industrie Michelin v. Commission* ('*Michelin I*') [1983] ECR 3461, para. 81; Case T-203/01 *Manufacture française des pneumatiques Michelin v. Commission* ('*Michelin II*') [2003] ECR II-4071, paras. 87-88; Case T-219/99 *British Airways v. Commission* [2003] ECR II-5917, paras. 272-273.

constraint on the dominant firm: this just seems to be assumed. There may be intuitive reasons to believe in the “suction effect” theory, but business doesn’t operate on intuition alone, and nor should policy.

Most importantly, there is no examination of where the final consumer would stand in all of this. Allowing a rebate programme may not necessarily guarantee that the price-cut is passed on to consumers – it may be used for more service, or it may simply be a loyalty-enhancing technique, as the Commission fears. This is not blind loyalty, though; it is loyalty with a view to the end-consumer’s interests in the products and at some competitive price. Forbidding the rebate removes the price-cut completely, however, from the customer and from the consumer. Perhaps their views should be considered? These rebate cases rarely if ever arise from a customer complaint. They are all from competitor complaints. Doesn’t it seem more sensible to at least involve customers in the decision about whether or not to accept a rebate, particularly when you are contemplating denying them of it completely? The approach in Europe though is that such evidence is not sought either from the immediate beneficiary of the rebate, nor from the end consumer. At the European Courts, the consistent legal position over the last two decades has been that the suction effect theory is real, and does not need to be proven – indeed the courts have assumed that rivals are foreclosed even when they are making more and more sales.³¹ Certainly no proof of possible harm to consumers has been required in the case law. As a result, in Europe a programme of commissions to travel agents operated by British Airways, was found to be ‘foreclosing’ Virgin and the company was fined heavily as a result.³² When Virgin brought the same complaint in the US, its case was summarily dismissed for not alleging antitrust injury.³³

It is not clear that the Guidance will unseat firm EU law, or force the European courts into a more direct examination of consumer welfare issues. If the Commission isn’t ready to go there yet, it doesn’t seem likely that the courts will.

³¹ As occurred in the *British Airways* case: Case T-219/99 *British Airways v. Commission* [2003] ECR II-5917; see above.

³² See *ibid.*

³³ See *Virgin Atl. Airways Ltd. v. British Airways Plc*, 69 F. Supp. 2d 571, 581, 582 (S.D.N.Y. 1999); and *Virgin Atlantic Airways Ltd. v. British Airways PLC*, 257 F.3d 256 (2nd Cir. 2001).

2. c) Tying and bundling

The Commission's Guidance states that

The risk of anticompetitive foreclosure is expected to be greater where the dominant undertaking makes its tying or bundling strategy a lasting one, for example through technical tying which is costly to reverse. Technical tying also reduces the opportunities for resale of individual components. (Guidance, para. 53)

In the case of bundling, the undertaking may have a dominant position for more than one of the products in the bundle. The greater the number of such products in the bundle, the stronger the likely anticompetitive foreclosure. This is particularly true if the bundle is difficult for a competitor to replicate, either on its own or in combination with others. (Guidance, para. 54)

Here again we see European suspicion of an improved offering by the dominant firm, this time with respect to the product rather than its price directly. And here again we see a concern for rivals who might not be able to improve their offering to match that of the dominant firm. Again we see no concern for consumer harm, or benefit, from the conduct.³⁴

Of course it would be naïve to suggest that tying or bundling should be *per se* legal. That is not what I am suggesting. There should be some form of analysis of the suggested harm but not just to rivals - also to final consumers; the benefits that they undoubtedly receive from a bundled package should also be analysed. Pulling ahead of one's rivals by offering more should not be viewed as foreclosing them; the rivals do that to themselves when they refuse to compete with the product bundle. If they try to match the bundle and are incapable of doing so, is that really a matter for government intervention?

³⁴ For a more extensive discussion on the economic approach to tying see Chapter 1 by Etro and Kokkoris in this Volume.

Or is that just competition? In contrast, if there is true exclusion and likely harm in the near term to consumers, then this should be proven.

2. d) Refusal to deal

The Commission begins by explaining its approach in terms that will be familiar to US antitrust lawyers, stating that it ‘starts from the position that, generally speaking, any undertaking, whether dominant or not, should have the right to choose its trading partners and to dispose freely of its property’ (Guidance, para. 75). The Commission moves swiftly on, however, to what amounts to a careful restatement of European case law³⁵ on refusal to deal, stating that it will act against such practices:

as an enforcement priority if the following cumulative circumstances are present:

- the refusal relates to a product or service that is objectively necessary to be able to compete effectively on a downstream market;
- the refusal is likely to lead to the elimination of effective competition on the downstream market; and
- the refusal is likely to lead to consumer harm. (Guidance, para. 81)

With respect to objective necessity, what is determinative is whether ‘an input is indispensable’, which occurs

where there is no actual or potential substitute on which competitors in the downstream market could rely so as to counter – at least in the long term - the negative consequences of the refusal. In this regard, the Commission will normally make an assessment of whether competitors could effectively duplicate the input produced by the dominant undertaking in

³⁵ Joined Cases C-241/91 P and C-242/91 *Radio Telefis Eireann (RTE) and Independent Television Publications (ITP) v. Commission (Magill)* [1995] ECR 743, para. 52-53; Case 7/97 *Oscar Bronner v. Mediaprint Zeitungs- und Zeitschriftenverlag, Mediaprint Zeitungsvertriebsgesellschaft and Mediaprint Anzeigengesellschaft* [1998] ECR I-7791, paras. 44-45; Judgment of 17 September 2007 in Case T-201/04 *Microsoft v. Commission* [2007] ECR II-3601, para. 421.

the foreseeable future. The notion of duplication means the creation of an alternative source of efficient supply that is capable of allowing competitors to exert a competitive constraint on the dominant undertaking in the downstream market³⁶. (Guidance, para. 83)

Here again we see the Commission's view that part of its role is to act when a rival is unable to compete without help from its dominant competitor. The fact that the rival has been cut off for what may be a legitimate business reason is not considered.

With respect to the second condition – that of elimination of effective competition - the Guidance appears to echo once more the concern about dominance *per se*; it states that:

[t]he likelihood of effective competition being eliminated is generally greater the higher the market share of the dominant undertaking in the downstream market; the less capacity-constrained the dominant undertaking is relative to competitors in the downstream market; the closer the substitutability between the dominant undertaking's output and that of its competitors in the downstream market; the greater the proportion of competitors in the downstream market that are affected, and the more likely it is that the demand that could be served by the foreclosed competitors would be diverted away from them to the advantage of the dominant undertaking. (Guidance, para. 85)

The third condition for analysing refusals expressly refers to consumer harm. This should be good news:

The Commission considers that consumer harm may, for instance, arise where the competitors that the dominant undertaking forecloses are, as a result of the refusal, prevented from bringing to market innovative goods

³⁶ Case 7/97 *Oscar Bronner v. Mediaprint Zeitungs- und Zeitschriftenverlag, Mediaprint Zeitungsvertriebsgesellschaft and Mediaprint Anzeigengesellschaft* [1998] ECR I-7791, para. 46; Case C-418/01 *IMS Health v. NDC Health* [2004] ECR I-5039, para. 29.

or services and/or where follow-on innovation is likely to be stifled³⁷.

(Guidance, para. 87)

Probably one of the starkest differences of position between the European and American approaches comes with respect to this issue of consumer harm due to reduced innovation, however. The EU is much quicker to mandate a duty to deal, for example, to avoid stifling follow-on innovation by rivals. The US imposes such a duty in very restricted circumstances. American authorities assume that such a duty would, in and of itself, harm the dominant firm's incentives to innovate. This is one area, however, where the European Commission does not rely on an assumption: it requires proof that the dominant firm could be harmed. In *Microsoft*, for example, the US authorities and courts took it as read that an order by the government to force a company to share its intellectual property with its rivals – even for a price – would chill its incentives to innovate.³⁸ In contrast, the European Court of First Instance held that such harm could not be assumed.³⁹ In Europe the dominant firm thus has the burden of proving that forced sharing harmed its incentives. The Guidance repeats this view by stating clearly that far from assuming that mandating licensing, for example, will inevitably chill incentives to innovate, 'it falls on the dominant undertaking to *demonstrate* any negative impact which an obligation to supply is likely to have on its own level of innovation' (Guidance, para. 90, emphasis added).

So here we see not only a serious and significant difference of approach in the ways that Europe and the US treat incentives to innovate, but also a difference of approach within the European analysis: consumer harm from a refusal to deal will be assumed without proof; harm to the dominant firm's incentives to innovate (from government intervention to mandate dealing) will not be assumed but must be proven.

³⁷ Judgment of 17 September 2007 in Case T-201/04 *Microsoft v. Commission* [2007] ECR II-3601, paras. 643, 647-649, 652-653 and 656.

³⁸ *U.S. v. Microsoft*, 253 F.3d 34 (D.C. Cir. 2001), at 65: 'In a competitive market, firms routinely innovate in the hope of appealing to consumers, sometimes in the process making their products incompatible with those of rivals; the imposition of liability when a monopolist does the same thing will inevitably deter a certain amount of innovation. This is all the more true in a market, such as this one, in which the product itself is rapidly changing.'

³⁹ Judgment of 17 September 2007 in Case T-201/04 *Microsoft v. Commission* [2007] ECR II-3601, paras. 696-697. 'The Commission also examined the applicant's argument that if it were required to give third parties access to that technology there would be a negative impact on its incentives to innovate. The Court finds that, as the Commission correctly submits, Microsoft, which bore the initial burden of proof, did not sufficiently establish that if it were required to disclose the interoperability information that would have a significant negative impact on its incentives to innovate.'

2. e) Predation

The primary difference between US and EC law on predation has always been that US authorities and courts require evidence that recoupment is likely, before prohibiting predatory behaviour,⁴⁰ whereas the EC does not.⁴¹ The US requirement of recoupment reflects the Chicago School belief that the market is inherently self-correcting: if monopolists cannot recoup their losses later, then it must be due to the existence of (actual or potential) competitive restraints; if such competitive restraints exist in the market, the consumer will not be harmed by any increased prices of the monopolist.⁴² The European Commission does not exhibit such faith in the market.⁴³ It believes that when predation occurs it is based on the assumption that below cost pricing can be a rational strategy adopted by a dominant firm to eliminate competitors.⁴⁴ EC law assumes that a dominant firm, by predating without possibility of recoupment, can still cause harm to its rivals – by for example disciplining them - and thus removing their competitive constraint. This difference is maintained in the new Guidance (para. 71). In addition, the EC is satisfied that mere intention to predate is sufficient, without looking for harm to rivals (Guidance, para. 66). Again, evidence that firms have been foreclosed and have exited is not necessary, with the Commission being satisfied if the competitor has been prevented from ‘competing vigorously’ (Guidance, para. 69).

3. The new efficiencies defence for abuse (Guidance, paras. 29-31)

The European Commission has at last introduced an express examination of efficiencies into its analysis of whether an abuse may violate European law. One would expect this to introduce express consumer welfare issues – and it does. The burden is on the dominant

⁴⁰ *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.* 509 U.S. 209 (1993). Recently, the Supreme Court confirmed that predatory buying also requires proof of recoupment: *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co.* 127 S. Ct. 1069 (2007).

⁴¹ See Case C-62/86 *AKZO Chemie BV v. Commission* [1991] ECR I-03359; and Case C-333/94 P *Tetra Pak v. Commission* [1996] ECR I-5951. The EC test for predation was recently restated by the CFI: Case T-340/03 *France Télécom SA v. Commission* [2007] ECR II-107.

⁴² See P Marsden and P Whelan, 'Re-Examining Transatlantic Divergences in Substantive and Procedural Competition Law', paper presented at the Sedona Conference, 'Antitrust Law and Litigation X: The Globalisation of Antitrust Enforcement', Florence, Italy, 17-18 September 2008.

⁴³ *Ibid.*

⁴⁴ See J Temple Lang and R O'Donoghue, 'Defining Legitimate Competition: How to Clarify Pricing Abuses under Article 82 EC' 26 *Fordham International Law Journal* 83 (2002), at 142.

firm to ‘guarantee that no net harm to consumers is likely to arise’. The Commission is the ultimate arbiter, however.

The Guidance sets out that the dominant firm ‘will generally be expected to demonstrate, with a sufficient degree of probability, and on the basis of verifiable evidence, that the following cumulative conditions are fulfilled⁴⁵:

- the efficiencies have been, or are likely to be, realised as a result of the conduct. They may, for example, include technical improvements in the quality of goods, or a reduction in the cost of production or distribution;
- the conduct is indispensable to the realisation of these efficiencies: there must be no less anti-competitive alternatives to the conduct that are capable of producing the same efficiencies;
- the likely efficiencies brought about by the conduct outweigh any likely negative effects on competition and consumer welfare in the affected markets;
- the conduct does not eliminate effective competition, by removing all or most existing sources of actual or potential competition.

It ‘then falls to the Commission to make the ultimate assessment of whether the conduct concerned ... based on a weighing-up of any apparent anticompetitive effects against any advanced and substantiated efficiencies, is likely to result in consumer harm.’ Despite the opportunity that the Guidance provides for dominant firms to defend their conduct, the cards are still stacked against them. In setting out its findings of an abuse, the Commission is not obliged to evidence any consumer harm at all. The dominant firm is however required to satisfy the above criteria: showing that its conduct creates efficiencies that are not only likely but are ‘verifiable’, that there is no less restrictive alternative, and most importantly, that there is no net reduction in consumer welfare. How the defendant is supposed to show this, when the initial claim of harm is speculative and incapable of measurement, is a very real and pressing question for advisors. Notable

⁴⁵ See, in the different context of Article 81, the Commission Communication – Notice – Guidelines on the application of Article 81(3) of the Treaty (OJ 101, 27.4.2004, p. 97).

also is the fact that much of the dominant firm conduct may well be due to its commercial strategy or interests, rather than always justifiable solely on the basis of net efficiencies.

Conclusion

Since the mid 1990s there have been notable and laudatory efforts by the European Commission to ‘modernise’ its approach to merger control, cartel enforcement and the review of vertical and other arrangements. Generally there has been a movement away from a formalistic, checklist-based review of arrangements that had traditionally prohibited some conduct *per se* by type and by category. The approach was largely pushed by the European Commission towards a consideration of a given conduct’s economic effects on competition in the market, and in particular, on consumer welfare. This development really must be underscored. It is a sea change in antitrust enforcement in Europe, and means that foreign advisors won’t say ‘it’s all Greek to me’ when asked to provide an initial view on how conduct might be viewed in Europe. It hasn’t quite gone all the way with respect to Article 102, however, and so this area will still need some explaining. Hopefully this paper will go some way towards outlining the differences in the European regime, and their analytical basis.

Furthermore, there is never likely to be complete convergence of approach between the US and the EC – and for very good reason. Laws reflect their society, its stage of economic development, and its ideals. Far from being stuck in the Dark Ages, and only recently evolving to a more Enlightened approach, European competition law maintained its strict view of exclusionary conduct in particular in order to further the ideal of a common market and then economic union. Networks of vertical arrangements that would otherwise be viewed as the *sine qua non* of an efficient multi-State distribution network were banned if they foreclosed entry from rivals, and particularly from other Member States.⁴⁶ European competition law’s view on monopolisation takes a similar view that conduct that is capable of foreclosing rivals will also be assumed to harm consumers.

⁴⁶ P Marsden and P Whelan, ‘The “Consumer Welfare” Standard as a Form of Substantive Protection for Consumers under European Competition Law’ in Ezrachi and Bernitz (eds), *Own Labels, Branded Goods and Competition Policy: The Changing Landscape of Retail Competition* (Oxford University Press: Oxford, 2008).

Here the concern is not so much about promoting trade within Europe but with preserving a form of rivalry. In Europe, an approach that protects small, medium sized and even large enterprises from the abuses of dominant firms is based on ‘Ordoliberalism’. It reflects a Germanic idea that the market needs to have some ‘order’ imposed on it to prevent the worst sorts of abuses of power. It is not a view that is unique to Europe though. In the US, we saw a similar concern for rivalry – rather than mere economic efficiency – but then it was called ‘populism’ or ‘structuralism’. It amounts to the same approach, fundamentally. What is different though, is that in the US, populism and structuralism were overwhelmed by the wave of economic reasoning that flooded out from the Chicago School. European Ordoliberalism itself has remained largely impervious to this tide of economic analysis. Instead the most that has happened is that the European Commission has agreed that it should find economic evidence of likely foreclosure, but not proof of what American antitrust is concerned with: actual or likely consumer harm.

There is nothing wrong with divergence per se. But it has ramifications. As long as this approach prevails in Europe there will continue to be perceptions and headlines that Europe focuses more on protecting or helping competitors, than on competition. This is a breeding ground for misplaced allegations of protectionism. What needs to be understood, instead, is that Europe is different; that it has a different view of competition and of government’s role in that regard. After all the years of consultation on the Guidance there is not likely to be any further convergence of approach across the Atlantic for quite some time. Learning how to advise on this approach, and how to work within it, is a ‘work in progress’. Hopefully this chapter will go some small way towards contributing to that work.