



eSAPIENCE CENTER FOR COMPETITION POLICY

VIEWPOINT:

**COMPETITION LAW AND ECONOMICS:
A MID-ATLANTIC VIEWPOINT**

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**COMPETITION LAW AND ECONOMICS:
A MID-ATLANTIC VIEWPOINT**

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by

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Introduction

When contemplating competition law and policy, many economists, I suspect, are somewhere in the Atlantic Ocean. That is to say, they feel uncomfortable with aspects of EC competition law on the grounds that it is too interventionist, and with aspects of US antitrust on the grounds that it is too *laissez faire*. I confess that I indulged in some mid-Atlantic musings during my time at the Office of Fair Trading. Sometimes the longitude tended to be around the Azores, but curiously, when in Brussels, my mind occasionally drifted towards Bermuda.

My aim this evening, then, is to offer some mid-Atlantic thoughts – first about competition economics, then about law, which I know much less about. There will be two main themes. The first is that in some respects there has been a remarkable degree of *convergence* not just internationally but also between economics and the interpretation of the law. The second is that the Ocean remains wide in other respects², and might be about to widen further. This last point is a reference to vertical price-fixing agreements, and the *Leegin* case now before the United States Supreme Court, which I suggest deserves our close attention in Europe.

¹ I am very grateful to Don Baker, Dennis Carlton, David Evans, Ariel Ezrachi, Eleanor Fox, Ben Gauntlett, Jeremy Lever, Ali Nikpay, Simon Priddis, Peter Roth and Kathrin Weisspfennig for helpful conversations and comments on the topic of this paper, responsibility for which is however mine alone.

² Not least in respect of institutions and procedures, which are however beyond my scope.

Competition economics – convergence

My first proposition, which might sound unlikely to an audience of competition law practitioners, is that competition economists are largely in agreement about the relevant economic principles. On this I am with Milton Friedman:

The public has the impression that economists never agree. They have the impression that if three economists are in a room they will get at least four opinions. That is false. If scientific issues are separated from policy and value issues, there is widespread agreement among economists whatever their political views. Over and over again I have been in a group that includes both economists and practitioners of other disciplines. Let a discussion start about almost anything and, in ten minutes or so, you will find all the economists on the same side against all the rest, whether the economists are on the left or the right or in the middle.³

Indeed even on competition *policy* issues – as distinct from cases on which they may have been engaged – there is substantial agreement among competition economists. Thus Massimo Motta's (2004) *Competition Policy: Theory and Practice* and Michael Whinston's (2006) *Lectures on Antitrust Economics* – to name the two books at the top of the reading lists I give to economics students – have a common analytical basis and show no doctrinal differences. Likewise the articles on the reading list, which are by authors from Berkeley, Oxford, Stanford, Toulouse and so on. The same common economic framework is reflected in the report on “An economic approach to Article 82” by the European Commission's Economic Advisory Group for Competition Policy (EAGCP, 2005). Its citations are trans-Atlantically diverse, yet its authorship – Gual (Barcelona), Hellwig (Bonn), Perrot (Paris), Polo (Milan), Rey (Toulouse), Schmidt (Munich) and Stenbacka (Helsinki) – could hardly be accused of being Anglo-Saxon, still less Anglo-American. I could go on.

You might be thinking “But what about Chicago?”. Indeed in the 1970s and early 1980s there were rival schools of thought. Structuralist approaches to industrial economics, with their anti-concentration policy implications, that had held sway were subject to fierce attack from the ‘Chicago School’ and elsewhere. Robert Bork described

³ Quoted in Breit, W., and R.W. Spencer (1995), *Lives of the Laureates: Thirteen Nobel Economists*, Cambridge, MIT Press.

antitrust as a policy at war with itself, and advocated *per se* lawfulness of a range of commercial conduct much of which had become close to *per se* illegal under prevailing standards. In US antitrust policy there followed the “Ascent of the Chicago School,” as Kovacic and Shapiro (2000) call it, through the 1970s and 1980s. European competition law and policy, of course, has had nothing like a Chicago period: the Great Lakes are far even from the Atlantic.

While Chicago was ascending in US antitrust law and policy, competition economics internationally was undergoing a broad-based analytic transformation. The application of game theory and contract theory, though they might sound abstract, enabled rigorous analysis of everyday market features that standard price theory (the basis for much of Chicago) left out, such as interdependent decisions between small numbers of firms, dynamics and imperfect information. The so-called “new industrial economics” gathered pace in the 1980s and was masterfully synthesized in Jean Tirole’s (1988) book – Tirole of the Massachusetts Institute of Technology and Toulouse, I might add. This way of thinking, as well as being more rigorous, absorbed the Chicago critique by recognizing, for example, that market concentration and vertical contractual relationships can be natural and efficient, but beyond Chicago showed how, depending on the circumstances, harm to competition and consumers can result from various market practices – thereby highlighting the key questions of fact to address in cases. In economics, if not in policy, we now have what can reasonably be called a “post-Chicago synthesis,” again to use a term of Kovacic and Shapiro. Even Chicago is now post-Chicago, as Dennis Carlton illustrates, though he is now in Washington DC.⁴

To a considerable extent, then, the economic principles and tools for competition analysis have converged. There is a broadly common way of thinking – a shared general framework in which to assess the facts and agree or disagree about what should happen in, say, a particular case.

⁴ For example, see Carlton and Waldman (2002), which, contrary to the Chicago School, argues that tying can be used to create, as well as preserve, market power.

Cartel and merger policy – convergence

To what extent can the same be said of competition law and policy? And how well do competition law and policy cohere with competition economics? The answers to these questions depend very much upon which areas of competition law and policy one is talking about.

Let us start with what Justice Scalia in the *Trinko* case called “the supreme evil of antitrust: collusion.” Economics, law and policy in all the principal jurisdictions agree that agreements to raise prices or restrict outputs between competitors should be *per se* illegal and subject to serious sanctions. That is to say, to establish that the law has been broken, it suffices to show that such agreements have been made, without any need for further analysis. The US Supreme Court recently emphasized in *Texaco v Dagher*⁵ that *per se* illegality is however the exception:

[T]his Court presumptively applies rule of reason analysis, under which antitrust plaintiffs must demonstrate that a particular contract or combination is in fact unreasonable and anticompetitive before it will be found unlawful. Per se liability is reserved for only those agreements that are “so plainly anticompetitive that no elaborate study of the industry is needed to establish their illegality.”

Most economists would not go so far as to say that horizontal price-fixing agreements are bad in *all* possible circumstances, but would agree that beneficial ones are so rare that it makes sense to ban the lot, having regard to the costs of administration and adjudication. As Whinston (2006, page 18) puts it, “the justification for the per se rule is really nothing more than an application of optimal statistical decision making.” Judge Easterbrook for the US Court of Appeals in *Schor v. Abbott Labs.* recently made a similar point but in relation to *per se* legality:

We appreciate the potential reply that it is impossible to say that a given practice “never” could injure consumers. A creative economist could imagine unusual combinations of costs, elasticities, and barriers to entry that would cause injury in the rare situation. ... But just as rules of per se

⁵ The Court ruled that it is not *per se* illegal for a lawful, economically integrated joint venture to set the prices at which the joint venture sells its products.

illegality condemn practices that almost always injure consumers, so antitrust law applies rules of *per se* legality to practices that almost never injure consumers.

Of course there are plenty of controversial subjects in the economics, law and policy of collusion about what constitutes an agreement (or concerted practice), appropriate sanctions, damages, amnesty programs and so on. But the *per se* illegality of price- and output-fixing cartels is agreed.

More surprising, perhaps, is the degree of harmony that appears to have been reached in merger policy. On this side of the Atlantic that was helped, I believe, by the 2004 revision to the European Community Merger Regulation, which among other things replaced the dominance test by the test cast primarily in terms of significant impediment to effective competition, which is much closer to, if not the same as, substantial lessening of competition. With the ECMR reforms came the important 2004 EC guidelines on the assessment of horizontal mergers, which DG Competition and national competition authorities had been discussing intensively for some time. Those EC guidelines are essentially consistent in approach with the US horizontal merger guidelines as they have developed (notably in 1992) since the radical 1982 revisions to the 1968 guidelines. There is also accord with the UK guidelines issued by the Competition Commission and OFT in 2003. More generally it was striking how much broad agreement about horizontal merger policy was found to exist in the International Competition Network working group that the OFT chaired, and indeed across the ICN community as a whole.

Horizontal mergers are also an area where law, policy and economics are more or less at one. On this let me just quote Jonathan Baker's (2003) comparison of the drafting of the 1968 and 1992 US horizontal merger guidelines:

Robert A. Hammond, who worked on the 1968 Guidelines at the Antitrust Division, once told me that the Justice Department drafting team thought about every major relevant Supreme Court antitrust decision and made sure that they could point to a sentence that encapsulated its holding. My immediate reaction, only partly facetious, was that if we were doing anything similar in drafting the 1992 Merger Guidelines, which I worked on while at the Antitrust Division, it was instead to encapsulate every

major article on industrial organization economics published in the *American Economic Review*.

While this was not exactly the approach taken to drafting the OFT guidelines, they are, I hope, soundly economics-consistent.

The same is broadly true of the draft EC *non-horizontal* merger guidelines issued last month (DG Competition, 2007). From the outset these draft guidelines clearly reflect the first of the ten principles set out by the merger sub-group of the Economic Advisory Group for Competition Policy (2006): “The competitive impact of non-horizontal mergers is fundamentally different from that of horizontal mergers.” The EAGCP note (page 3) goes on to make the nice observation that while there are “canonical models” of harm to competition from horizontal mergers (Cournot, Bertrand, repeated games), there are none such for vertical or conglomerate mergers. Indeed the nearest to a “canonical model” (Chicago School) is of *absence of harm* to competition in those contexts. Contrary to Chicago, non-horizontal mergers can harm competition, though only if there is existing market power. The task for guidelines is to highlight how, so that coherent theories of harm can be measured against the facts of cases. This seems an exemplary post-Chicago approach.

Abuse of dominance – continuing divergence

The argument so far has been that for cartels and mergers there is substantial consistency of approach both geographically and as between competition law and economics. One cannot say the same for abuse of dominance, on which I will be brief on this occasion – see DG Competition (2005), EAGCP (2006) and Vickers (2005) for more discussion.

Arguably there *should* be trans-Atlantic difference in policies towards abuse of dominance. The European economy historically has been more monopolized than that of the US, and its competitive self-righting mechanisms may be less robust. Private actions are prevalent in the US (and with the possibility of treble damages) but not (yet) in Europe. So perhaps for single-firm conduct, as distinct from cartels and possibly mergers, the balance of risks between chilling pro-competitive conduct and failing to curb anti-

competitive conduct is markedly different across the Atlantic, to an extent that warrants a different stance of law and policy. Moreover, there is substantial *intra*-jurisdictional uncertainty, if not variation, as controversial cases like *LePages* illustrate in the US.⁶

These points have some merit but I very much doubt they can explain or justify the degree of difference now apparent between the approaches to Article 82 and to section 2 of the Sherman Act. An immediate difference is that in some circumstances pure *exploitation* of market power can breach European competition law, unlike US antitrust law.⁷ As to *exclusionary* abuse, two very recent judgments in predatory pricing cases – the two *Ws* – illustrate the trans-Atlantic difference. On 30 January this year the Court of First Instance gave judgment in the *Wanadoo* case (*France Télécom v Commission*). Three weeks later on 20 February the Supreme Court issued its opinion in the *Weyerhaeuser* case. Each judgment endorses prior case law without qualification.

In *Wanadoo* dominance and abuse were found despite the new and fast-growing nature of the market for high-speed Internet access. The judgment underlines that prices below variable cost are to be assumed eliminatory – abusive in themselves. Prices above variable cost but below total cost must be regarded as abusive if part of a plan to eliminate rivals – as shown by documents revealing a strategy of market “pre-emption.” To find predatory abuse there is no need to show that recoupment of losses is likely.

Weyerhaeuser concerned allegations of predatory bidding in an input market (for logs), not predatory pricing on the selling side. The Court of Appeals had not applied the Supreme Court’s *Brooke Group* tests for predatory pricing – i.e. showing price below an appropriate measure of cost, and demonstrating a dangerous probability of recouping the investment in below-cost pricing. Arguably, law and policy should be more cautious in condemning low selling prices than high bids for inputs, on the view that low selling prices are pro-consumer and normally the essence of competition. But the Supreme Court adopted the symmetrical position, underlined the *Brooke Group* tests and made clear that

⁶ Another example is the apparent split between circuits of the US Court of Appeals over whether monopoly leveraging can by itself be a violation of section 2 of the Sherman Act. Judge Easterbrook in *Schor v Abbott*, quoted above, said not, on the Chicago School view that ‘a monopolist can take its monopoly profit just once’.

⁷ However the Court of Appeal in *Attheraces v BHB* showed a degree of aversion to price regulation via competition law, and held that cost-based assessment of excessive pricing allegations is too narrow.

they apply equally to the input side of markets. Only higher bidding that results in below-cost pricing in the output market can be the basis for a finding of predation, and a dangerous probability of recoupment must also be proved.

Neither judgment is surprising, and I am not seeking to criticize either of them. The point is to note the continuing trans-Atlantic contrast, and in an area – predatory pricing – where Article 82 law is relatively well-developed and economics-coherent. There were features of each case – the nascent market in the EC case and the input market in the US case – that might have allowed at least some modification of tone, but neither Court apparently wished that. Compare the US Court of Appeals for the Tenth Circuit in *U.S. v. AMR* in 2003, which in dismissing a case did at least say:

“Recent scholarship has challenged the notion that predatory pricing schemes are implausible and irrational. [...] Post-Chicago economists have theorized that price predation is not only plausible, but profitable, especially in a multi-market context where predation can occur in one market and recoupment can occur rapidly in other markets. [...] Although this court approaches the matter with caution, we do not do so with the incredulity that once prevailed.”

It might be said that the need to show dominance in EC law does away with the need to show recoupment in predation cases, but even if there were stricter standards of dominance analysis in Europe that would not reconcile the two bodies of law. In practice, it has been extraordinarily difficult to bring a successful predation case in the US since *Brooke Group*, quite unlike the EC. On predation, then, the Atlantic remains wide, with many economists, I believe, somewhere out in the Ocean.

Much the same can be said for exclusionary abuse generally. Last week’s judgment from the European Court of Justice in the *British Airways* reward scheme case, for example, did nothing to narrow the Atlantic. In Europe the initiative now lies with the Commission. There have been promising but so far inconclusive signs that the Commission will seize it by adopting a more economics- and effect-based policy approach, but that is a topic for another day.

Vertical agreements – prospective divergence?

The area of US antitrust law to have seen the most rapid change in interpretation has been non-price vertical agreements. From the late 1960s to the early 1980s, very much influenced by Chicago School economics, the Courts and enforcement agencies moved from *per se* illegality to rule of reason for a wide range of vertical restraints. Though EC law is perhaps less tolerant of non-price vertical agreements than US law, the 1999 reforms to the block exemption regulation for vertical agreements reflect a consistent economic approach, which in particular recognizes that (non-price) vertical agreements are generally benign in competitive conditions.

As to vertical agreements on price, US and EC law have until now been broadly consistent with each other. Each has however been less consistent with economic analysis, which in post-Chicago spirit does not support absolute hostility to RPM agreements. But the US Supreme Court recently granted *certiorari* in the *Leegin* case, where the question is whether to overturn a precedent on RPM that has stood for nearly a century.

The question before the Supreme Court in the *Leegin* case, as articulated in the Brief of *Amici Curiae* Economists in Support of Petitioners, is as follows:

Should minimum resale price maintenance continue to be deemed *per se* unlawful under Section 1 of the Sherman Act, or, in light of modern economic understanding and antitrust policy, should it instead be subject to the rule of reason, like other vertical price and non-price restraints?

Minimum RPM has been *per se* illegal under US federal law for nearly a century, since the *Dr. Miles* case of 1911.⁸ In 1968 in *Albrecht v Herald* the *per se* ban was extended even to maximum RPM – i.e. the situation where the manufacturer sets a ceiling on retail price. The economic (and other) absurdity of this rule was wonderfully set out by Judge Posner for the Court of Appeals in *Khan v. State Oil* (1996), who nevertheless continued:

Yet despite all its infirmities, its increasingly wobbly, moth-eaten foundations ... *Albrecht* has not been expressly overruled. ... *Albrecht* was unsound when decided, and is inconsistent with later decisions by the

⁸ More particularly, RPM *agreements* were held to be *per se* illegal under section 1 of the Sherman Act but, as clarified by the *Colgate* case of 1919, a ‘unilateral’ refusal by a manufacturer to deal with retailers undercutting pre-announced retail prices was not. However, the distinction is blurry in practice.

Supreme Court. It should be overruled. ... But all this is an aside. We have been told by our judicial superiors not to read the sibylline leaves of the U.S. Reports for prophetic clues to overruling. It is not our place to overrule *Albrecht*.

Taking Judge Posner's cue, the Supreme Court promptly did overrule *Albrecht*, in *State Oil v Khan* (1997).

Leegin makes women's accessories such as handbags and shoes, and sells them through retailers under its "Brighton" brand.⁹ It had a promotion policy requiring retailers selling Brighton goods to pledge to comply with its retail pricing policy. Retailer Kay's discounted below those prices, and Leegin suspended its supplies. Kay's sued Leegin for violation of section 1 of the Sherman Act. In its defense Leegin sought to introduce an economist's expert report, which concluded on the facts that Leegin's policy was pro-competitive. The district court, having regard to settled *per se* precedent, excluded the report as irrelevant. The jury found that the parties had entered into an agreement to fix retail prices, and so Leegin was found liable without the need for further inquiry. Damages of \$1.2 million were awarded to Kay's. Leegin got no joy from the Court of Appeals, but the Supreme Court granted *certiorari*. Oral argument is next Monday 26 March.

The amicus brief for the United States urges the Court to reverse *Dr Miles* so that RPM agreements are no longer *per se* illegal.¹⁰ So does an amicus brief filed by twenty-three leading US economists of industrial organization, of whom eight (Bresnahan, Froeb, Gilbert, A. Joskow, Ordovery, Scheffman, Shapiro, and Warren-Boulton) have served as senior economist at the DoJ or FTC.¹¹

The economists' brief denies that minimum RPM almost always produces anti-competitive effects. To the contrary, RPM can help align the incentives of manufacturers and retailers pro-competitively to the benefit of consumers – by promoting service

⁹ This summary is based on the amicus brief for the United States.

¹⁰ The brief is filed by the DoJ and FTC. The FTC was however divided 3-2, and Commissioner Harbour has taken the unusual step of writing an open letter to the Court dissenting.

¹¹ Professors Comanor and Scherer have also filed an *amicus* brief (in support of neither party) that argues for a dual approach in which RPM is (a) rebuttably *per se* illegal if retailer-induced, and (b) subject to rule-of-reason, with a first-stage structural test, if supplier-induced. Their recommendation is based on the view that efficiency benefits from RPM relate to (b) and not (a).

provision at retail level (the “free-rider” argument), by ensuring retailer contribution to product quality, and by supporting inventory investment in the face of demand uncertainty. The free-rider argument, in short, is that there are circumstances where consumers care not only about price but also about retail services that enhance product quality, for which it is impractical to charge separately and which carry no obligation to purchase. Without vertical restraints, retailers providing those services would be undercut by “free-riding” retailers that do not, and incentives to provide the services would be lacking. Vertical restraints, including RPM on occasion, can maintain incentives for such service provision. Inter-brand competition, if healthy, ensures that market incentives are to offer the price/quality offerings that consumers want.

The general point is that vertical restraints, including RPM, can enhance inter-brand competition without unduly diminishing intra-brand competition, including on price. And if inter-brand competition is manifestly abundant, what material harm to competition can come from RPM? It is true that minimum RPM can in some circumstances facilitate cartels of manufacturers or, as Basil Yamey (1952) documented long ago, of retailers, but by no means so often as to justify *per se* illegality – i.e. absolute and unconditional condemnation. Moreover, price and non-price vertical restraints, which are appraised under the rule of reason, require consistent treatment.¹² In short, the economists’ brief accords with Judge Posner’s crisp statement in *Khan v. State Oil* that most economists believe that neither maximum nor minimum RPM ‘is pernicious when the supplier is neither the cat’s paw of colluding distributors nor acting in concert with his competitors’.

By contrast the American Antitrust Institute has filed an amicus brief urging that the *Dr. Miles* rule be upheld.¹³ The brief emphasizes the importance of the principle of *stare decisis*, reviews the history of congressional interest in the ban on RPM agreements, and notes reliance on the rule by enforcement agencies. It argues that anti-competitive uses of RPM are significant, and that pro-competitive uses are not common or important,

¹² Eleanor Fox kindly referred me to the opinion of Justice White, concurring in part, in the 1977 *Sylvania* case that overruled the *per se* treatment of non-price vertical restraints in the 1967 *Schwinn* case. Justice White doubted the force of the majority’s distinction between price and non-price vertical restraints, and added that it called into question the established *per se* rule against price restraints.

¹³ So too have most States in a joint *amicus* brief.

especially compared to less restrictive alternative means of aligning retailer incentives. Decision theory implies that it is not just the relative frequency of pro- and anti-competitive consequences that matters to the assessment of a *per se* rule, but the severity of resulting harm in either case. Vertical agreements on price, says the brief, are sufficiently more harmful overall than non-price agreements to warrant different treatment under the law. Rule of reason cases are lengthy, costly and hard for plaintiffs to win. Other jurisdictions, including the EU, generally ban RPM. Finally, the brief argues that if the Court does overrule *Dr. Miles*, it should adopt a presumption of illegality rebuttable by demonstration that RPM was reasonably necessary to achieve a legitimate business purpose of benefit to consumers, which, if shown, would shift the burden of proof of anti-competitiveness back to the plaintiff.

US law is not EC law and even Supreme Court decisions have no direct impact on this side of the Atlantic. However, it may be time for a European reappraisal of the hard-core categorization of vertical price agreements, especially if *Dr. Miles* is reversed. Recall that Commission Regulation No 2790/1999 of 22 December 1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices states in Article 4 that the block exemption

shall not apply to vertical agreements which, directly or indirectly, in isolation or in combination with other factors under the control of the parties, have as their object:

(a) the restriction of the buyer's ability to determine its sale price, without prejudice to the possibility of the supplier's imposing a maximum sale price or recommending a sale price, provided that they do not amount to a fixed or minimum sale price as a result of pressure from, or incentives offered by, any of the parties; ...

This does not quite amount to *per se* illegality, because in theory exemption under Article 81(3) is still possible.¹⁴ However, as the Commission guidelines make clear, individual exemption of agreements containing such “hardcore” restrictions is unlikely. Likewise and furthermore, the Commission’s 2001 *de minimis* notice on agreements of

¹⁴ On point is the 1995 judgment of the European Court of Justice in the *Publishers Association* case, which overturned a Commission decision (upheld by the Court of First Instance) not to grant an exemption to the UK Net Book Agreement. The ECJ found that the Commission had not adequately considered the reasons why the national court had previously judged the NBA beneficial.

minor importance expressly excludes RPM, as a “hardcore” restriction, from the kinds of agreement between non-competitors that the Commission considers not to have an appreciably restrictive effect on competition.

There is a natural attraction to this approach, notwithstanding economic logic, while the US – the most mature competition law jurisdiction – condemns minimum RPM *per se*. If something is *per se* illegal “even” in the US, there may be felt to be automatic comfort with adopting a similar stance here. But what if the Supreme Court reverses *Dr. Miles*? The trans-Atlantic automatic comfort would then fall away. At least in those circumstances, reconsideration of the degree of hostility to RPM in EC competition law would seem appropriate.

I say that as no great fan of RPM. For example, I believe (though would like to see more empirical analysis) that the ending of RPM for books¹⁵ and for over-the-counter medicines in the UK has been pro-competitive and pro-consumer. Vertical agreements on price can most certainly have adverse horizontal effects and indeed be elements of trilateral agreements or concerted practices with horizontal operation. Thus horizontal issues were central to the OFT decisions about price-fixing of football shirts and of Hasbro toys and games, and to recently-concluded appeals of those matters in *Argos & Anor v OFT*. Vertical price agreements may well be worse in practice than in theory. But still, it remains hard to see how *per se* (or hardcore) treatment of RPM is justified in economic logic.

Vertical and horizontal agreements *are* fundamentally different. Without *some* (pre-existing or resulting) degree of market power, vertical agreements are generally not of competition concern. In the absence of collective enforcement, RPM does not seem *so* prone to cartel-facilitation to create a powerful presumption of market power from its very presence, especially if it practiced neither by a firm with substantial market share nor as part of a network of such agreements across much of a market. Efficiency rationales for RPM are not all spurious. The formal distinction between price and non-

¹⁵ The UK Net Book Agreement moreover provided for *collective* enforcement of RPM by publishers. Thus it was a horizontal agreement as regards enforcement. Given its horizontal aspect, there may well be a much stronger case for banning collective RPM than individual RPM. Indeed that was the position under the Resale Prices Act 1956.

price vertical agreements is not so large in terms of economic effect as to justify *radically* different treatment under the law.¹⁶ I recognize that policy considerations might trump these points, and that they are in reality unlikely to receive European attention unless *Dr. Miles* is reversed in the US. But if it is, the time might be ripe for a serious European debate about competition policy towards RPM.

A continuum from *per se* illegality to full rule-of reason?

I mentioned earlier that the amicus brief from the American Antitrust Institute in *Leegin* urges the Court to adopt a rebuttable presumption against RPM in the event that the *Dr. Miles* precedent is reversed. But is there any middle ground between *per se* illegality and full rule-of-reason?

The answer, at least for the US, appears to be Yes. A recent example is the *Polygram* case, better known as “The Three Tenors.” Polygram and Warner made a joint venture to distribute the three tenors recording from the 1998 World Cup. Later they also agreed that, around the time of the release of the 1998 recording, they would not advertise or discount the recordings from the 1990 World Cup (distributed by Polygram) and the 1994 World Cup (distributed by Warner). The FTC found the latter agreement illegal, though not *per se*, under section 5 of the FTC Act. The FTC’s approach was that for such an agreement there was a rebuttable presumption of illegality. An adequate pro-competitive justification for it had not been established, so with no need for elaborate market analysis, the finding of illegality could be made.

The FTC decision drew criticism, including Victor Goldberg’s enjoyable paper, sub-titled *La Triviata*, which begins:

Picture this. Luciano Pavarotti, Placido Domingo, and Jose Carreras are in a recording studio preparing to record yet another “Three Tenors” album. The orchestra is tuning up, the singers are going over the music, when suddenly in burst the Antitrust Police. The three are carted away in handcuffs for conspiring to combine their unique talents in restraint of trade. “Had they not combined in this manner,” intoned the commissioner, “there could have been three recordings, not one”.¹⁷

¹⁶ ‘Since price and non-price vertical restraints can have similar economic effects, parity of treatment would seem desirable’: Hay and Vickers (1988, page 64).

¹⁷ Goldberg (2005, page 56).

The FTC decision was appealed, but upheld by the Court of Appeals. Judge Ginsburg, writing for the Court, noted how, since the late 1970s

the Supreme Court has steadily moved away from the dichotomous approach – under which every restraint of trade is either unlawful *per se*, and hence not susceptible to a procompetitive justification, or subject to full-blown rule-of-reason analysis – toward one in which the extent of the inquiry is tailored to the suspect conduct in each particular case.

The move has not been to a trichotomy, with an intermediate “quick look” category, but “away from any reliance on fixed categories towards a continuum.” It will be most interesting to see where in such a framework the Supreme Court places RPM in the *Leegin* case.

Another recent Supreme Court case of some interest in this context is *Illinois Tool Works*. The case concerned the tying of ink to printers, where the tying product was patented. Years ago, tying was widely *per se* illegal in the US, but, as the judgment explains:

Over the years, however, this Court’s strong disapproval of tying arrangements has substantially diminished. Rather than relying on assumptions, in its more recent opinions the Court has required a showing of market power in the tying product.

Thus in the 1984 case *Jefferson Parish*, concerning hospital services, the Court explained that condemnation of tying arrangements depended on market power, but added that market power could be presumed if the tying product were patented. In *Illinois Tool Works*, however, the Court concluded that the mere fact that a tying product is patented does not support any presumption of market power. As to the influence of economics, the Court noted that:

It is no doubt the virtual consensus among economists that has persuaded the enforcement agencies to reject the position that the Government took when it supported the *per se* rule that the Court adopted in the 1940’s.

Thus there has been a shift from condemnation of tying *tout court* to conditional condemnation (“qualified *per se*”), with the conditions evolving over time. The

categories are not simply (unqualified) *per se* and rule-of-reason (without any presumptions).

Are there EC instances of such modification over time? The September 2006 judgment of the Court of First Instance in *GlaxoSmithKline* may well be of interest in this regard. The case concerned restrictions on parallel trade in GSK's general sales conditions for certain medicines in Spain. GSK's arrangements with its distributors were held to constitute agreements, so the question fell to be decided under Article 81. Limitations on parallel trade may be thought to be "hardcore," yet the judgment at paragraph 119, referring to prior case law, eschews formalism, saying:

the application of Article 81(1) EC to the present case cannot depend solely on the fact that the agreement in question is intended to limit parallel trade in medicines or to partition the common market, which leads to the conclusion that it affects trade between Member States, but also requires an analysis designed to determine whether it has as its object or effect the prevention, restriction or distortion of competition on the relevant market, to the detriment of the final consumer. ... [T]hat analysis, which may be abridged when the clauses of the agreement reveal in themselves the existence of an alteration of competition ... must, on the other hand, be supplemented, depending on the requirements of the case, where that is not so.

So such restrictions are not *per se* illegal, but abridged analysis may in some circumstances suffice. After analysis, the Court concluded that the Commission had been entitled to find that the agreements had anti-competitive effect within the meaning of Article 81(1), or as put in paragraph 190: "the effect of reducing the welfare of final consumers." However, after further analysis the Court found that the Commission had too readily rejected GSK's arguments for exemption under Article 81(3).

More generally, this CFI judgment is notable for its rejection of formalistic argument¹⁸ and its many references, illustrated above, to consumer welfare. May this portend greater convergence between economics and competition law in Europe?

¹⁸ In this respect it echoes the opinion of Advocate General Jacobs in the Article 82 case concerning GSK's policies in Greece.

Conclusion

An over-simplified summary of the viewpoint offered in this lecture would have three propositions. First, for cartels and mergers there is broad trans-Atlantic convergence of policy, and law and economics are in tune. Second, for abuse of dominance the Atlantic remains wide, with many economists afloat somewhere in the middle. Third, for vertical agreements on price, there has been trans-Atlantic harmony of law, but not between law and economics. But that will change if the Supreme Court reverses *Dr. Miles* in its *Leegin* opinion.

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