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The election of the new democratic administration in the United States in November 2008 was overwhelmingly greeted in Europe as an opportunity to reinforce transatlantic cooperation and convergence in competition law and policy. This study evaluates the plausibility of greater convergence between EC competition law and U.S. antitrust law in a number of areas: single-firm conduct, vertical contractual restraints, mergers, and state action (state subsidies).

I. INTRODUCTION

It has been observed, even by American lawyers and economists, that there have been different cycles, both in antitrust doctrine and enforcement, as practiced by the Antitrust Authorities (Department of Justice, "DoJ", and the Federal Trade Commission, "FTC") and the courts. In the last twenty years, these cycles have had some overlap with administration types: a more pro-business approach by the Republicans and a more pro-consumer approach by the Democrats.¹ There has been a clear continuity in enforcement

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¹ The "pendulum swings" metaphor identified, e.g., by Jonathan Baker and Carl Shapiro, *Detecting and Reversing the Decline in Antitrust Merger Enforcement*, 22(3) ANTITRUST (Summer 2008). This has been criticized by William Kovacic, *The Modern Evolution of US Competition Policy Enforcement Norms*, 71 ANTITRUST LAW JOURNAL 377 (2004).

in the areas of naked horizontal price-fixing and market division. The area of single-firm conduct, however, has experienced some noticeable swings, with merger enforcement being an intermediate area that showed doctrinal continuity but also experienced substantial ups and downs in activity— decreasing during the second term of the Reagan administration and the George W. Bush administration.

While the European Commission has also had different commissioners holding the reins of antitrust policy and enforcement, it is more difficult to detect any difference in the EC ideological approach to antitrust, since there are no divisions across party line nor is it a directly-elected body. It is important to take into account the mutual influence that developments on each side of the Atlantic may have had on antitrust policy. In particular, it is clear that the reform of the European antitrust policy instituted by the European Commission in the late 1990s has been influenced by the development of a more active, yet economically sound, antitrust agenda in the United States, largely inspired by post-Chicago antitrust economics.² One could also advance the theory that the recent Guidance paper of the European Commission on Article 82³ may never have seen the light of day, had the DOJ not published a report on single-firm conduct under Section 2.⁴

² Ioannis Lianos, *La transformation du droit de la concurrence par le recours à l'analyse économique* (Bruylant, 2007).

³ European Commission, GUIDANCE ON THE COMMISSION'S ENFORCEMENT PRIORITIES IN APPLYING ARTICLE 82 EC TREATY TO ABUSIVE EXCLUSIONARY CONDUCT BY DOMINANT UNDERTAKINGS, COM(2008) available at <http://ec.europa.eu/competition/antitrust/art82/guidance.pdf> (hereinafter Guidance).

⁴ U.S. DOJ, COMPETITION AND MONOPOLY: SINGLE-FIRM CONDUCT UNDER SECTION 2 OF THE SHERMAN ACT, 2008 available at <http://www.usdoj.gov/atr/public/reports/236681.pdf>, (hereinafter DoJ Report).

The election of the new democratic administration in the United States in November 2008 was overwhelmingly greeted in Europe as an opportunity to reinforce the transatlantic cooperation and convergence in competition law and policy in a number of areas:

First, mainstream European competition law tradition has always felt closer to the more antitrust interventionist (post-Chicago inspired) policies of the Clinton administration—in particular with regard to unilateral conduct of dominant firms—than to the sparse public enforcement of Section 2 of the Sherman Act during the incumbent Republican administration as well as the overly cautious approach in enforcing Section 2 of the Sherman Act advocated in the DOJ single-firm conduct report. In contrast, during the last eight years, we have witnessed more convergence between the two sides of the Atlantic in cartel enforcement—the Republican administration has been active in criminal antitrust enforcement in this area.⁵ On the other side of the Atlantic, the European Commission has imposed considerable fines on cartels⁶ and adopted a cartel settlement procedure,⁷ while some EU Member States have adopted criminal sanctions for cartels as well as increasingly sophisticated leniency policy notices that improve the effectiveness of cartel enforcement.⁸ Convergence in the area of cartels will certainly continue. A more

⁵ See, Scott B. Hammond, *Recent developments, Trends and Milestones in the Antitrust's Division Criminal Enforcement Program*, March 26, 2008, available at <http://www.usdoj.gov/atr/public/speeches/232716.htm>

⁶ See statistics on fines imposed (2003-2008) at <http://ec.europa.eu/competition/cartels/statistics/statistics.pdf>

⁷ See, <http://ec.europa.eu/competition/cartels/legislation/settlements.html>

⁸ See, most recently, the revised OFT GUIDANCE NOTE ON LENIENCY AND NO-ACTION (December 2008), available at http://www.of.gov.uk/shared_of/reports/comp_policy/oft803.pdf

questionable issue is the possibility for more convergence regarding the enforcement policy for Section 2.

Second, one of the most important questions with regard to vertical contractual restraints will be how the Commission will approach Resale Price Maintenance agreements ("RPM") in its revision of the regulation and guidelines on vertical restraints. The transatlantic dialogue could certainly profit from the decision of the Supreme Court on the *Leegin* case, along with the positions taken by the majority and the dissenting minority.

Third, we want to emphasize the good cooperation between the American and EU authorities on merger enforcement and we expect an increase in U.S. enforcement of horizontal and vertical mergers, thus avoiding cases like *GE-Honeywell*.

Fourth, the ongoing financial and economic crisis is still the overwhelming preoccupation of both sides of the Atlantic. So far, both sides have learned from experiences in each area, but we need to avoid the mistakes made during the Great Depression, when competition policy was put on the back-burner and structural policies that could strengthen long-term growth were not adopted. Finally, we will briefly refer to some problems in the area of state action and state aids.

II. SINGLE-FIRM CONDUCT

A. The Big Picture: The "Towards More Convergence" Hypothesis

The debate over the interpretation of Article 82 EC ("Article 82") has been raging for some time now.⁹ Encouraged by the successfully accomplished reform of Article 81

⁹ European Commission, DG Competition, DISCUSSION PAPER ON THE APPLICATION OF ARTICLE 82 OF THE TREATY TO EXCLUSIONARY ABUSES (hereinafter Discussion Paper), December 2005, available at

EC as well as of the EC merger control regulation, the European Commission initiated a review of Article 82 with the aim of introducing a more economic-oriented approach. An essential component of this call for reform was the opposition to the current “form-based approach” allegedly followed in Article 82. Proponents of the Article 82 reform advocate an “effects-based approach,” which would focus “on the presence of anticompetitive effects that harm consumers, based on the examination of each specific case, on sound economics and grounded on facts.”¹⁰ This is presented in opposition to the “form-based” approach which grants excessive weight to the nature of the conduct of the dominant firm and to specific, essentially precedent-based, categories of abuses.

To this distinction between form-based and effects-based approaches, one could also add the different beliefs that seem to influence competition law enforcers on each side of the Atlantic. William Kovacic rightly observed that

(i)n their technical findings and in their attitude, modern U.S. Supreme Court’s decisions in cases such as Brooke Group, Trinko and Weyerhaeuser have demonstrated greater skepticism about abuse of dominance claims than judicial decisions in matters such as France Telecom/Wanadoo, Michelin II and British Airways. EU decisions in IMS Health and Microsoft show a greater inclination to condemn refusals to deal than modern U.S. rulings such as Trinko. Unlike Brooke Group and Weyerhaeuser, the France Telecom/Wanadoo decision rejects the need to apply a recoupment test to resolve allegations of exclusionary pricing. A finding of dominance can occur in the European Union at or somehow below a 40 per cent market share, while the U.S. offence of attempted monopolization usually treats shares below 50 per cent as being inadequate to establish substantial market power.¹¹

<http://ec.europa.eu/comm/competition/antitrust/art82/discpaper2005.pdf> The Discussion paper is a consultation document, prepared by the staff of the DG Competition.

¹⁰ Report by the EAGCP, *An Economic Approach to Article 82*, July 2005, available at http://ec.europa.eu/competition/publications/studies/eagcp_july_21_05.pdf , at 2.

¹¹ William E. Kovacic, *Competition policy in the European Union and the United States: convergence or divergence in the future treatment of dominant firms?*, 8 COMPETITION LAW INTERNATIONAL, at 11 (October 2008).

The recent DoJ Report on single-firm conduct exacerbates these differences by adopting an overly cautious approach in the enforcement of Section 2. The Antitrust Division of the DoJ wants to develop different tests for different types of conduct, “depending upon, among other things, the scope of harm implicated by the practice; the relative costs of false positives, false negatives, and enforcement; the ease of application; and other administratibility concerns.”¹²

Giving a larger weight to the cost of false positives than false negatives and advocating the definition of “safe harbors” for firms with monopolist power, the DoJ Report also recommends the application of a disproportionality test as the default standard for the enforcement of Section 2. This test is essentially a cost-benefit analysis test which gives considerably more weight to pro-competitive effects than to anticompetitive effects:

conduct that potentially has both pro-competitive and anti-competitive effects is anti-competitive under section 2 if its likely anti-competitive harms substantially outweigh its likely pro-competitive benefits.¹³

This bias in favor of defendants may, first, be explained by the higher risk of private antitrust litigation and the procedural specificities of the U.S. enforcement system. Donald Baker rightly observes that “the central role given to private plaintiffs and juries in the United States has understandably bred long-term caution about reading Section 2 expansively.”¹⁴ The “risk of private litigation” may well explain the asymmetry of the

¹² DoJ Report, at 46.

¹³ *Ibid*, at 45.

¹⁴ Donald I. Baker, *An Enduring Antitrust Divide Across the Atlantic Over Whether to Incarcerate Conspirators and When to Restrain Abusive Monopolists*, Speech, NYU Law, October 17, 2008, on file with the author.

standard of proof. The relatively short history of private litigation in Europe and the filtering role of the European Commission in the context of public enforcement show that this risk is far lesser in Europe.¹⁵

Second, risk perception could also relate to the prior attitudes of U.S. antitrust enforcers in favor of defendants. As explained in a different context by Beckner and Salop, decision makers may be risk-neutral or risk-averse: Risk-neutral decision makers weigh “potential harms equally with potential benefits,” while risk-averse decision makers “would even reject conduct with a higher expected value in light of the significant downside risk;” in other words, they will give additional weight to potential harms.¹⁶ In this context, risk can be understood as uncertainty over the effects of the decision as to both present and future cases.¹⁷ The fact that decision makers give more weight to anticompetitive effects than to efficiency gains may indicate they are risk-averse to possible false negative errors. The asymmetry between the weight attached to anticompetitive effects and pro-competitive effects indicates that the DOJ is risk-averse to false positives regarding the enforcement of Section 2 of the Sherman Act. A risk-neutral decision maker would have given the same weight to both effects.

If the first reason is likely to influence public antitrust enforcement in an Obama administration, the question remains open with regard to the second reason explaining the

¹⁵ See, J. Thomas Rosch, *I Say Monopoly. You Say Dominance: the Continuing Divide on the Treatment of Dominant Firms: Is it Economics?*, FTC, Sept. 8, 2007, available at <http://www.ftc.gov/speeches/rosch/070908isaymonopolyiba.pdf>

¹⁶ C. Frederick Beckner III & Steven C. Salop, *Decision Theory and Antitrust Rules*, 67 ANTITRUST L J 41 (1999)

¹⁷ Although the concepts of risk and that of uncertainty are not, in theory, similar, risk being considered as measurable uncertainty while uncertainty cannot, by definition, be measured [see FRANK H. KNIGHT, *RISK, UNCERTAINTY AND PROFIT*, 25 (1921)]; in this context the two terms will be used interchangeably.

over-cautious public antitrust enforcement of the George W. Bush administration. Some authors have advanced the view that the current U.S. antitrust policy is heavily inspired by Chicago economics antitrust principles, while European antitrust policy is inspired by more interventionist post-Chicago economics.¹⁸ One could expect that the Obama administration will depart from the pro-defendant rhetoric of Chicago economics, thus opening room for greater convergence with EC competition law.¹⁹

One could speculate that the Obama administration will not adopt the recommendations of the DOJ single-firm conduct report and that it will advance a more active agenda of public enforcement of Section 2,²⁰ precisely because it will be less risk-averse for false positives. This is linked to the broader economic philosophy of the Obama administration.²¹ It remains an open question as to what would be the economic underpinnings of the Section 2 antitrust policy in this case: would it be a return to the post-Chicago industrial economics times of the Clinton administration or would it be a shift to some type of behavioral law and economics/empirical economics approach?²² The Obama administration will need, in any case, to deal with the conservative antitrust

¹⁸ J. Thomas Rosch, *The Challenge of non-Horizontal Merger Enforcement*, FTC Speech, Sept. 27-28, 2007 available at <http://www.ftc.gov/speeches/rosch/070927-28non-horizontalmerger.pdf>

¹⁹ Which seems, according to John Vickers, *Competition Law and Economics: a Mid-Atlantic Viewpoint*, 3(2) GCP MAGAZINE (Mar-07), to be the post-Chicago synthesis.

²⁰ See, D. Daniel Sokol, "Change and Continuity in International Antitrust under an Obama Administration", 1(2)GCP MAGAZINE (Jan-09) at 4-5.

²¹ See, Barack Obama, *Statement of President-elect Barack Obama for the American Antitrust Institute*, ¶3 (2007), http://www.antitrustinstitute.org/archives/files/aai-%20Presidential%20campaign%20-%20Obama%209-07_092720071759.pdf

²² See, Maurice E. Stucke, *New Antitrust Realism*, 1(2)GCP MAGAZINE (Jan-09).

jurisprudence of the Supreme Court.²³ This will certainly affect all policy areas, not only antitrust law.²⁴

The situation is the reverse in the EU context, where the European Commission promotes a more cautious—in terms of antitrust intervention—agenda than the European judiciary by using its capacity to adopt guidelines that often more creatively interpret case law of the European courts (Court of First Instance "CFI" and European Court of Justice "ECJ").²⁵ In general, however, the European approach to single-firm conduct is more restrictive, for dominant firms, than the U.S. antitrust approach. One of the most important reasons for a more active antitrust enforcement is certainly a different institutional background and history. For example, public enterprises and state monopolies have played a major role in Europe.²⁶ In fact, the process of liberalization is still under way in several sectors. The recently published EU guidance on the Commission's enforcement priorities on Article 82 EC (hereinafter Guidance)

²³ There are currently two cases pending at the Supreme Court: *Pacific Bell Telephone Company et al., Petitioners v. LinkLine Communications, Inc.* (Docket 07-512); *Federal Trade Commission, Petitioner v. Rambus Incorporated* (Docket 08-694).

²⁴ Ronald Dworkin, *The Supreme Court Phalanx: The Court's New Right Wing Bloc*, NEW YORK REVIEW OF BOOKS (2008).

²⁵ On the many functions and influence of guidelines, including creative interpretation, see Hillary Greene, *Guideline Institutionalization: the Role of Merger Guidelines in Antitrust Discourse*, 48 WILLIAM & MARY L REV 771 (2006).

²⁶ This is a factor that may explain the low standard of proof for anticompetitive effects in some recent cases involving former state monopolies or firms with exclusive rights: E.g. *Case T-271/03, Deutsche Telekom AG v. Commission* [2008], para 237; *European Commission, Case COMP/38.784-Wanadoo España vs. Telefónica* [2007] available at http://ec.europa.eu/comm/competition/antitrust/cases/decisions/38784/dec_en.pdf, para 304, 309 & 625.

nevertheless adopts an effects-based approach in interpreting Article 82 EC, thus signaling a willingness to create a greater convergence with U.S. antitrust law.²⁷

B. Taking A Closer Look: The “Towards More Convergence” Hypothesis Tested

The EU Commission guidance on Article 82’s objective is to set enforcement priorities that will guide the Commission’s action in applying Article 82 to exclusionary conduct. It does not constitute a statement of the law of Article 82, which is, according to the EC Treaty, interpreted by the jurisprudence of the ECJ and the CFI.²⁸ The document indicates the European Commission's intention to creatively interpret existing case law of the European Courts, stretching its content to render it more compatible with an approach based on game theory and neoclassical economics. The old clothing of Article 82 EC, which includes concepts such as the special responsibility of dominant firms or that of obligatory trading partner, are still important references but are simultaneously put in a more “modern,” consumer interest-oriented shape.

The focus of Article 82 is on consumer harm, defined broadly as covering all practices restricting competition in the form of higher prices, lower innovation, and/or

²⁷ The guidance is a softer law instrument than guidelines: it is complementary to the Commission’s specific enforcement decisions. The Commission could not have adopted guidelines contrary to the rulings of the European courts. The choice of the instrument of guidance on enforcement priorities offers to the Commission more leeway in presenting its approach for Article 82. The Commission maintains the ability to reject a complaint when it considers that a case lacks priority for other reasons (e.g. lack of Community interest).

²⁸ Guidance, para 3; See also, Opinion of Advocate General Kokott, Case C-95/04 P, *British Airways v. Commission* [2007] ECR I-2331, para 28, “it is immaterial how the Commission intends to define its competition policy with regard to Article 82 EC *for the future*. Any reorientation in the application of Article 82 EC can be of relevance only for future decisions of the Commission, not for the legal assessment of a decision already taken. Moreover, even if its administrative practice were to change, the Commission would still have to act within the framework prescribed for it by Article 82 EC as interpreted by the Court of Justice.”

narrower consumer choices. The Commission’s approach is impressionistic: sometimes the guidance refers to consumer harm, other times to consumer welfare: no definition is provided.²⁹ The ECJ has yet to explain its conception of consumer harm. The concept of dominant position is given a convenient economic alter ego—that of substantial market power—with the emphasis being on the ability of dominant firms to ignore competitive constraints rather than on a more structured interpretation of such indicators as market share and barriers to entry.³⁰ The concept of anticompetitive foreclosure epitomizes the importance of “the impact on consumer welfare” of the conduct.³¹

Qualitative as well as quantitative evidence of likely “consumer harm” is required. The recent decisions of the European Commission illustrate the increasing importance of empirical economic evidence when determining anticompetitive effects.³² The approach is not different from that advocated in the recent non-horizontal merger guidelines of the European Commission. A counterfactual test for the relevant market will compare the actual or likely future situation following the dominant undertaking’s market conduct in the absence of the conduct in question or with another realistic business alternative.³³

²⁹ Yannis Katsoulacos, *Comments on the Commission’s Guidance Paper on Article 82 E.C.*, December 2008, available at <http://www.cresse.info/default.aspx?articleID=12578&heading=>, point 1.

³⁰ Guidance, para 11.

³¹ Guidance, para 19-20.

³² See, Case COMP/38.784-Wanadoo España vs. Telefónica [2007] available at http://ec.europa.eu/comm/competition/antitrust/cases/decisions/38784/dec_en.pdf, Part VI, where the Commission examined empirical evidence in order to substantiate the anticompetitive effects of the alleged margin squeeze.

³³ Guidance, para 20.

The guidance paper introduces a sharp dichotomy between price and non-price exclusionary conduct. Only the exclusion of competitors as efficient as the dominant firm will trigger antitrust intervention.³⁴ Certainly, the Commission recognizes that

in certain circumstances a less efficient competitor may also exert a constraint which should be taken into account when considering whether a particular price-based conduct leads to anticompetitive foreclosure³⁵

but this possibility is given less weight than was previously given in the 2005 DG Comp Staff Discussion paper.³⁶

This is also a debated issue in U.S. antitrust law, with many authors taking positions in favor of antitrust intervention, even if less efficient competitors are excluded.³⁷ These authors believe that in a network sector or a sector characterized by substantial “learning-by-doing” or marketing-branding effects we cannot expect an entrant to be as efficient as an incumbent. Following the adoption of an efficiency test, the Commission applies a cost-based standard for all pricing abuses,³⁸ including bundled rebates.³⁹ This seems, at first sight, similar to the position of the DoJ Report and some

³⁴ Guidance, para. 26.

³⁵ Guidance, para 23. Note that this possibility is not taken into account at the first step of the competition assessment, the cost-based test (which operates basically as a filter for) but during the second step of the analysis, the existence of an anticompetitive foreclosure.

³⁶ Discussion paper, para 67, which included it as a possible exception to the operation of the cost-based test.

³⁷ E.g. Steven C. Salop, *Exclusionary Conduct, Effect on Consumers, and the Flawed Profit-Sacrifice Standard*, 73 ANTITRUST L.J. 311, 328 (2006); Einer Elhauge, *Loyalty Discounts and Naked Exclusion* (Harvard Law & Econ. Discussion Paper No. 608, 2008), *abstract available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1093749 (remarking that “the equally efficient rival test misses the point that sometimes the loyalty discounts will create anticompetitive effects by making the rival less efficient”).

³⁸ Guidance, para 24.

³⁹ Guidance, para 59.

U.S. courts of appeal.⁴⁰ This convergence with the EU and the United States on assessment of rebates is clear if one reads their submissions in the most recent OECD Policy roundtable on rebates.⁴¹

The Commission is essentially advocating a safe harbor for “conditional rebates,”⁴² when the “effective price” over the “relevant range,” (which could be either the incremental purchases for incremental rebates or the contestable share (portion) for retroactive rebates), remains consistently above the Long Run Average Incremental Costs (“LRAIC”) of the dominant undertaking.⁴³ This would normally allow an equally efficient competitor to profitably compete notwithstanding the rebate. If the effective price is between Average Avoidable Costs (“AAC”) and LRAIC, the Commission will proceed to a more detailed competition law assessment. If the effective price is below AAC, which is the cost benchmark for predatory pricing,⁴⁴ there is a presumption of anticompetitive foreclosure.⁴⁵ The Commission also adopts the lower predatory standard (prices below AAC) as the threshold for bundled rebates—if the dominant undertakings’

⁴⁰ E.g. *Concord Boat Corp. v. Brunswick Corp.*, 207 F.3d 1039, 1061-62 (8th Cir. 2000); *Virgin Atl. Airways Ltd. v. British Airways PLC*, 257 F.3d 256, 266-69 (2d Cir. 2001); *Cascade Health Solutions v. PeaceHealth*, 515 F.3d 883, 894-903 (9th Cir. 2007).

⁴¹ OECD, Policy Roundtable, Fidelity and Bundled Rebates and Discounts, 2008, available at <http://www.oecd.org/dataoecd/41/22/41772877.pdf>

⁴² These are defined in the Guidance (para 36) as “rebates granted to customers to reward them for a particular form of purchasing behaviour.” This definition seems to include in the category single-product as well as bundled discounts that provide the customer a rebate if its purchases over a defined reference period exceed a certain threshold. These rebates have effects similar to exclusive purchasing obligations but more attenuated. They should be distinguished from unconditional bundled discounts, which have effects similar to tying and are subject to a different test (Guidance, para 58-60). In contrast, the OECD report and some national submissions do not make this distinction and group all forms of bundled rebates and loyalty-inducing single product rebates under the category of “conditional discounting” (see OECD, Policy Roundtable, at 7; see also, the submission of the United Kingdom, at 121).

⁴³ Guidance, para 42.

⁴⁴ Guidance, para 63.

⁴⁵ Guidance, para 23-26 & para 40-43.

competitors are selling identical bundles or could do so in a timely way without being deterred by possible additional costs—which is also similar to the standard suggested by the DOJ Single-firm conduct report.⁴⁶

The DOJ Single-Firm conduct report embraces an equivalent cost-based safe harbor. Where bundle-to-bundle competition is not possible, the DOJ suggests a discount allocation safe harbor that will compare the dominant's firm cost for the competitive product in the bundle to the "inputted" price of that product, i.e. the price after allocating to the competitive product all discounts and rebates attributable to the entire bundle. The discount could fall within the scope of Section 2 only if the plaintiff shows that the defendant sold the competitive product at an inputted price that was below the product's incremental costs.⁴⁷ In comparison, the American Antitrust Institute ("AAI"), a liberal think tank advancing a more active antitrust enforcement agenda for Section 2, rejects in its transition report a cost-based safe harbor for bundle rebates, more in accordance with recent game theory and the case law of some other circuits.⁴⁸

The next administration should reject cost-based safe harbors for loyalty and bundled discounts by dominant firms and support a structured rule of reason that would allow plaintiffs to establish that such discounts are *prima facie* exclusionary under certain conditions.⁴⁹

⁴⁶ Guidance, para 60 & footnote 38; DoJ Report, at 101.

⁴⁷ DoJ Report, at 101-102. The Antitrust Modernization Commission's Report provides for an additional condition, as it requires from the plaintiff to prove that the defendant is likely to recoup these short-term losses: AMC Report, at 99.

⁴⁸ E.g. *SmithKline Corp v. Eli Lilly & Co.*, 575 F.2d 1056 (3rd Cir. 1978); *LePage's Inc. v. 3M*, 324 F.3d 141 (3d Cir. 2003); *United States v. Dentsply Int'l, Inc.*, 399 F.3d 181 (3d Cir. 2005).

⁴⁹ American Antitrust Institute, *Transition Report on Competition Policy to the 44th President*, Oct. 6, 2008, available at <http://www.antitrustinstitute.org/archives/transitionreport.ashx>, at 71 (hereinafter, AAI Transition Report).

The position of the Guidance paper on predatory pricing gets closer to the Brooke Group⁵⁰ standard in the United States than to older ECJ and CFI precedents, at least as currently interpreted. The competition assessment includes two steps. First, the plaintiff needs to establish the existence of a sacrifice, which may be either charging prices below AAC or earning revenues lower than would have been expected from a reasonable alternative conduct (for example, the dominant undertaking incurred a loss that it could have avoided).⁵¹ Second, the Commission will apply an "as efficient as competitor" test in order to determine if the conduct is capable of harming consumers.⁵² There is a presumption of anticompetitive foreclosure if the dominant undertaking prices below LRAIC, but the Commission takes into account a number of factors. These include the likelihood that rivals will compete, the existence of a benefit for the dominant company after the predatory conduct in the form of greater market power (a stealth recoupment test), or the possibility of delaying entry and the decline in prices that would otherwise have occurred by creating entry barriers.⁵³ The Commission is also open to considering efficiency gains, even if it recognizes that the defense is unlikely to succeed in predatory pricing cases.⁵⁴

The test is a long way forward, in terms of modern economic orthodoxy, from the standard developed by the ECJ in *Akzo*⁵⁵ as well as that developed by the CFI in *France*

⁵⁰ Brooke Group Ltd. v. Brown & Williamson Tobacco Corp, 509 U.S. 209 (1993).

⁵¹ Guidance, para 63-64.

⁵² Guidance, para 66.

⁵³ Guidance, para 67-69.

⁵⁴ Guidance, para 73.

⁵⁵ Case C-62/86, AKZO Chemie Bv v. Commission [1991] ECR I-3359.

Télécom/Wanadoo.⁵⁶ If it is followed by the Court, the recent opinion of Advocate General Mazák in *France Télécom* that proof of recoupment is essential in a predatory pricing case under Article 82 may signal a new era of convergence between EC and U.S. competition law on predatory pricing claims.⁵⁷

The CFI echoed the dichotomy between price/non-price abuses in *Deutsche Telekom*, a case involving margin squeeze.⁵⁸ Following the Commission's position, in order to determine if the pricing practices were abusive, the Court chose to emphasize the likelihood that the dominant undertaking's pricing practices would remove from the market an economic operator that was just as efficient as the dominant firm.⁵⁹ The CFI cited inter alia the case law of the ECJ in *Akzo* as an authority for the proposition that

the abusive nature of a dominant undertaking's pricing practices is determined in principle on the basis of its own charge and costs, rather than on the basis of the situation of actual or potential competitors.⁶⁰

Issues of administrability and predictability mainly explain this choice:

any other approach could be contrary to the general principle of legal certainty. If the lawfulness of the pricing practices of a dominant undertaking depended on the particular situation of competing undertakings, particularly their cost structure—information which is generally not known to the dominant undertaking—the latter would not be in a position to assess the lawfulness of its own activities.⁶¹

⁵⁶ Case T-340/03, *France Télécom SA v. Commission* [2007] ECR II-107.

⁵⁷ AG Mazák, Case C-202/07P, *France Télécom SA v. Commission* (September 28, 2008), para 56-64.

⁵⁸ Case T-271/03, *Deutsche Telekom / Commission*, April 10, 2008, available at <http://www.curia.eu>

⁵⁹ Case T-271/03, above, para. 187 & 199 available at <http://www.curia.eu>. See also, Case T-5/97, *Industrie des poudres sphériques SA v. Commission* [2000] ECR II-3755, para 180.

⁶⁰ Case T-271/03, above, para. 188.

⁶¹ *Ibid.*, para 192.

In other parts of the judgment, the CFI was less clear regarding the choice of an adequate benchmark to assess the efficiency of the competing undertakings. It simply indicated that the legality of the dominant's firm practice is determined on the basis not only of its own costs but that the situation of rival companies could also serve as a relevant benchmark.⁶² The Guidance paper is more explicit as to the adequate benchmark: this is the LRAIC of the downstream division of the integrated dominant firm. Only when it is not possible to clearly allocate the dominant firm's costs to downstream and upstream operations will the LRAIC of a nonintegrated competitor downstream be used.⁶³

It is interesting to note that the Commission's Guidance establishes a parallel between the margin squeeze doctrine and that of refusals to deal: both are treated under the same chapter and as essentially practices that are substitutable for dominant firms.⁶⁴ In *Industrie des poudres sphériques* ("IPS") the CFI recognized that a margin squeeze abuse could take place if there was a disproportion between an upstream and a downstream price, without any need to demonstrate that either the wholesale price was excessive in itself or that the retail price was predatory in itself.⁶⁵

⁶² Ibid. para 198, where the CFI emphasizes the need to provide equal opportunities to the various economic operators, in particular if the later have different costs and revenue structures. See, Simon Gevenaz, *Margin Squeeze after Deutsche Telekom*, 5(1)GCP MAGAZINE 21-23 (May 2008) (hereinafter *Margin Squeeze*).

⁶³ Guidance, para 79.

⁶⁴ Guidance, part D.

⁶⁵ Case T-5/97, *Industrie des poudres sphériques SA v. Commission*, [2000] ECR II-3755, para 179 ; See also Case T-271/03, *Deutsche Telekom AG v. Commission* [2008] nyr, para. 167 ; Case COMP/38.784-Wanadoo España v. Telefónica [2007] available at http://ec.europa.eu/comm/competition/antitrust/cases/decisions/38784/dec_en.pdf , para 283.

The approach followed in EC competition law may be contrasted to the position of some U.S. courts and commentators that margin squeeze should not constitute an independent doctrine of antitrust liability.⁶⁶ The existence of Article 82(b) and the fact that “unfair” prices could be found abusive under EC competition law may be an explanation for this divergence of approach. An alternative is to treat “margin squeeze” as predatory pricing using both an upstream and downstream price. The case law of the European courts has not, however, been clear until now on the relationships among the doctrines of margin squeeze, refusal to deal, and predatory pricing. This question may not arise in situations where the dominant undertaking has a regulatory duty to deal, but may be an important issue in all other cases. It is possible to argue that the plaintiff in a margin squeeze case should provide evidence that access to the upstream input was indispensable for rivals and, more generally, for effective competition in the downstream level.⁶⁷ After all, a firm that has the ability to refuse to deal should also be able to decide to deal on unattractive terms. Other authors advance, nevertheless, the view that margin squeeze case law is less concerned with the ‘indispensable’ nature of the relevant upstream input than with the existence of alternative upstream supplies at competitors’ disposal that could allow them to compete.⁶⁸

⁶⁶ See, Gregory Sidak, *Abolishing the Price Squeeze as a Theory of Antitrust Liability*, 4 JOURNAL OF COMPETITION LAW AND ECONOMICS 279-309 (2008); Dennis W. Carlton, *Should ‘Price Squeeze’ be a Recognized Form of Anticompetitive Conduct?*, 4 JOURNAL OF COMPETITION LAW AND ECONOMICS 271-278 (2008); *Covad Communications Company v. Bell Atlantic Corp.*, 398 F.3d 666 (D.C. Cir. 2005). See however, *Linkline Communications, Inc. v. SBC California, Inc.*, 503 F.3d 876 (9th Cir. 2007), accepting antitrust liability for margin squeeze. The Supreme Court has granted certiorari and its decision is eagerly expected.

⁶⁷ See, Robert O’ Donoghue, *Regulating the Regulated: Deutsche Telekom v. European Commission*, 5(1) GCP MAGAZINE 19 (May 2008), referring to Case T-271/03, para. 237 where the CFI observes that (“(h)aving regard to the fact that the applicant’s wholesale services are thus indispensable to enabling a competitor to enter into competition with the applicant on the downstream market in retail access services, a margin squeeze between the applicant’s wholesale and retail charges will in principle hinder the growth of competition in the downstream markets”, emphasis added).

⁶⁸ Simon Genevaz, *Margin Squeeze after Deutsche Telekom*, GCP MAGAZINE 26 (May 2008).

The recent decisions of the Commission are ambiguous. In *Telefónica* the Commission held that

in the light of the specific factual, economic and legal context of the case, in particular the fact that wholesale access at regional level is mandated since March 1999 and wholesale access at national level is mandated since April 2002 and the fact that the former monopoly's ex ante incentives to invest in its infrastructure are not stake in the present case, the legal test applied by the European Court of Justice in *Oscar Bronner* is not applicable in the present case."⁶⁹

However, what would have been the case if access was not mandated or if the dominant firm did not benefit from the investments of a former legal monopoly and therefore its incentives to invest would have been jeopardized by antitrust liability? Would the *Oscar Bronner* conditions have applied in this case? The Court has, for the moment, been short in explaining the theoretical underpinnings of the distinction between the antitrust doctrines of margin squeeze and refusal to deal. The Commission's Guidance does not provide a detailed explanation either but it seems that the *Oscar Bronner* conditions, in particular the fact that the plaintiff should prove that refusal of a deal/margin squeeze relating to a product or service that is "objectively necessary" for the nondominant firm to be able to compete effectively on a downstream market is also a requirement for margin squeeze cases. In our view, these are more complex questions to answer than a model of predatory pricing. The U.S. antitrust law approach on margin squeeze will be known after the Supreme Court renders a decision in the *Pacific Bell v. Linkline* case.⁷⁰

⁶⁹ *Wanadoo España v. Telefónica*, above, para 309.

⁷⁰ US Supreme Court, Docket 07-512, <http://origin.www.supremecourtus.gov/docket/07-512.htm> .

The approach of EC competition law towards refusals to supply new customers, as interpreted by the European Commission in the Guidance paper, seems also closer to U.S. antitrust law than the jurisprudence of the ECJ and the CFI. The Guidance paper emphasizes the incentive of dominant firms to “invest and innovate.”⁷¹ The Commission raises the concern that “the knowledge that they may have a duty to supply against their will may lead dominant undertakings—or undertakings who foresee that they may become dominant—not to *invest*, or to *invest less*, in the activity in question.”⁷² More investment, because of monopolistic profits, becomes a synonym to innovation, an assumption which is similar to that of the U.S. Supreme Court in *Trinko*.⁷³ Furthermore, contrary to what the CFI decided in *Microsoft*,⁷⁴ the European Commission treats refusals to deal and refusals to license Intellectual Property (“IP”) rights alike. They adopt the higher standards of proof applying to IP rights—in comparison to tangible property rights—for all refusals to deal, by introducing the new product rule as part of the test for any type of refusal to deal.⁷⁵ The objective is clear: emphasize innovation as the main antitrust concern in these cases. The Commission reshapes the conditions for a refusal to deal to be found anticompetitive, as defined by the ECJ in *Oscar Bronner*⁷⁶ by adding the requirement of consumer harm:

⁷¹ Guidance, para 74.

⁷² *Ibid.*

⁷³ *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398, 407 (2004).

⁷⁴ Case T-201/04, *Microsoft v. Comm’n* [2007] ECR II-3601, para 334, “(t)he Court notes that the circumstance that the refusal prevents the appearance of a new product for which there is potential consumer demand is found only in the case-law on the exercise of an intellectual property right”.

⁷⁵ Guidance, para 86.

⁷⁶ Case C-7/97 *Oscar Bronner GmbH v. Mediaprint Zeitungs- und Zeitschriftenverlag GmbH* [1998] ECR I-7791, para. 41 (for there to be an abuse, the refusal to deal should eliminate all competition in the

in examining the likely impact of a refusal to supply on consumer welfare, the Commission will examine whether for the consumers, the likely negative consequences of the refusal to supply in the relevant market outweigh over time the negative consequences of imposing an obligation to supply.⁷⁷

The Commission gives only two examples of consumer harm: First, the excluded competitor is, as a result of the refusal, either prevented from introducing innovative goods or services to the market or the refusal to deal is likely to stifle cumulative innovation. Second, when the price of the input market is regulated and the price in the downstream market is not regulated, the refusal to supply is able to extract more profits in the unregulated downstream market than it would do otherwise.⁷⁸

The Commission is, in any case, ready to consider efficiency gains, including claims by the dominant undertaking that its own innovation will be affected as well, more generally, the level of follow-on innovation by its competitors.⁷⁹ The Commission's aggressive stance towards refusals to supply existing customers⁸⁰ is nevertheless closer to the position defended by the AAI's Transition Report, which finds that, where the monopolist has previously dealt with the excluded competitor, a refusal to deal that creates significant exclusionary effects is actionable under Section 2 of the Sherman Act.⁸¹

downstream market and the input to which access is refused should be indispensable to carrying on business in the downstream market).

⁷⁷ Guidance, para 85.

⁷⁸ Guidance, para 86-87.

⁷⁹ Guidance, para 88-89.

⁸⁰ Guidance, para 83.

⁸¹ AMERICAN ANTITRUST REPORT, at 56.

C. The Devil Is In the Detail: The “Towards More Convergence” Hypothesis

Questioned

There are, however, considerable differences with little chance of convergence between the more effects-based approach of the Guidance paper and U.S. antitrust law, even potentially under an Obama antitrust administration.

The most important difference relates to the restrictive conditions of an efficiency defense for dominant firms under Article 82. The dominant undertaking bears the evidentiary burden of proof with regard to the existence of objective justifications/efficiency gains.⁸² In practice, it would be very difficult for a dominant undertaking to prove the existence of efficiency gains/objective justifications, the control and the conditions for such a defense being at least as restrictive as those of Article 81(3) EC.⁸³ In contrast, the standard of proof for the existence of consumer harm is particularly low, as there is no need to prove the existence of an actual or direct consumer detriment.⁸⁴ The CFI noted in *Microsoft* that consumer choice would be affected if rival products of equal or better quality cannot compete on equal terms.⁸⁵ Nevertheless, in other parts of the decision, the Court interprets this condition as requiring only the preservation of market access for competitors—without requiring that the plaintiff brings evidence that competitors excluded from the market are, or would likely, produce better quality products than those of the dominant firm. Consumer choice seems, in certain parts

⁸² Case T-201/04 *Microsoft v. Commission* [2007] 5 CMLR 846, para. 1144. Guidance, para 27.

⁸³ Guidance, para 29: “...the dominant undertaking will generally be expected to demonstrate. See also, Case C-95/04 P, *British Airways v. Commission* [2007] ECR I-2331, para 86.

⁸⁴ Guidance, para 6 (the protection of the effective competitive process is the primary objective of the enforcement of Article 82), para 19 (likely consumer harm).

⁸⁵ Case T-201/04, para 652

of the CFI decision, to equate to the preservation of competitive rivalry in the marketplace.⁸⁶

As it is also the case in article 81 EC, the standard of proof in Article 82 for harm to competition and for possible defenses is asymmetrical. In the context of article 82, it is generally more difficult to substantiate efficiency gains, and it is even more difficult for efficiency gains and other objective justifications to outweigh likely anticompetitive effects.⁸⁷ In contrast, in U.S. antitrust law, the standard of proof for anticompetitive effects/efficiencies is symmetrical, both for Sections 1 and 2 of the Sherman Act.⁸⁸ One could explain the adoption of a cost-based test for pricing abuses as compensation for the asymmetrical standard of proof in EC competition law for efficiency gains. Otherwise, it would have required dominant undertakings to substantiate the efficiency gains for every rebate/discount that would have produced an exclusionary effect—a mission impossible in terms of litigation costs, and which could have seriously affected incentives to provide discounts that could eventually benefit consumers. This is, however, a second-best solution in comparison to a rule of reason approach that would impose a symmetrical standard of proof for anticompetitive effects and possible justifications.

Tying practices are also an area where convergence would be more difficult to establish. The Guidance paper on Article 82 adopts an anticompetitive foreclosure test, which, at first sight, seems close to the structured rule of reason approach of the United

⁸⁶ Ibid. para 664.

⁸⁷ See, Giorgio Monti, *EC Competition Law* (CUP, 1st ed., 2007), 203 observing that “no firm has yet managed to defend itself successfully” under Article 82 EC.

⁸⁸ Although the DoJ Report raises the bar for prosecuting firms with monopoly power under section 2 vis-avis section 1 by suggesting an asymmetrical standard of proof. See our analysis *infra*.

States in *US v. Microsoft*⁸⁹ which is also advocated by the DoJ in the single-firm conduct report.⁹⁰ However, in practice, there are important differences between the two standards. First, the Guidance paper adopts a supply-oriented definition of the distinct (separate) products condition by accepting indirect evidence of the existence of distinct products when there is a market presence of undertakings specializing in the manufacture or sale of the tied product without the tying product.⁹¹ Second, the Commission treats technical tying more restrictively than contractual tying, as it considers the risk of anticompetitive foreclosure is expected to be greater in this case.⁹² In contrast, “technological” tying is subject to the rule of reason in U.S. law, whereas contractual tying falls under the quasi-per se rule of *Jefferson Parish*.⁹³

It is unclear how tying law will evolve in the future in the United States. The DoJ single-firm conduct report not only strongly supports the abandonment of the quasi-per se rule for tying but also highlights the risks for courts, and antitrust law in general, in interfering in a firm's decision of how to design its products, thus adopting a very positive view for technological tying.⁹⁴ In contrast, the AAI Transition Report supports the current

⁸⁹ United States v. Microsoft Corp., 253 F.3d 34 (D.C. Cir. 2001).

⁹⁰ DoJ Report, at 89-90.

⁹¹ Guidance, para 50. Compare with the entirely demand-side forward looking approach followed in United States v. Microsoft Corp., 253 F.3d 34, 87-88 (D.C. Cir. 2001).

⁹² Guidance, para 52. The recent challenge by the European Commission of the bundling of Microsoft's Internet Explorer with Windows seems to have been inspired by this principle. See, European Commission, Press Release, MEMO/09/15, January 17, 2009.

⁹³ *Jefferson Parish Hospital Dist. No. 2 v. Hyde*, 466 U.S. 2 (1984).

⁹⁴ DoJ Report, at 88: “the Department agrees with courts and panelists urging restraint in the area of product design and believes that great caution should be exercised before condemning a technological tie under the antitrust laws.”

modified per se rule for tying, as articulated in *Jefferson Parish*, with certain caveats,⁹⁵ as well as the nonstructural definition of market power followed by the Supreme Court in *Kodak*,⁹⁶ which is interpreted restrictively by the DoJ Single-firm Conduct Report.⁹⁷

Overall, the European approach for bundling/tying seems inconsistent. The Commission adopts different standards for the various forms of bundling (contractual, technological, and commercial (bundled rebates)), strict standards for contractual tying, stricter standards for technological tying, and lenient standards for bundled rebates, all without clearly explaining how these fit with the overall objectives and aims of Article 82. It is important to acknowledge that, in an effects-based approach, the antitrust standards applied should be coherent, meaning that any similarity or difference in the treatment of these practices should be adequately explained. Antitrust categories are not clear cut: it is possible to present the facts of a case as fitting into more than one antitrust category. For example, there is a fine line between the characterization of the facts of the Windows Media Player (WMP) Microsoft case as being a bundled discount rather than a tying case. The WMP was offered for free, which may formally correspond to a bundled discount, a practice that entails the offering by the supplier to the distributor of a discount (zero price in this case) for accepting a bundle of different products or services. The fact that the Courts analyzed the facts of the case as tying should not conceal the importance of developing a coherent conceptual framework for all types of bundling.⁹⁸ When

⁹⁵ AAI Transition Report, at 57.

⁹⁶ *Ibid.*, at 85. *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451 (1992).

⁹⁷ DoJ Report, at 83.

⁹⁸ See the analysis in Nicholas Economides & Ioannis Lianos, *The Elusive Antitrust Standard on Bundling in Europe and in the United States in the Aftermath of the Microsoft Cases* (September 25, 2008).

deciding to adopt different antitrust tests for each practice, one should take into account the effects of a possible re-characterization of a practice as falling within the scope of another antitrust category. Otherwise you could jeopardize the effectiveness of antitrust enforcement.

Despite the adoption of an as-efficient-as-competitor test for price-related abuses, there are still important differences between the EC competition law and U.S. antitrust law on rebates. These have been explained in detail in the literature.⁹⁹ We would like, however, to highlight the following.

First, there is a slight divergence between the two jurisdictions in the assessment of the exclusionary anticompetitive effect of these practices. In the United States, there is a distinction to make between single-product conditional discounts and bundled rebates. Concerning the first category, only retroactive and individualized rebates can potentially be an antitrust concern. However, no case has been successful at the court of appeal level.¹⁰⁰ There have been many different standards suggested for single-product rebates which would not employ a cost-based test, ranging from the application of the predatory cost/price test to a standard such as that applying to bundled rebates or another one similar to exclusive dealing agreements.¹⁰¹ The DoJ Report leans towards the predatory-

NET Institute Working Paper No. 07-47; NYU Law and Economics Research Paper No. 08-02. Available at SSRN: <http://ssrn.com/abstract=1078932>

⁹⁹ Ibid. See also, Damien Geradin, *A Proposed test for separating pro-competitive loyalty rebate: a conceptual framework*, (August 27, 2008). Available at SSRN: <http://ssrn.com/abstract=1259830>.

¹⁰⁰ *Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227 (1st Cir. 1983); *Concord Boat Corp. v. Brunswick Corp.*, 207 F.3d 1039 (8th Cir. 2000); *Virgin Atlantic Airways Ltd v. British Airways PLC*, 257 F.3d 256 (2d Cir. 2001). See, however

¹⁰¹ For an analysis, see DoJ Report, at 110-116.

pricing standard,¹⁰² not because this is supported by economics, but for two other reasons: greater predictability of the test for undertakings and the risk that a stricter standard could chill aggressive competitive behavior that would benefit consumers (risk of false positives). These assumptions are not specifically supported by empirical evidence and seem to be based entirely on prior beliefs regarding the likelihood and the cost of enforcement errors.

The standard for bundled rebates also remains unclear. The Antitrust Modernization Commission ("AMC") has suggested an attribution test that would take all the discounts provided by the monopolist and apply them to all the units sold by the competitor in the nonmonopolized product market: If the price is below the AVC of the monopolist or there is no possibility of recoupment, the bundled rebate will not be found to be anticompetitive.¹⁰³ The test is basically a predatory pricing test where the main concern is to limit antitrust intervention in situations where there is a very strong likelihood that an equally efficient competitor would be excluded following the bundled discount scheme. A version of this standard was adopted by both the Ninth Circuit in *Cascade Health Solutions* (without including, however, a recoupment test)¹⁰⁴ and the DoJ Report.¹⁰⁵ Other circuits have rejected a cost-based test for a rule of reason approach.¹⁰⁶

¹⁰² *Ibid.*, at 116.

¹⁰³ ANTITRUST MODERNIZATION COMM'N, REPORT AND RECOMMENDATIONS 94-98 (2007), available at http://govinfo.library.unt.edu/amc/report_recommendation/amc_final_report.pdf

¹⁰⁴ *Cascade Health Solutions v. PeaceHealth*, 515 F.3d at 910 n.21 ("We do not believe that the recoupment requirement from single product cases translates to multi-product discounting cases. Single-product predatory pricing, unlike bundling, necessarily involves a loss for the defendant. . . . By contrast, as discussed above, exclusionary bundling does not necessarily involve any loss of profits for the bundled discounter.")

¹⁰⁵ DoJ Report, at 101-102.

¹⁰⁶ *Notably, LePage's Inc. v. 3M*, 324 F.3d 141 (3d Cir. 2003).

In contrast, the European Courts have taken a more aggressive position towards single-product rebates, as they have condemned all-unit as well as incremental rebates (both standardized or individualized) if these produce an exclusionary effect without objective justification. In addition, the courts have not employed a cost-based test.¹⁰⁷ The Commission's Guidance paper adopts a variation of the attribution test that closes the gap between EC competition law and the positions adopted in *Cascade Health Solutions* (also suggested by the AMC and the DoJ Report) but with some important differences still remaining. The test attributes the discounts only to the contestable share of the non-monopolized product sold by the competitor¹⁰⁸ and not to all units sold, as is the case in the *Cascade Health Solutions* and AMC test and it employs the LRAIC as the relevant cost benchmark (and not AVC as in U.S. antitrust law).¹⁰⁹ It is therefore easier for the plaintiff to prove that the discount is an antitrust infringement in EC competition law, although the Commission's Guidance standard is more restrictive than the test applied by the Third Circuit in *3M*.¹¹⁰ The Guidance paper applies a slightly different cost standard for unconditional bundled rebates as it takes into account the incremental price that customers pay for each of the dominant undertaking's products in the bundle and assesses

¹⁰⁷ See, for the analysis of the case law, RICHARD WHISH, *COMPETITION LAW 720-726* (6th ed. 2009).

¹⁰⁸ This is established for existing competitors by looking to the specific market context: "how much of a customer's purchase requirements can realistically be switched to a rival. For potential competitors, the Commission will assess the scale at which a new entrant would realistically be able to enter. This will be done by taking into account the historical growth pattern of new entrants in the same or similar markets": Guidance paper, at 16.

¹⁰⁹ We are indebted to Nicholas Economides for drawing our attention to this difference.

¹¹⁰ *LePage's Inc. v. 3M*, 324 F.3d 141 (3d Cir. 2003). A rule of reason approach without any cost-based test.

if this price remains above the LRAIC of the dominant undertaking when this product is included in the bundle.¹¹¹

The Commission adopts a series of presumptions for certain categories of single-product conditional rebates including a positive one for standardized rebates as these are actionable under Article 82 only if it can be established that the rebate approximates the requirements of an appreciable proportion of customers.¹¹² In addition, transaction cost advantages can only be considered as a plausible efficiency gain for standardized rebates.¹¹³ The Commission clearly downgrades predation as the main competition law concern for conditional rebates and instead emphasizes, as the main issue, leveraging that leads to anticompetitive foreclosure.¹¹⁴ One could advance the position that there is an assumption in EC competition law that rebates conditional on loyalty may create an attraction effect.¹¹⁵ According to Bechenkamp and Maier-Rigaud,

this “attraction” effect consists in a high reluctance to quit rebate or discount schemes, even in the switch condition where it is rational to switch to the linear scheme. This expectation is based on the assumption that participants evaluate the situation as a sunk cost situation. If this assumption is adequate, an “attraction” effect should be found, i.e. an emphasized status quo bias in the discount and the rebate scheme.¹¹⁶

This assumption is allegedly based on empirical economic findings and constitutes an effect that “a non-behaviorally informed standard economic theory would

¹¹¹ Guidance, para 58-60.

¹¹² Guidance, para . 44.

¹¹³ Ibid, para 45

¹¹⁴ Ibid, para 38

¹¹⁵ Ibid, para 39

¹¹⁶ Martin Bechenkamp & Frank P. Maier-Rigaud, *An Experimental Investigation of Article 82 Rebates Schemes*, 2(2) COMP L REV SUPP 1 (2006), at 14.

not predict.”¹¹⁷ The European Commission seems to have relied on this assumption in the *Prokent-Tomra* case, where it condemned Tomra’s loyalty-inducing schemes, essentially based on the maintenance of Tomra’s dominant position on the market despite the potential of its rivals to challenge it.¹¹⁸ The recent antitrust case on single-product rebates brought against Intel in the United States and in Europe will provide an interesting test for possible convergent or divergent standards in both jurisdictions.

It is dangerous to predict legal developments, but in our view, there are few chances for a complete convergence between EC competition law and U.S. antitrust law in the area of single-firm conduct, even under an Obama administration. First, there are the institutional constraints of the case law of the Supreme Court, which has gradually restricted the scope of antitrust intervention under Section 2 of the Sherman Act.

Second, we do not know if the European Courts are going to accept or reject the effects-based approach of the Commission’s Guidance regarding some of the specific conducts, although some of the recent decisions show a predisposition of the European Courts to accept decisions with deeper economic evidence. But the European Courts seem to have adopted a very specific interpretation of the concept of consumer harm in the few recent cases, where they referred to consumer interest as an objective of EC competition law.¹¹⁹

¹¹⁷ Ibid.

¹¹⁸ Case COMP/E-E-1/38.113 – *Prokent-Tomra* C(2006)734, para 335-345. Pending case T-155/06 at the Court of First Instance (action for annulment of the Commission’s decision).

¹¹⁹ See, Joined Cases C-468/06 to C-478/06, *Sot. Lélos Kai Sia E.* [2008], para. 68 (the ECJ made, for the first time, explicit the objective of EC competition law: the protection of the final consumers “by means of undistorted competition and the integration of national markets”); T-168/01, *GlaxoSmithKline Unlimited v Commission* [2006] ECR II-2969, para 118 (the protection of the welfare of final consumers constitutes the objective of Article 81(1)). Cases C-501, 513, 515 & 519/06 P (judgment pending).

The Courts' conception starts from the assumption that an important ingredient of Article 82 EC is the idea that dominant firms have a special responsibility to protect competition. Their commercial freedom is restricted in comparison to non-dominant undertakings. This principle is based on the belief that dominant firms are in a position to directly influence the market activities of other economic agents and may therefore constitute an informal institution that can indirectly affect consumers' ultimate choices.¹²⁰ The underlying theoretical assumption is that rivalry brings variety to the marketplace, in the sense that entrepreneurs test a certain number of hypotheses on the bundles of parameters of a "product" (price, quality, services and so on), which they think will satisfy consumer preferences.

Variety ultimately preserves consumer choice and consumers' ability to test the solutions adopted by the entrepreneurs. The variety of "products" (or solutions suggested by the entrepreneurs) may not be the outcome of the "natural" selection process of the marketplace, but the result of the "artificial selection" of formal and informal institutions, which "channel the competitive process and give it a certain direction," thus selecting "at the same time, artificially, which entrepreneurial hypotheses will survive."¹²¹ EC competition law aims to protect consumer sovereignty, which is the ability of the consumers to influence price, quality, variety, and, subsequently, the competitive (or innovation) process according to their own preferences.¹²² The emphasis on the special

¹²⁰ Again this may be a result of the traditional importance of public enterprises and state monopolies. Since in the EU competition policy is an instrument to reach the Single Market, sector liberalization and competition is a way to foster market integration.

¹²¹ Chris Mantzavinos, *Individuals, Institutions, and Markets* (CUP, 2001), at 174.

¹²² For another formulation of this principle see, Neil Averitt & Robert H. Lande, *Consumer Sovereignty: A Unified Theory of Antitrust and Consumer Protection Law*, 65 ANTITRUST L J 713, 715

responsibility of dominant firms to protect the competitive process should therefore be understood as a proxy for consumer sovereignty; open and contestable markets are a prerequisite for consumer empowerment.¹²³

This doctrine may not always be compatible with mainstream neoclassical economic theory. Recent economic thinking has, nevertheless, cast doubt on several assumptions and the analytical framework of neoclassical price theory. Behavioral law and economics challenge the perfect rationality premise that permeates much of neoclassical economic analysis. This has profound implications for antitrust policy and doctrine.¹²⁴ Furthermore, recent evolutionary thinking on consumer theory has challenged the neoclassical price theory assumption that consumers act upon exogenously given preferences.¹²⁵ Consumers are influenced in their decision by

the context of choice, defined by the set of options under consideration. In particular, the addition and removal of options from the offered set can influence people's preferences among options that were available all along.¹²⁶

Firms with their marketing activities may, for example, endogenously shape consumer preferences by establishing an artificial selection process. Neoclassical economic theory operates on the assumption that preferences are revealed by market

(1997) (consumer sovereignty is “the set of societal arrangements that causes that economy to act primarily in response to the aggregate signals of consumer demand, rather than in response to government directives or the preferences of individual businesses”).

¹²³ We could add that as liberalization proceeds, the objective of market integration becomes more and more a consumer interest objective.

¹²⁴ See, Maurice Stucke, *Behavioral Economists at the Gate: Antitrust in the Twenty-First Century*, 38 Loyola U Chicago L J 513 (2007).

¹²⁵ Richard H. Thaler, *Towards a positive theory of consumer choice*, 1 JOURNAL OF ECONOMIC BEHAVIOR & ORGANIZATION 39-60 (1980).

¹²⁶ Elda Shafir, Itamar Simonson, & Amos Tversky, *Reason-based choice*, 49 COGNITION 11 (1993).

behavior¹²⁷ and ignores the psychological aspect of the formation of these preferences. Recent studies have challenged this assumption: “preferences are actually constructed—not merely revealed.”¹²⁸

The restrictive position of the ECJ and the European Commission with regard to technological tying and de facto standardization, and the broad definition by the European Commission of the concept of consumer welfare as including the preservation of consumer choice and variety, are examples that indicate the importance of the principle of consumer sovereignty—not only in informing the detailed competition law assessment of the alleged anticompetitive conduct but also in framing the general standards and presumptions of Article 82 EC.

Third, even if there is convergence in the substantive standards of the competition assessment of single-firm conduct in EC competition law and U.S. antitrust law, it is not certain that there will be effective convergence in the constraints antitrust imposes on the commercial strategies of dominant firms. If we look to the market shares of alleged dominant firms, EC competition law tends to subject Article 82 firms with lesser degree of market power than U.S. antitrust law. Furthermore, private enforcement is much more active in the United States than in Europe, thus leading to more significant costs for dominant firms if they do not comply with the competition law provisions for single-firm conduct.¹²⁹

¹²⁷ Paul Samuelson, *Consumption Theory in terms of revealed Preference*, 15 *ECONOMICA* 243 (1948).

¹²⁸ Elda Shafir, Itamar Simonson & Amos Tversky, at 34. Although these new hypothesis may not change significantly received economic theories for competition analysis.

¹²⁹ We are indebted to David Evans for this remark. As the United States noted in their submission to the OECD, Policy Roundtable, Fidelity and Bundled Rebates and Discounts, at 131, antitrust challenges to

III. VERTICAL CONTRACTUAL RESTRAINTS

The Supreme Court decision on *Leegin*¹³⁰ finally overruled Dr. Miles and the per se rule against vertical minimum price-fixing ("RPM"). This case is particularly relevant for the current discussion regarding the revision of the EU Vertical Guidelines that blacklisted RPM. Despite a sharply divided decision, there was unanimous agreement that competition economics indicated there were both pro-competitive and anticompetitive effects, as also argued under amicus curiae by DoJ and FTC.

However, Judge Breyer, in his dissenting opinion, argued that economic evidence showed that anticompetitive effects are more important. During the period of the Fair Trade Acts (1937-1945), retail prices were higher in states that had passed statutes allowing vertical minimum price-fixing than in states that had not, and retail prices were lower after the repeal of those acts.¹³¹ However, this natural experiment is between per se legality and per se illegality and not with a regime of rule of reason.¹³² This also shows that we need further empirical studies about this type of practice; studies that could be undertaken when revising the EU Guidelines.

rebates have all been private treble damages cases. There is no provision for treble damages in EC competition law.

¹³⁰ *Leegin Creative Leather Products v. PSKS, Inc.*, 127 S. Ct. 2705 (2007); *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220, U.S. 373 (1911).

¹³¹ Comparing prices in the former States with prices in the latter States, the Department of Justice argued that minimum resale price maintenance had raised prices by 19 percent to 27 percent. See *Hearings on H. R. 2384 before the Subcommittee on Monopolies and Commercial Law of the House Committee on the Judiciary*, 94TH CONG., 1ST SESS., 122 (1975). In today's dollars, Justice Breyer estimated that the agreements translate to a higher annual average bill for a family of four of roughly \$750 to \$1,000. The dissent was signed by Justices John Paul Stevens, David H. Souter, and Ruth Bader Ginsburg.

¹³² However, Einer Elhauge, *Harvard not Chicago: which Antitrust School drives recent US Supreme Court Decisions*, 3(2) COMPETITION POL'Y INT'L, (Autumn 2007), rightly points that this experiment is against Chicago School's position on the per se legality of RPM.

Various experts have argued persuasively that RPM and vertical non-price restraints have parallel competitive justifications and similar influences on both competition and consumer welfare. Yet RPM remained bound to a rule of per se illegality. Conversely, the law has long treated horizontal price fixing and horizontal market division identically.

Another important consistency argument for overturning per se illegality is the fact that since *Broadcast Music* was decided in 1979,¹³³ courts have admitted that the per se rule does not apply if horizontal price-fixing advances the pro-competitive purposes of a productive business relation, so it would be perverse to give a stricter scrutiny to vertical price-fixing, which is usually a less anticompetitive practice.

The enforcement of RPM had also become quite messy. For example, in *Colgate* unilateral terminations of a dealer by a supplier were found to benefit from immunity from Section 1 of the Sherman Act as there was no antitrust agreement/conspiracy. And the reality is that in both the EU and the United States, very few cases have been either pursued by authorities or litigated. In the United States, rival retailers and manufacturers lack legal standing and consumers have to prove they were harmed.

But both economists and lawyers have to be more explicit about effects. As the Supreme Court recognized, RPM may have serious anticompetitive consequences. Resale price maintenance agreements can diminish or eliminate price competition among dealers of a single brand or (if practiced generally by manufacturers) among multi-brand dealers. They can prevent dealers from offering customers lower prices; they can prevent dealers

¹³³ *Broadcast Music, Inc. v. Columbia Broadcasting System*, 441 U.S. 1 (1979).

from responding to a fall in demand by cutting prices; they can encourage dealers to substitute service for price competition; and they can inhibit expansion by more efficient dealers.

Resale price maintenance agreements can also help strengthen the market power of firms in concentrated industries. In such industries firms may more easily tacitly collude. RPM can make it easier for each producer to identify when a competitor has begun to cut prices. And because the dealer will be unable to stimulate increased consumer demand by passing along the producer's price cut to consumers, a producer who cuts wholesale prices without lowering the minimum resale price will stand to gain little, if anything, in increased profits. Because of these effects, William S. Comanor and Frederic M. Scherer in their *Amici Curiae* in *Leegin* stated that "it is uniformly acknowledged that [resale price maintenance] and other vertical restraints lead to higher consumer prices."

RPM can also have pro-competitive or efficiency effects. The majority opinion lists two: First, such agreements can facilitate new entry. For example, a newly entering producer wishing to build a product name might be able to convince dealers to help it do so—if, but only if, the producer can assure those dealers that they will later recoup their investment. Without resale price maintenance, dealers entering later might take advantage of the earlier investment and, through price competition, drive prices down to the point where the early dealers cannot recover what they spent. The result might be increased competition at the producer level, i.e., greater inter-brand competition, that brings with it

net consumer benefits. But this result depends on the existence of other brands.

Second, without resale price maintenance, a producer might find its efforts to sell a product undermined by “free riding.” Without resale price maintenance, some dealers might take a “free ride” on the investment that others make in providing sale assistance services. Under these circumstances, dealers might prove unwilling to invest in the provision of necessary services.

Judge Breyer invokes the difficulty in distinguishing and evaluating those effects in practice. But this is a problem in all cases where we have to use the rule of reason. And there is no fundamental economic reason or model—contrary to the cases of horizontal price-fixing—where cooperation among firms dictates that the cartel solution is the more likely consequence, thereby allowing a presumption in favor or against RPM.

Back in Europe, Regulation 2790/99 treats minimum RPM as a hardcore restriction that does not benefit from the possibility of exception of the prohibition under Article 81(3).¹³⁴ Theoretically, EC competition law offers the possibility of justifying a hardcore restriction, such as resale price maintenance, under Article 81(3), although under the current guidelines this seems unlikely to succeed.¹³⁵ The structure of Article 81, with the possibility to justify under article 81(3) a practice that has an anticompetitive object or effect, is nevertheless flexible enough to accommodate a standard of presumptive but rebuttable illegality of RPM or a full rule of reason approach, should the

¹³⁴ COMMISSION REGULATION (EC) NO 2790/1999 of 22 Dec. 1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices, (1999) OJ L 336/21, Art. 4(a)

¹³⁵ COMMISSION NOTICE, GUIDELINES ON VERTICAL RESTRAINTS, (2000) OJ C 291/1, para 46. See also, COMMUNICATION FROM THE COMMISSION NOTICE, GUIDELINES ON THE APPLICATION OF ARTICLE 81(3) OF THE TREATY, (2004) OJ C 101/97, para 46. Nevertheless, there have been instances where the specific conditions of the product market were found to justify the application of Art. 81(3) for RPM: e.g. Case 243/85, Binon & Cie v. SA Agence et Messageries de la Presse [1985] ECR 2015, para 46.

Commission decide to follow the approach of the majority opinion of the Supreme Court in *Leegin*.¹³⁶

The Europeans should also watch for possible legislative action to restore the rule that agreements among manufacturers and retailers, distributors, or wholesalers to set the minimum price below which the manufacturer's product or service cannot be sold violates the Sherman Act, in particular the recent legislative proposals promoted by Senators Kohl, Biden, Whitehouse, and Clinton.¹³⁷ In the event U.S. antitrust authorities decide to publish guidelines on vertical contractual restraints,¹³⁸ an additional issue may be the integration of a new model for vertical contractual restraints that would take into account the commercial reality of multi-brand distribution and retailer market power.¹³⁹ The role of intra-brand competition in this context may be more important than what was originally contemplated by the Chicago school of antitrust economics.¹⁴⁰ Additional issues with regard to convergence between the EU and the United States in this area would be the definition of the concept of antitrust agreement, as opposed to unilateral

¹³⁶ See the discussion of the roundtable on *The law and economics of resale price maintenance: a comparative perspective*, 4 CONCURRENTS 53-67 (2008), available at http://www.concurrences.com/article_revue_web.php3?id_article=22112&lang=en

¹³⁷ See, <http://www.govtrack.us/congress/bill.xpd?bill=s110-2261> .

¹³⁸ As this has been suggested by the AAI Transition Report, at 58.

¹³⁹ That could possibly integrate the dual-stage model for distribution of R L Steiner, *Intrabrand Competition-Stepchild of Antitrust* 36 THE ANTITRUST BULLETIN 155 (1991); R L Steiner, *The Inverse Association Between the Margins of Manufacturers and Retailers*, 8 REVIEW OF INDUSTRIAL ORGANIZATION 717 (1993); M P Lynch, *Why Economists are Wrong to Neglect Retailing and How Steiner's Theory Provides an Explanation of Important Regularities*, 49 ANTITRUST BULLETIN 911 (2004); In the European context, see Ioannis Lianos, *Some reflections on the vertical restraints antitrust category*, 4 CONCURRENTS 17-26 (2008), available at http://www.concurrences.com/article.php3?id_article=22105&lang=fr

¹⁴⁰ AAI, Transition Report, at 57.

practice, in order to define the scope of Article 81 or Section 1 of the Sherman Act,¹⁴¹ and the prohibition of conduct affecting parallel trade between member states, a specificity of EC competition law.¹⁴²

Another important area requiring convergence is the repeal of the Robinson-Patman Act¹⁴³ in the United States and national laws in several European states that prohibit selling at prices below cost, regardless if it configures predatory pricing or just promotional prices. This is bad economics.

IV. MERGERS

A. Horizontal Mergers

A survey of experienced antitrust lawyers conducted by Baker and Shapiro shows a more lax approach towards mergers during George W. Bush's two terms in office and in particular at the DoJ.¹⁴⁴ This survey shows a significant drop in the perception by antitrust lawyers of the restrictive effects (for undertakings) of merger control.¹⁴⁵

Enforcement statistics published by both agencies show a 50 percent drop in the rate of merger enforcement actions relative to filings (average of about .9 percent).

¹⁴¹ The AAI, Transition Report, at 58 proposes the legislative or judiciary repeal or reform of the *Colgate* doctrine "insofar as that doctrine treats RPM coerced by a manufacturer's threatened refusal to deal as unilateral conduct". For an analysis of the definition of the agreement/collusion requirement in the context of Article 81, in particular for vertical restraints, see Ioannis Lianos, *Collusion in vertical relations under Article 81*, 45 COMMON MARKET LAW REVIEW 1027-1077 (2008).

¹⁴² Joined cases C-468/06 to 478/06, *Sot. Lelos kai Sia v GlaxoSmithKline* [2008], para 56-57 & 66 (article 82 EC); T-168/01, *GlaxoSmithKline Unlimited v Commission* [2006] ECR II-2969; Pending appeal at the ECJ, Case C-501/06P (Article 81 EC).

¹⁴³ As suggested by the Antitrust Modernization Commission, see http://govinfo.library.unt.edu/amc/report_recommendation/amc_final_report.pdf at 311.

¹⁴⁴ Jonathan Baker and Carl Shapiro, *Reinvigorating Horizontal Merger Enforcement* (October 2007). Available at SSRN: <http://ssrn.com/abstract=991588>.

¹⁴⁵ One case cited by the authors is the Whirlpool/Maytag merger that led to very high concentration ratios (70 percent). Just after the merger they announced price increases of 6 to 12 percent.

This may be the result of the courts' rejecting the DoJ decision to oppose Oracle's acquisition of People's Soft and also in *Sun Gard*. These cases have seriously shaken the edifice of antitrust merger analysis, in particular the doctrine of unilateral effects that is now in clear need of being reaffirmed.¹⁴⁶ In the Oracle case, Judge Walker required the government to show that the merger would "create a monopoly or quasi-monopoly in a narrow market, while simultaneously expressing skepticism about narrow markets as arbitrary or unprincipled submarkets."¹⁴⁷ In fact, he rejected complaints by customers *ad limine*; the demonstration that the elimination of significant competition between the two merging parties, among a small number of rivals, could lead to competitive harm; and that merger simulations in general could not be trusted because data may be not of high quality.

According to Baker and Shapiro, there are two major reasons for this weaker merger enforcement. The first is the view that "effective competition requires three and sometimes only two rivals," and concentration analysis has been downgraded too much, while Industrial Organization and game theory tells us that it is still a crucial element in any merger analysis. The second is that entry needs to be only potential, which is at odds with the predatory pricing doctrine. In fact, agencies need to show that it is not only potential but also likely.

¹⁴⁶ In view of this experience, Jonathan Baker and Carl Shapiro have advocated a new method for merger analysis that does not rely excessively on market definition, but on two indicators: the diversion ratio between the products of the merging parties and their gross margins. See also, Joseph Farrell & Carl Shapiro, *Antitrust Evaluation of Horizontal Mergers: An Economic Alternative to Market Definition* (December 9, 2008). Available at SSRN: <http://ssrn.com/abstract=1313782>. This is a theory that in our view deserves wider application in both sides of the Atlantic.

¹⁴⁷ Jonathan Baker and Carl Shapiro, *Reinvigorating Horizontal Merger Enforcement*, October 2007, mimeo, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=991588

However, there were also some important contributions by the U.S. antitrust agencies. One is the methodology and successful challenging of the Exelon and PSEG electricity merger in 2006. The other is the methodology used to evaluate coordinated effects in mergers, used in the *Premdor* case¹⁴⁸ and developed further by the FTC, using game theory.

Since *GE/Honeywell*, international cooperation has intensified and avoided any other major divergence in merger evaluation. Since the United States and their EU counterparts launched the effort, participants have coordinated on more than 60 merger reviews and negotiated remedies on at least 14 mergers.¹⁴⁹ Recent examples of intergovernmental cooperation with one set of remedies for anticompetitive issues in several jurisdictions include the \$14.4 billion purchase of U.K.-based BOC Group plc by Germany's Linde AG in July, Procter & Gamble Co.'s \$57 billion acquisition of Gillette Co. in 2005, and Boston Scientific Corp.'s \$27.3 billion deal for Guidant Corp. a year ago.

B. Vertical and Conglomerate Mergers

Some further dialogue and work is needed in the areas of vertical and conglomerate mergers. There has been almost no challenge to vertical mergers in the United States for a long time (following the Chicago antitrust economics' positive view of vertical integration). The 1992 Merger Guidelines did not concern vertical or conglomerate mergers and the 1984 Merger Guidelines advocated a very cautious

¹⁴⁸ *U.S. v. Premdor Inc.*, Fed Reg 45, 326 (Aug. 28, 2001)

¹⁴⁹ Randolph Tritell, Director of the U.S. Federal Trade Commission's Office of International Affairs, Fordham Law Center's annual international antitrust conference, September 2008.

standard of antitrust intervention for vertical mergers.¹⁵⁰ In contrast, the EU has adopted guidelines which are strongly inspired by post-Chicago antitrust economics, in particular the Raising Rivals Costs ("RRC") theory. Reflecting the same concern for anticompetitive foreclosure as in the Commission's guidance on its enforcement priorities under Article 82 EC, the non-horizontal merger guidelines provide the Commission with the tools to challenge vertical mergers in circumstances where the acquiring firm has the ability and the incentive to foreclose competitors at the downstream or upstream market (input and customer foreclosure), harming consumers.¹⁵¹ The European Commission has blocked or brought some vertical merger cases to Phase II of EC merger control, thus indicating the likelihood that vertical mergers may significantly impede effective competition.¹⁵²

Also regarding conglomerate mergers, there is a need of further dialogue in order to avoid a new GE/Honeywell case. Although most post-Chicago economists would question the traditional leveraging theory, there is no doubt that some of the predatory practices are rooted in the cost of financing and distortions introduced by risk and uncertainty in the financial markets. Does this reasoning transpose to conglomerate mergers? More specifically, does the "deep pockets" theory have any place in conglomerate mergers? Finally, the non-horizontal merger guidelines are mute as to

¹⁵⁰ J. Thomas Rosch, *The Challenge of non-horizontal merger enforcement*, FTC Speech, September 27-28, 2007, available at <http://www.ftc.gov/speeches/rosch/070927-28non-horizontalmerger.pdf>

¹⁵¹ COMMISSION'S GUIDELINES ON THE ASSESSMENT OF NON-HORIZONTAL MERGERS [2008] OJ C 256/6, available at http://ec.europa.eu/competition/mergers/legislation/notices_on_substance.html

¹⁵² E.g. COMP/M.3440 - *EDP/ENI/GDP*, C(2004)4715 final. See, most recently, Case No COMP/M.4942 - *Nokia-Navteq*, C(2008)3328 ; Case No COMP/M.4731 - *Google-DoubleClick* - C(2008)927 final; Case No COMP/M.4854 - *TomTom/TeleAtlas* C(2008)1859; Case No COMP/M.4403 - *Thales/Finmeccanica/Alcatel Alenia Space & Telespazio* (2007) D202107; Case No COMP/M.4180 - *Gaz de France/Suez* C(2006)5419; Case No COMP/M.4874 - *Itama/Barcovision* C(2008).

diagonal mergers that may eliminate a crucial supplier to a rival downstream firm. We are starting to enter the terrain of designs more complex than simple vertical mergers.

V. STATE ACTION (STATE AIDS)

The number one item in any governments' agenda right now is the financial and economic crisis.¹⁵³ We have seen the near collapse of the financial systems in developed countries being shored up by capital injections from states and fiscal packages, which produce a large immediate impact on public debt. However, there has been no major concern voiced regarding the distortions some of these measures could cause to the competitive process and/or the competitive risks of constructing market situations that could be difficult to unravel in the future.

We strongly believe that policies for providing liquidity to the financial system and shoring-up the solvency of the financial system can be structured both without any major distortions to the competitive process and with minimal government intervention. First, we know that the origin of the problem is a monumental failure to define and enforce the right regulatory strategies vis-à-vis credit contracts: the problem of information asymmetry that may produce adverse selection and moral hazard. So, regulatory reforms are badly needed. Second, market-based solutions are always preferable to having states take over institutions or directly managing banks. But shareholders have to feel the brunt of their mistakes. If they are to be bailed out by

¹⁵³ The speed at which financial crisis evolve requires a prompt intervention by monetary authorities. These and competition authorities should be involved in defining guidance and frameworks for measures that have the highest impact in reducing systemic risk and preserving competitive structures. See Abel Mateus, *The Current Financial Crisis and State Aid in the European Union: Has It Been Timely and Appropriate?* GCP, Dec. 8, 2008.

taxpayers, there should be capital write-downs and loss recognition. Otherwise, we will be inviting moral hazard and build the foundations of the next financial crisis.

As the European Commission guidance recognizes, overall interventions and nondiscriminatory measures are always preferable, although regulators have to decide on their application on a case-by-case basis.¹⁵⁴ Reducing distortions is also synonymous with reducing taxpayers' costs over the long-term. For example, if the U.S. Treasury gave priority to bank recapitalization (like the United Kingdom proposed), it would obtain more impact in avoiding bankruptcies of financial institutions and systemic risk—from the same dollar spent—than the TARP (Troubled Asset Relief Program) proposal. Reducing distortions also requires liquidating insolvent institutions as early as possible, recovering as much as possible from the toxic assets that end up in state institutions. But as the Swedish approach showed during the Nordic crisis, it may not be possible to avoid “cleaning-up bank balance sheets” so that lending can resume for highly-leveraged economies. Hiding and hoping that the problem goes away was a recipe for the Japanese lost decade.

There are two further important issues. First, mergers and acquisitions undertaken to solve solvability problems that can be harmful to competition are undesirable.¹⁵⁵

¹⁵⁴ COMMUNICATION FROM THE COMMISSION – THE APPLICATION OF STATE AID RULES TO MEASURES TAKEN IN RELATION TO FINANCIAL INSTITUTIONS IN THE CONTEXT OF THE CURRENT GLOBAL FINANCIAL CRISIS, (2008) OJ C270/8, available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2008:270:0008:0014:EN:PDF>

¹⁵⁵ So far, American antitrust authorities have been mute on the large mergers that have occurred in the United States. In the case of Lloyds TSB/HBOS the Secretary of Commerce approved the merger against the advice of OFT. The CAT upheld the decision despite the complaint by some consumer groups that argued that other measures (like bank recapitalization) were already in place. The Court found that the Secretary's decision had been within its administrative authority in view of the U.K. competition law and its limitation in case of “public interest”. The problem still remains if there are no other less distorting alternatives.

Consumers and enterprises will be taxed over the long-term by higher prices and a reduction in both economic recovery and in competitiveness at large, thereby lowering long-term welfare more significantly than what can be gained in the short-term.

Alternatives more amicable to competition are usually available. Second, antitrust should not be suspended in times of financial crisis, nor should the financial sector in general be excluded from antitrust, as the U.S. Supreme Court seemed to establish in its recent *Credit Suisse*¹⁵⁶ decision.¹⁵⁷

¹⁵⁶ *Credit Suisse Securities v. Billing*, 127, S. Ct. 2383, 2389 (2007). The intersection of competition law and sector-specific regulation in Europe is inspired by different principles, competition law being a quasi-constitutional provision that supersedes any sector-specific regulation at the EU or at the national level. See, Case T-271/03, *Deutsche Telekom AG v. Commission* [2008]; Guidance, para 81.

¹⁵⁷ In our opinion, regulation of the financial system should aim for financial stability (e.g. avoiding the moral hazard by bankers as agents of the depositors that are the principals) and transparent information of capital markets, while competition laws aims to maintain a competitive financial system. These two objectives are not in conflict if we choose the right policies.