



THE ONLINE MAGAZINE FOR GLOBAL COMPETITION POLICY

Guidance On Enforcement Priorities Regarding Exclusionary Abuses: A Comparative Overview

Yves Botteman and Kenneth P. Ewing

Step toe & Johnson LLP

Guidance On Enforcement Priorities Regarding Exclusionary Abuses: A Comparative Overview

Yves Botteman and Kenneth P. Ewing*

On December 3, 2008, the European Commission published a guidance document (“Guidance”) concerning the Commission’s enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant companies.¹ The Guidance affirms in general terms the Commission’s intent to focus enforcement decisions on conduct likely to harm consumers, not just individual competitors, and to consider the economic benefits of conduct somewhat as it does with “efficiencies” in the context of Article 81(3) of the EC Treaty or under the EC Merger Regulation.

When laying down the factors that it will assess when considering whether to initiate an enforcement proceeding, however, the Guidance reveals greater readiness on the part of the Commission to find a violation by a market-dominating firm than that reflected in a comparable report recently released by the U.S. Department of Justice (“DOJ”) on its policies regarding the same kinds of unilateral conduct (the “Report”).²

*Yves Botteman is a Senior Associate in the Brussels office of Steptoe & Johnson LLP where he practices EC competition law. Kenneth Ewing is a Partner in the Washington, D.C. office of Steptoe & Johnson LLP where he is a member of the Regulatory & Industry Affairs Department. Mr. Ewing is the Team Leader of the firm’s antitrust practice.

¹COMMISSION COMMUNICATION – GUIDANCE ON THE COMMISSION’S ENFORCEMENT PRIORITIES IN APPLYING ARTICLE 82 EC TREATY TO ABUSIVE EXCLUSIONARY CONDUCT BY DOMINANT UNDERTAKINGS [hereinafter “Guidance”]. The Guidance, along with a press release, a list of questions and answers, the Commission staff working paper, and other useful citations, is available at <http://ec.europa.eu/comm/competition/antitrust/art82/index.html>.

²U.S. DEP’T OF JUSTICE, COMPETITION AND MONOPOLY: SINGLE-FIRM CONDUCT UNDER SECTION 2 OF THE SHERMAN ACT (Sept. 8, 2008) [hereinafter “Report”], available at www.usdoj.gov/atr/public/reports/236681.htm. The Federal Trade Commission did not join DOJ’s report,

The Commission's enforcement approach also differs from that of the DOJ in several other respects that will be important for companies seeking to comply with both U.S. and EU legal regimes. Such companies may be disappointed not to find in the Guidance the kinds of clear tests, safe-harbors, and presumptions that the DOJ's Report helpfully articulated. Conversely, those considering whether to complain to the Commission about dominant firm conduct may now have a clearer idea of the kinds of arguments to make.

I. BACKGROUND

The Commission began to review its enforcement policy regarding abuses of dominance under Article 82 EC in 2005.³ As reflected in a speech by Neelie Kroes, EU Commissioner for Competition, at the Fordham Corporate Law Institute, the objective of this review was twofold, namely to improve the quality of the Commission's decisions in exclusionary abuse cases and to make sure that the Commission's staff pursues the right cases.⁴ In December 2005, the Commission's Directorate-General for Competition published a discussion paper on exclusionary abuses under Article 82 EC.⁵ This paper provided a detailed account of the case-law before the Commission and EU courts and

but its policy staff recently issued four working papers regarding some of the issues addressed in DOJ's Report. See *FTC Press Release, Staff Working Papers on Section 2*, posted on Federal Trade Commission Website (Jan. 16, 2009), available at www.ftc.gov/opa/2009/01/section2.shtm (with links to papers). Since these working papers do not necessarily reflect FTC policy, we focus here on DOJ's Report.

³See ECONOMIC ADVISORY GROUP ON COMPETITION POLICY, REPORT BY THE EAGCP: AN ECONOMIC APPROACH TO ARTICLE 82 (July 21, 2005), available at: http://ec.europa.eu/comm/competition/publications/studies/eagcp_july_21_05.pdf

⁴EC Competition Comm'r Neelie Kroes, *Preliminary Thoughts on Policy Review of Article 82*, Speech at Fordham Corporate Law Institute, New York (Sept. 23, 2005), available at <http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/05/537&format=HTML&aged=1&language=EN&guiLanguage=en>.

⁵EUROPEAN COMMISSION DG COMPETITION DISCUSSION PAPER ON THE APPLICATION OF ARTICLE 82 OF THE TREATY TO EXCLUSIONARY ABUSES (Dec. 2005), available at <http://ec.europa.eu/comm/competition/antitrust/art82/discpaper2005.pdf>

served as the basis for a critical review of the Commission's enforcement policy in this area. For more than two years, we have seen little of the policy review other than occasional references in public speeches.

On the enforcement front, however, the Commission was quite active during this period. It adopted prohibition decisions and fined *Tomra* for exclusive dealing practices in March 2006 and *Telefonica* for margin squeeze in July 2007. It also initiated proceedings against several undertakings for alleged exclusionary conduct, including two statements of objections against Intel (exclusive dealing and rebates) and one against Alcan (tying). These cases are still pending. Finally, the Court of First Instance largely upheld the Commission's approach in *Microsoft* on both refusal to deal and tying theories.

Meanwhile, over the same period in the United States, the DOJ and the Federal Trade Commission ("FTC") carried out a detailed review of their enforcement policies under Section 2 of the Sherman Act. While it has not prosecuted Section 2 cases in years, the DOJ published a Report in September 2008 summarizing current U.S. law and developing specific tests for several categories of potentially abusive unilateral conduct. These tests include a combination of safe-harbors and presumptions intended to enable businesses to make practical judgments without fear of legal challenges. Although this report did not receive the support of the FTC and generated mixed reactions among legal practitioners in the United States, it serves as a useful point of comparison to the Commission's Guidance.

II. KEY FEATURES OF THE GUIDANCE

The Commission's Guidance sets forth the enforcement priorities and the relevant factors that the Commission staff will consider when investigating alleged exclusionary abuses committed by single dominant firms.⁶ It indicates what factors are relevant and what evidence should be provided in support in order to bring an exclusionary abuse case before the Commission. At various points, the Guidance refers to economic concepts, many of which will resonate relatively well with economists and legal practitioners on both sides of the Atlantic. The Guidance does not, however, outline a specific methodology for assessing the various factors or for assigning weight to each. Notwithstanding the general references to economic concepts, little is said about the analytical framework for applying them in any given case.

The Guidance rests on three important economic concepts, namely: (i) foreclosure of competitors' access to suppliers or customers as the initial step to demonstrate anticompetitive harm; (ii) a hypothetical "as efficient competitor" that should be protected from foreclosure; and (iii) economic efficiencies as possible justification for alleged harmful conduct.

The first concept reflects one of the fundamental differences between the approaches of the Commission and the DOJ. The Commission, like the DOJ, posits that enforcement action should be targeted towards practices that are the most harmful to consumers and that proceedings under Article 82 EC should be initiated only to protect

⁶The Guidance does not apply to exploitative abuses, such as excessive pricing, or to conduct by companies that jointly dominate a market.

the competitive process, not to protect less efficient competitors.⁷ One might therefore expect the Commission to lay down a consumer-focused test for assessing consumer harm. Instead, detrimental impact on consumer welfare is assessed through the prism of likely anticompetitive foreclosure effects; no evidence of (likely) negative impact on consumers is required. Intervention will thus be warranted when complainants provide convincing evidence of market dominance as well as information about the percentage of total sales affected by and the duration of the alleged anticompetitive conduct, possible evidence of actual foreclosure, and direct evidence of any exclusionary strategy.⁸ This sets the bar at a relatively low level for potential complainants and emphasizes effects on competitors—foreclosure—rather than consumers. In contrast, the DOJ expressed some doubt that “foreclosure” of rivals’ sales is enough to demonstrate consumer harm and its default standard for unilateral conduct—whether harm to competition is “disproportionate” to consumer benefits—attempts to identify specific harms to consumers caused by the unilateral conduct.⁹

The "as efficient competitor" test is used as the benchmark for determining whether a priced-based conduct is exclusionary. The idea is to preserve vigorous price competition without inhibiting even dominant firms from offering low prices that are not abusive. The Guidance discusses two measures of cost in order to determine whether a

⁷Guidance, para. 6.

⁸Guidance, para. 20.

⁹Report, pages viii, 23, 30. Interestingly, the FTC staff working paper on general standards for exclusionary conduct argued against both the Commission’s “as efficient competitor” and DOJ’s default “disproportionality” tests. See Karen L. Grimm, *General Standards for Exclusionary Conduct* 3, 19, 27-29, 31 (Nov. 3, 2008) (concluding in favor of a rule-of-reason approach of shifting evidentiary burdens within a framework of balancing anticompetitive harms against consumer benefits).

dominant firm's prices are so low as to exclude an "as efficient competitor" from the market. The Commission's initial rhetoric seems to parallel that of the DOJ, which repeatedly sought to identify levels of cost that could be used by businesses to guide their own decision-making. It focuses on the average avoidable cost ("AAC") and long-run average incremental cost ("LRAIC") of the dominant firm. Prices below the AAC, which includes all costs that could be avoided if the challenged pricing conduct did not occur, are presumed to cause losses in the short-term that could deter or drive out even an as efficient competitor from the market place. LRAIC is generally higher than AAC because it includes costs that could not be avoided by eschewing the challenged conduct. Unlike DOJ, which generally will consider the AAC as the relevant benchmark, the Commission indicates that it will ordinarily look at LRAIC as the dividing line between acceptable and unacceptable pricing by a dominant firm.¹⁰ In practice, therefore, unilateral conduct may be more likely to fail the Commission's cost test and attract enforcement scrutiny in Europe than in the United States.

The last important feature of the Commission's enforcement approach to exclusionary practices involves two defenses. The first defense the Commission will consider is that the challenged conduct was objectively necessary. Here, the Guidance does not revolutionize the Commission's practice. In particular, staff will continue to apply strict standards to claims that allegedly abusive conduct is objectively justified; namely, that such conduct must be indispensable and proportionate to the legitimate goal of the conduct. Although it has been articulated by defendants in recent cases, the second

¹⁰Guidance, para. 25.

defense is something of a new policy development. The Commission will now consider arguments that the challenged conduct creates economic efficiencies that benefit consumers overall. Like efficiencies arguments recognized in the field of restrictive practices and agreements between undertakings and mergers,¹¹ arguments offered to justify conduct challenged under Article 82 will have to show that the efficiency benefits to consumers outweigh any competitive harm to consumers and that the conduct generating the efficiencies does not eliminate all or most existing sources of competition.¹²

III. OVERVIEW OF SPECIFIC FORMS OF ABUSE

In addition to outlining a general framework for analysis, the Guidance discusses several specific forms of conduct. The Commission’s approach differs in several respects from that of the DOJ as outlined in its Report.

A. Exclusive Dealing

The Guidance characterizes any obligations imposed upon customers to purchase exclusively from a dominant company as a source of concern when the obligation is likely to harm consumers as a whole, in particular if competing sellers are prevented from entering the market or expanding sales. The Commission notes that it is particularly concerned when the dominant firm is an “unavoidable trading partner” for part of the customer demand, because it supplies a “must-stock” brand or because the rival does not

¹¹Guidance, Section III.D.

¹²Guidance, para. 29, last bullet point.

have the capacity to meet total customer demand. In such cases, even short-term exclusive dealing arrangements can be suspect.¹³

When exclusive dealing takes the form of conditional rebates; that is, when customers receive compensation for a particular form of purchasing behavior, the factors and assessment methods developed in *Michelin II*¹⁴ and *British Airways*¹⁵ should continue to apply. The price-based foreclosure effect will be assessed by comparing the "estimated effective price"—which is the normal (list) price paid by the customer less the rebate it loses by switching, computed over the range of sales affected by the rebate—with the LRAIC of the dominant firm. Prices above LRAIC will generally be deemed unobjectionable. Prices below LRAIC will require further investigation, with enforcement generally expected if the effective price falls below AAC.¹⁶ The Commission specifically notes, however, that even rebates that do not involve any sacrifice of profits by the dominant firm can objectionably foreclose rivals.¹⁷

In any case, the loyalty-inducing effect of the rebate scheme is further evaluated in light of its terms and conditions (i.e., whether it is incremental or retroactive, individualized or standardized, and over which relevant period).

The Commission considers that efficiencies are more likely to arise and outweigh any foreclosure effects when the rebate scheme is standardized and incremental rather than individualized and retroactive.

¹³Guidance, para. 35.

¹⁴Case T-203/01, *Michelin v. Commission (Michelin II)*, [2003] ECR II-4071.

¹⁵Case T-219/99, *British Airways v. Commission*, [2003] ECR II-5917.

¹⁶Guidance, para. 43.

¹⁷Guidance, para. 36.

The Commission's approach marks the first of several very stark contrasts to that of the DOJ. The DOJ is much readier to recognize economic benefits of exclusive relationships. Although the DOJ also expresses some concern that the practice can inhibit rivals, its caution to avoid deterring economically beneficial relationships is reflected in its requirement that any specific consumer harm identified after detailed fact-finding should be disproportionately greater than the economic benefits of the conduct.¹⁸

B. Tying and Bundling

The practices of tying and bundling the sale of multiple products have received much attention in Europe, particularly in view of the landmark decision of the European Court of First Instance in the *Microsoft* case affirming the illegality of technically tying the Windows Media Player with the Windows operating system.¹⁹ The Guidance lays down the basics of what complainants should pay attention to, in particular the need to demonstrate the existence of two distinct product markets and dominance on the tying product market. The Guidance then briefly articulates several mechanisms by which tying or bundling could anticompetitively foreclose competition by reducing customer demand for a rival's products, without, however, specifying thresholds or analytical methods to identify how much is too much. Of note is the Commission's expectation that anticompetitive foreclosure of rivals is more likely to occur when the tied or bundled products are technically linked. With respect to claims of greater efficiency, the Guidelines highlight reduced transaction and distribution costs.²⁰

¹⁸Report, pages xi, 140, 41.

¹⁹Case T-201/04, *Microsoft v. Commission*, [2007] ECR II-3601.

²⁰Guidance, para. 61.

Like exclusive dealing, tying and bundling are treated by the DOJ as more likely to be economically beneficial to consumers than the Commission would appear to accept. The DOJ's Report also discusses technical tying, which it considers often beneficial to consumers as a form of product innovation. In general, the DOJ will rely upon the same disproportionality test that it would employ in exclusive dealing cases.²¹

C. Predation

Under the Guidance, the Commission will take action against predatory conduct when a dominant firm sacrifices short-term revenues to drive competitors out of the market or deter new ones from entering. Pricing below AAC will be seen as a clear indication of such a sacrifice. However, the sacrifice does not necessarily require losses but can also be found in "net revenues lower than what could have been expected from a reasonable alternative conduct."²² To assess the likelihood of foreclosure, however, the Commission will compare effective prices with the dominant firm's LRAIC, which generally will be higher than AAC. As a practical matter, therefore, if conduct can be shown to yield effective prices below LRAIC and a "reasonable alternative" can be shown to yield higher net revenue, then the Guidance suggests that enforcement is likely. Although the Commission does not preclude all efficiency justifications, particularly regarding economies of scale or expanding the market, the Guidance expresses skepticism that predation can create efficiencies.

The Guidance also makes clear that the Commission will not require evidence that the dominant firm can recoup its sacrifice by charging higher prices after its predation

²¹Report, pages x, 90.

²²Guidance, para. 64.

succeeds in excluding or deterring rivals. Proof of overall profits to the dominant firm will not be required and likely consumer harm can be shown by evidence of likely foreclosure and the existence of entry barriers. Rather than embarking on second-guessing price levels that would have prevailed absent predation, the Commission considers that it is sufficient to examine the overall disciplining effect of the strategy, namely whether competitors could revert to their competitive behavior once the predatory pricing ends. Factors explaining how this may occur will be considered. In sum, the Commission does not mandate a showing of harm to consumers but merely the inability of competitors to resume their competitive behavior.

The Commission's policy differs markedly from that of DOJ. Concerned to avoid deterring pro-consumer price-cutting by dominant firms, DOJ's enforcement will insist on a much more stringent "sacrifice" test. Not only must the effective price fall below AAC, but the dominant firm must be shown capable of recouping its lost revenues and securing additional profits by having excluded or deterred rivals.²³

D. Refusal to Deal and Margin Squeeze

Refusal to deal is perhaps the dominant-firm conduct against which the Commission's enforcement has been most prolific in recent years. EU courts have also built up a well established line of cases, which is reflected in the Guidance. Concerns about input foreclosure have also generated much attention in the context of mergers,²⁴

²³Report, pages ix, 65, 67-68.

²⁴GUIDELINES ON THE ASSESSMENT OF NON-HORIZONTAL MERGERS UNDER THE COUNCIL REGULATION ON THE CONTROL OF CONCENTRATIONS BETWEEN UNDERTAKINGS, OJ C 265 of 18 October 2008.

and margin squeezes have been extensively examined in regulated industries, such as telecoms.²⁵

In its Guidance, the Commission largely borrows from *IMS Health*²⁶ and *Microsoft*.²⁷ Refusals to supply even a potential rival in a “downstream” market by a dominant firm in a potential market for the input may be found abusive. Such refusals to deal might involve not only manufactured goods or services, but also licenses of intellectual property and access to production facilities or networks. They also can involve refusals to supply both existing purchasers and proposed new customers of the dominant firm. In general, the Commission will seek to enforce against such refusals when:

1. they relate to a product or service that is objectively necessary in order to compete effectively in the downstream market;
2. they are likely to eliminate effective competition in the downstream market; and
3. the refusal is likely to lead to consumer harm.

Objective necessity, however, can be shown by demonstrating that rivals cannot effectively duplicate the input in the foreseeable future. Elimination of competition can be shown by demonstrating high market shares for the dominant firm in the downstream market.

Likely consumer harm may be inferred from the foreclosure, but also if the rival would be prevented from developing new products. The emergence of a “new” product,

²⁵See, *inter alia*, case T-271/03, *Deutsche Telekom v. Commission*, 10 April 2008, not yet reported.

²⁶Case C-418/01, *IMS Health v. NDC Health* [2004] ECR I-5039, paragraph 44.

²⁷Case T-201/04, *Microsoft v. Commission* [2007] ECR II-3601.

which was considered as a necessary condition for a finding of infringement in *IMS Health*,²⁸ has been qualified by the Court of First Instance in *Microsoft* to include also situations where the refusal prevents “technical development.”²⁹ Under the Guidance, the Commission seems to go a step further by treating the development of a new product as a sufficient condition for a finding of consumer harm. The Guidance indicates that harm is considered more likely when the refusal terminates an existing supply relationship.

In the case of businesses involved in any regulated industry that receive government funding or that developed their “upstream” market position “under the protection of special or exclusive rights,” the Guidance asserts that imposing an obligation to supply inputs to a downstream rival is unlikely to deter innovation by the dominant company and therefore the Commission would not require any of these three factors to be assessed before intervening.³⁰

This last area of unilateral conduct involves the most striking difference between the policies of the Commission and DOJ. In contrast to the Commission’s evidently heightened concern, DOJ’s Report argues strongly that the traditional “essential facilities” doctrine³¹ and the related suspicion of disrupting an existing supply relationship with a rival should be abandoned in their entirety. So strongly does DOJ hold

²⁸Case C-418/01, *IMS Health v. NDC Health* [2004] ECR I-5039, paragraph 38.

²⁹Case T-201/04, *Microsoft v. Commission* [2007] ECR II-3601, paragraph 647.

³⁰Guidance, para. 80.

³¹This doctrine was not endorsed by the U.S. Supreme Court in *Verizon v. Trinko*, 540 U.S. 398 (2004).

these views that the Report states squarely that unilateral refusals to deal should not play a meaningful part in its enforcement efforts.³²

IV. CONCLUDING REMARKS

The Commission and the DOJ have come up with diverging policy reports, each after having carried out a thorough review of their respective enforcement case-law and practice in relation to unilateral conduct. With the Guidance, the Commission has now formally endorsed economic effect-based analysis in the area of unilateral exclusionary practices. However, while both agencies use similar economic concepts and theories, they come to markedly diverging enforcement visions.

First, the Commission is less concerned about showing actual harm to consumers than the DOJ. For the Commission, evidence that the conduct is likely to result in anticompetitive foreclosure suffices. Second, the Commission will balance the perceived anticompetitive effects against the proffered pro-competitive benefits of the conduct, whereas the DOJ will find a practice unlawful only if the harm is substantially disproportionate to the pro-competitive benefits. Third, in relation to pricing behavior, the Commission will use LRAIC as the relevant benchmark against which to assess the likely exclusionary effects of the conduct under investigation. In contrast, the DOJ considers the AAC as the relevant benchmark.

It remains to be seen whether the above-stated policy differences will result in significant diverging enforcement actions and outcomes in the years to come.

³²Report, pages xi, 129.