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***Verbalising a General Test for
Exclusionary Conduct under Article 82 EC***

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Verbalizing A General Test For Exclusionary Conduct Under Article 82 EC
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This paper considers the vexed issue of how to verbalize a generally-applicable definition of exclusionary conduct under laws relating to unilateral behaviour (or “monopolization”, in US antitrust law parlance), such as Article 82 EC.

The issue is of obvious practical importance: business firms that are, or may be, dominant need reasonably clear guidance on fundamental matters such as the restrictions on their unilateral pricing conduct and to what extent they are obliged to deal with third parties with whom they do not wish to deal. Equally, in many sectors such as recently-liberalized utility sectors, new entrants face serious market entry obstacles as a result of abusive vertical foreclosure, e.g., discrimination, denial of access, quality degradation, etc. There is thus a clear need both for enforcement and for rules that companies themselves can reasonably apply *ex ante*.

The issue is also highly topical. The EU Commission's review of Article 82 is continuing, with a draft set of guidelines expected later in 2007. The US antitrust agencies also concluded, on 8 May 2007, their year-long hearings on single-firm conduct.¹

Unfortunately, however, the basic test for exclusionary conduct has not been clarified to any great extent. The application of Article 82 to exclusionary conduct has been described as “vague” and “conclusory”.² Similar criticisms have been voiced in the United States,³ where leading antitrust thinkers have described the treatment of unilateral abusive conduct as “the biggest substantive issue facing antitrust”.⁴

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¹ Comprising 18 days of hearings, 28 different panels, and 130 panellists drawn from a range of stakeholders (e.g., lawyers, economists, business people, academics, and business historians).

² Robert O'Donoghue and A. Jorge Padilla, *The Law And Economics Of Article 82 EC*, Hart Publishing, 2006, p. 177.

³ See Einer Elhauge, “Defining Better Monopolization Standards”, 56 *Stanford Law Review* 253 (2003).

⁴ Richard A. Posner, “Vertical Restraints and Antitrust Policy”, 72 *University of Chicago Law Review* 229 (2005).

Given the uncertain and vague nature of current definitions of exclusionary behaviour, lawyers and economists have made a number of recent proposals that seek to offer a unified definition of exclusionary conduct.⁵ These include the “profit sacrifice” test and its close cousin the “no economic sense” test, the “equally efficient competitor” test, the “consumer welfare” test, and the “limiting production to the prejudice of consumers” test. These tests obviously have much in common, but their principal proponents have also sought to argue that alternative tests are flawed and mutually exclusive.

This paper outlines some general considerations that should guide the framing of useful, operational rules for unilateral conduct, and in particular the relevance of error costs, the need for administrable *ex ante* rules, and the problems of imperfect information (Section I). It then considers the main elements of each of the principal tests proposed for the assessment of exclusionary conduct, followed by the principal criticisms aimed at them (Section II). The role of efficiencies is also then considered, as this is a central element in many of the proposed tests (Section III). Finally, a tentative conclusion is set out on the usefulness of each test as an operational rule (Section IV).

I. Designing Optimal Rules

Legal rules, including competition law rules, should be designed in a way that makes their enforcement efficient and practical.⁶ This is premised on the notion that perfect information allowing competition authorities and courts to weigh the pro-competitive and anticompetitive effects of a practice in every case will almost never be available. A related point is that, for unilateral conduct, it is not reasonable to expect firms to subject everyday business decisions to detailed balancing analysis to scrutinize their compatibility with competition law. For example, firms operating on an EU-wide basis cannot reasonably be expected to assess the consumer welfare impact of offering different prices and terms and conditions in each Member State, in order to avoid unlawful discrimination claims under Article 82(c). In most instances, the sheer multiplicity of different countries, customers, prices, and factors that lead to pricing changes make this wholly impractical. Antitrust commentators therefore propose that legal rules should be guided by several considerations that make their enforcement optimal. Two particular considerations bear mention: (1) error costs; and (2) form versus effects rules.

⁵ For an overview of the main tests, see John Vickers, “Abuse of Market Power,” Speech to the 31st conference of the European Association of Research in Industrial Economics, Berlin, 3 September 2004. See also Organisation for Economic Co-operation and Development, “Competition on the Merits,” Background Note, 9 May 2005.

⁶ See, e.g., Richard Posner, “An Economic Approach To Legal Procedure And Judicial Administration” 2 *Journal Of Legal Studies* 399 (1973). For a recent application more specific to unilateral conduct, see David Evans, “How Economists Can Help Courts Design Competition Rules: An EU And US Perspective”, 28(1) *World Competition* 93 (2005).

A. Error Costs

In competition law, the optimal theoretical legal rule would always identify anticompetitive conduct while always allowing pro-competitive conduct to go unpunished. Unfortunately in practice, virtually all legal rules suffer from imperfections as a result of lack of information, enforcement, and other sources of potential error (e.g., lack of expertise). These difficulties mean that competition rules must grapple with the dangers of allowing anticompetitive practices to go unpunished (so-called “false negatives” in statistical parlance) and or treating pro-competitive practices as anticompetitive (so-called “false positives”).

Which of the two errors is likely to be more costly depends on whether a particular practice is, on balance, more likely to lead to harm or good. On a very general level, there are probably good reasons why the risk of over-deterrence is greater than under-deterrence in the context of Article 82. Competition laws are generally more hostile to collusive arrangements between firms (be they mergers or other agreements) than they are to unilateral conduct. This is mainly on the assumption that competitive harm is generally more likely to occur from two or more firms agreeing to limit their output than unilateral action by one firm. Put differently, it is one thing for a firm to acquire market power through superior products or skill, but quite another for two or more firms to restrict competition between them in favour of cooperative arrangements that confer market power. This distinction is not necessarily hard and fast – many dominant firms may acquire a monopoly position by means other than skill and foresight (e.g., where the government grants them special or exclusive rights) – but it is probably correct, as a general matter, to treat market power that results from an agreement between two or more firms differently from the way unilateral action by a firm with market power is treated.

Regarding specific types of abusive practices, Article 82 already incorporates certain rules that reflect concerns for over-deterrence and under-deterrence. A good example concerns unconditional price cuts by a dominant firm. Price competition is of course to be encouraged. At some point, however, price competition may cause harm to consumers, where for example a dominant firm charges low prices to cause rivals’ exit, and later recoups its investment through increased prices in future. While the precise measurements differ, economists have long argued that firms should be presumed to be acting lawfully when prices are above production costs, usually marginal cost or some analogous measure. This insight is captured by the first rule on predatory pricing in the *AKZO* case, that prices below average variable cost (a proxy for marginal cost) are presumed to be exclusionary.⁷ (However, even that presumption has been relaxed in recent years given the legitimate reasons why a dominant firm might price below cost for a period, e.g., in order to introduce new products, or to build a network.)

⁷ See Case C-62/86, *AKZO Chemie BV v Commission* [1991] ECR I-3359, paras. 70-71.

Some economists have also devised theoretical models showing that prices above cost can sometimes harm consumer welfare.⁸ The basic idea is that less efficient rivals can bring about reductions in price that are sufficient to compensate for their relative inefficiency, as well as the notion that many of them will become as or more efficient over time. But this insight has not led to general restrictions on above-cost price cuts under Article 82, precisely because of the very high risk of wrongly condemning aggressive, but legitimate, price competition. Instead, such price cuts have been condemned in only exceptional cases, usually where the firm in question is a virtual monopolist and/or the pricing strategy is part of a series of abusive acts with the same aim.⁹ Many commentators would argue that even this exception goes too far and risks false positives. But there is nonetheless a strong consensus that above-cost unconditional price cuts should be presumed lawful in all but extreme cases.

B. Form Versus Effect

An evaluation of the risks of false negatives and positives, and prior beliefs about the degree of benefit and harm of particular practices, has led to the application of different types of tests for antitrust rules. At one extreme are practices that subject to *per se* legality or illegality rules, i.e., the practice is deemed lawful or unlawful without the need for a detailed inquiry into its actual or likely effects on competition. A *per se* rule may be absolute in the sense that no exceptions are permitted or modified in the sense that a rebuttable presumption of legality or illegality applies. *Per se* rules are only appropriate where: (1) experience and logic suggest that the benefit/harm resulting from a practice is so clear and unambiguous that there is no point in wasting court or regulatory resources in investigating its effects; and (2) the risk of false positives or false negatives is small. The only universally accepted *per se* antitrust rule is hard core horizontal price-fixing.

At the other extreme lie “rule of reason” inquiries, where the benefits and harm caused by a practice are carefully evaluated. This inquiry may be structured, in the sense that conduct is evaluated through a series of screens to distinguish lawful and unlawful conduct, or it may be unstructured in that harm and benefits are simply assessed and compared. Economists overwhelmingly agree that a rule of reason (or effects) based approach is appropriate when dealing with unilateral conduct, and they have criticized past policy under Article 82 EC for its excessive reliance on form over effects. A recent report by the Economic Advisory Group on Competition Policy on Article 82 EC – which was commissioned by the Chief Economist of DG Competition – proposes an effects-based approach for the following reasons:¹⁰

⁸ See Mark Armstrong and John Vickers, “Price Discrimination, Competition, and Regulation”, 41(4) *Journal of Industrial Economics* 335 (1993).

⁹ See, e.g., Joined Cases C-395/96 P and C-396/96 P, *Compagnie Maritime Belge Transports SA, Compagnie maritime belge SA and Dafra-Lines A/S v Commission* [2000] ECR I-1365.

¹⁰ See Report by the Economic Advisory Group on Competition Policy, “An Economic Approach to Article 82,” July 2005, available at: http://ec.europa.eu/comm/competition/publications/studies/eagcp_july_21_05.pdf, at p. 6.

“A more consistent approach would start out from the effects of anticompetitive conduct ... and consider the competitive harm that is inflicted on consumers. Adopting such an effects-based approach would ensure that these various practices are treated consistently when they are adopted for the same purpose. In contrast, a form-based approach creates the risk that they will be treated inconsistently, with some practices possibly enjoying a relatively more lenient attitude (e.g., because of different standards). Arbitrating among these different treatments may facilitate exclusion, or induce the dominant firm to adopt alternative exclusionary methods, which may well inflict a higher cost on consumers.”

Another way of looking at these types of rules is to consider whether unilateral practices should be assessed on the basis of their form or actual or likely effect. Historically, a number of practices under Article 82 could have been regarded as being subject to *per se* illegality rules. Exclusive dealing, for example, was subject to a strong presumption of illegality in earlier cases such as *Suiker Unie* and *Hoffmann-La Roche*.¹¹ This presumption has been relaxed in recent cases, most notably in *Van den Bergh*,¹² as a result of which exclusive dealing under Article 82 is now more aptly characterized as being based on a rule of reason, much in the same way as a rule of reason applies under Article 81.

Similarly, regarding predatory pricing, the *AKZO* case suggested that pricing below average variable cost is subject to a *per se* rule. This finding has also been relaxed in recent cases, in line with economic thinking indicating that pricing below average variable cost may have a non-exclusionary explanation. For example, in *Wanadoo*, the Commission did not conclude that the dominant firm’s prices were unlawful from the mere fact that they were below average variable cost for a significant period; rather, the Commission also looked at the strategic rationale for those prices and their effects on competition. The current rules might therefore best be described as constituting a regime of modified *per se* illegality.

Finally, individualized retroactive loyalty rebates that apply over a relatively long reference period were also effectively subject, in the past, to a *per se* illegality rule (absent objective justification).¹³ Again, however, this rule has been substantially relaxed and has shifted towards a rule of reason-type inquiry, with some structural screens to eliminate unproblematic cases.¹⁴ In sum, there are now virtually no practices that could be described as *per se* unlawful under Article 82.

¹¹ See Joined Cases 40 to 48, 50, 54 to 56, 111, 113 and 114/73, *Coöperatieve Vereniging “Suiker Unie” UA and others v Commission* [1975] ECR 1663; and Case 85/76, *Hoffmann-La Roche & Co AG v Commission* [1979] ECR 461.

¹² See Case T-65/98, *Van den Bergh Foods Ltd v Commission* [2003] ECR II-4653.

¹³ See Denis Waelbroeck, “*Michelin II: A Per Se Rule Against Rebates by Dominant Companies?*” 1 *Journal of Competition Law & Economics* 149–71 (2005).

¹⁴ See *Prokent/Tomra*, Decision of 29 March 2006, where the Commission claims to have applied a more lenient approach. No published decision is available, however, against which this claim can be verified. For the Commission’s views, see Frank Maier-Rigaud and Dovile Vaigauskaite, “*Prokent/Tomra, a textbook case?*”, *DG COMP Competition Newsletter*, 2006 No 2, pp. 19–24. The Court of Justice in *British Airways* seems to have applied something akin to a *per se* approach to retroactive rebates, but the case seems largely reflective of the

In between the *per se* and pure effects approaches lies an intermediate approach where simple error-cost analysis, based on economic evidence, is used to structure administrable legal rules (a “structured rule of reason”). Such rules can help bridge the gap between a formal (and most likely prescriptive) approach and a pure effects-based approach (which is unlikely to yield much by way of business certainty *ex ante*). Take above-cost unconditional price cuts. On the basis of economic theory, the case may be made that such price cuts can harm consumer welfare in certain circumstances. But no clear legal rule has been devised to say when harm to consumer welfare occurs. Absent a clear rule, restricting unconditional above-cost price cuts is likely to greatly chill price competition. The optimal solution might therefore be to do nothing, even if in so doing certain anticompetitive practices thereby escape censure. However, under Article 82, the situation is one of modified *per se* legality: unconditional above-cost pricing is presumed legal absent exceptional circumstances (e.g., action by a virtual monopolist, industries with very high fixed-variable costs ratios).¹⁵

This debate has also found its way into the discussions of the Article 82 reforms. But the choice sometimes posited between an approach based on legal form and one based on economic effects is to some extent false and ignores a number of practical considerations. Relying only on legal form almost certainly leads to incorrect conclusions by ignoring the mixed economic effects of many unilateral practices. More importantly, if a form-based approach were adopted, it would be of limited practical importance, since *per se* legality guidance would almost certainly be offered only for a handful of practices that companies probably already know are legal. (As noted above, almost no practice is *per se* illegal now under Article 82, so telling firms what they certainly cannot do is likely to be of limited use in practice.) In other words, by its nature, general guidance for dominant firm conduct will not be permissive. Equally, however, proponents of an economic effects analysis also need to recognize that the law would be *much* less clear than it is already if each case depended on an assessment of the economic benefits and harm produced by a given type of conduct, most of which can only be assessed *ex post* (if at all). Economists sometimes underestimate the importance of legal certainty to businesses.

II. The Principal Suggested Tests For Exclusionary Conduct

The search for clearer standards in abuse of dominance cases has led to a proliferation of different general tests for exclusionary conduct. Many of these tests are closely related –

Court’s unwillingness to re-assess what it classified as findings of fact by the Court of First Instance in the same case. The Court’s judgment does not in any event necessarily preclude an effects-based approach, since it held that the discounts must have an “exclusionary effect”. See C-95/04 P, *British Airways v Commission*, judgment of 15 March 2007, not yet reported, para. 68.

¹⁵ See *Cewal, Cowac and Ukwal*, 1993 OJ L34/20, upheld by the CFI on appeal in Joined Cases T-24/93, T-25/93, T-26/93, and T-28/93, *Compagnie Maritime Belge Transports SA and Others v Commission* [1996] ECR II-1201 and by the ECJ in Joined Cases C-395/96 P and C-396/96 P, *Compagnie Maritime Belge Transports SA and Others v Commission* [2000] ECR I-1365.

certainly more so than some of their proponents would seem to suggest. The main tests are as follows:

- ***Profit sacrifice/no economic sense.*** A first test is based on the notion of profit sacrifice, meaning that exclusionary conduct requires a firm to deliberately forego a more profitable course of action.¹⁶ A closely-related cousin is the “no economic sense” test, which would treat conduct as exclusionary if it would make no economic sense but for its tendency to exclude rivals.¹⁷
- ***Equally-efficient competitor test.*** A second test is the equally efficient competitor test.¹⁸ This holds that the only conduct that is exclusionary is that which would exclude an equally or more efficient rival. Conduct that excludes less efficient rivals is deemed to be competition “on the merits”, on the ground that the competitive process would result in the elimination of such undertakings in any event.
- ***Consumer welfare test.*** A third suggested test is a test based on consumer welfare. Under this test, only conduct that harms consumer welfare, or harms consumer welfare more than it enhances efficiency, is considered exclusionary.¹⁹ This test is expressly rooted in the objective of maximizing consumer welfare.

The main elements of the foregoing tests, and the principal criticisms, are outlined below. But the differences between these tests should not be overstated. In essence, each seeks: on the one hand, to identify situations in which conduct is inefficient and hence anti-consumer; and, conversely, to allow efficient conduct that yields consumer benefits over time. There is also a fourth test:

- ***Limiting production.*** This final test is expressly grounded in the wording of Article 82(b), which states that “limiting production, markets or technical development to the prejudice of consumers” is illegal. In its most

¹⁶ The profit sacrifice test was originally proposed by industrial economists in the early 1980s. See Janusz Ordover and Robert Willig, “An Economic Definition of Predation: Pricing and Product Innovation” 91 *Yale Law Journal* 8 (1981). The test was intended to provide an objective, transparent, and economically based framework for assessing exclusionary unilateral behaviour. The economists defined exclusionary behaviour as a “response to a rival that sacrifices part of the profit that could be earned under competitive circumstances were a rival to remain viable, in order to induce exit and gain consequent additional monopoly profits”. *Ibid.*, pp. 9-10.

¹⁷ See Gregory Werden, “The ‘No Economic Sense’ Test for Exclusionary Conduct,” paper submitted to the British Institute of International and Comparative Law, 5th Annual Antitrust dialogue, London, 9-10 May 2005.

¹⁸ Richard Posner, *Antitrust Law*, 2nd ed., University of Chicago Press, 2001, pp. 194-95.

¹⁹ See Andrew Gavil, “Exclusionary Distribution Strategies by Dominant Firms: Striking a Better Balance”, 72 *Antitrust Law Journal* 3 (2004); Steven Salop, “Section 2 Paradigms and the Flawed Profit-Sacrifice Standard”, available at: www.crai.com.au/agenda/salop%20paper.pdf; Maurits Dolmans, “Efficiency Defences Under Article 82 EC Seeking Profits Or Proportionality? The EC 2004 *Microsoft* Case in the Context of *Trinko*,” 24th Annual Antitrust And Trade Regulation Seminar, NERA, Santa Fe, New Mexico 8 July 2004 (on file with author).

basic form, this test suggests that foreclosure or handicapping of competitors, by which competition is reduced still further, is illegal if harm to consumers would actually or likely result.²⁰

A. Profit Sacrifice/No Economic Sense

Elements of the profit sacrifice test. The profit sacrifice test assumes that a firm would not rationally engage in exclusionary conduct unless it considers that any short-term sacrifice of profits would be more than compensated for by the expected gains as a result of the exclusion or discouraging of rival firms if the conduct is successful. The most obvious example concerns predatory pricing. The theory is that a firm would not knowingly sell below cost unless it had a reasonable expectation that short-term losses will be offset by the additional profits that follow in the medium- to long-term from the exclusion of rivals. The issue of recoupment – which arguably plays a role under Article 82 – in effect seeks to measure whether profit sacrifice would be rational by assessing whether the longer term gains of below-cost pricing are likely to outweigh its short-term costs. (This is not, however, a strictly mathematical question, but involves a more general inquiry as to whether the predator could increase or maintain market power in the future.)

Recent antitrust case law in the US has endorsed a profit sacrifice test to some extent, but judicial acceptance of the test has been mixed. In *American Airlines*,²¹ the Department of Justice (as plaintiff) argued that the appropriate inquiry in a predatory pricing case was whether incrementally-added capacity was money losing, even if the service provided by the incumbent airline remained profitable overall on the relevant city pair. The 10th Circuit held that, even under the standard advanced by the DOJ itself, it had not been demonstrated that the additions of capacity at issue were unprofitable.²²

In *Trinko*,²³ the DOJ (as *amicus curiae*) advocated essentially the same sacrifice test for assessing unilateral refusals to deal. Although the Supreme Court's majority opinion did not expressly refer to the sacrifice test, it justified past cases in which a duty to deal was imposed on the basis that the defendant had foregone a more profitable course of conduct in refusing to deal. For example, in its discussion of *Aspen Skiing*, the Court attached importance to the fact that the defendant had refused to deal even when the requesting party offered a price equal to the retail price charged by the defendant downstream. It pointed to the defendant's willingness to forego short-term benefits through "[t]he unilateral termination of a voluntary (and thus presumably profitable) course of dealing", and its "unwillingness to

²⁰ See John Temple Lang and Robert O'Donoghue, "The Concept Of An Exclusionary Abuse", *Global Competition Law Centre Research Papers on Article 82 EC*, College of Europe, July 2005, p. 38, available at: <http://www.coleurop.be/content/gclc/documents/GCLC%20Research%20Papers%20on%20Article%2082%20EC.pdf>.

²¹ *United States v AMR Corp*, 140 F. Supp. 2d 1141 (D. Kan. 2001), *affirmed*, 335 F.3d 1109 (10th Cir. 2003).

²² See R. Hewitt Pate, "The Common Law Approach and Improving Standards for Analysing Single Firm Conduct," Fordham International Antitrust Conference, New York, 23 October 2003.

²³ *Verizon Communications Inc v Law Offices of Curtis V. Trinko LLP*, 540 US 398 (2004).

renew the ticket *even if compensated at retail price*”, as facts that suggested its “distinctly anticompetitive bent”. As a result, the DOJ has indicated that it plans to assert the sacrifice standard with renewed confidence following *Trinko*.²⁴

Criticisms of the profit sacrifice test. The profit sacrifice test has been criticized in important respects. The first set of criticisms is fundamental in nature. Certain commentators have argued that the test is flawed in two critical respects.²⁵ First, they argue that a number of types of conduct do not involve profit sacrifice, but have been recognized as exclusionary. For example, filing a false or overbroad patent application may be cheaper than filing a correct and properly-defined one. The same point can be made about other forms of non-price predation (e.g., falsely disparaging a rival), reprisal abuses, and anticompetitive forms of raising rivals’ costs. A profit sacrifice test would therefore seem to wrongly exclude such abuses.²⁶

A second criticism is that a profit sacrifice test could capture a number of forms of highly desirable market activity. For example, in the area of intellectual property or major investments in tangible property, the initial investments would typically be unprofitable but for the prospect of later monopoly returns reaped by (lawfully) excluding competitors. A literal application of the sacrifice test might treat such investments as predatory despite the fact that, in general, they clearly benefit consumer welfare by offering a better market option. Of course, it might be argued that good sense would prevail in such circumstances and that the conduct in question would be seen as creating dynamic benefits. But a rule that contains exceptions based on the notion that “we will know them when we see them” is precarious.

Another set of criticisms concerns the ease of application and predictability of the profit sacrifice test in practice. A number of difficulties are said to arise.²⁷ First, there is the problem of determining the sacrifice: a sacrifice relative to what? It is not clear, for example, whether the profit sacrifice requires a firm to opt for the *most* profitable course of action to avoid a finding of exclusionary conduct or whether it should be required to have passed on a *more* profitable alternative. (Presumably, it is the latter.) It is also not clear what degree of sacrifice would be sufficient to establish exclusionary conduct or whether the rule is a strict one, i.e., is any profit sacrifice automatically abusive?

Second, many abuse of dominance cases do not involve extending a monopoly and increasing profits; instead, they concern actions designed to *maintain* a monopoly. For example, a reprisal abuse may be carried out simply to make clear to rivals and customers that

²⁴ See “The Struggle For Standards”, remarks by J. Bruce McDonald, Deputy Assistant Attorney General, Antitrust Division, US Department of Justice, presented at American Bar Association Section of Antitrust Law, Spring Meeting, Washington, D.C., 1 April 2004 (quoting *Trinko*, cited in previous footnotes (emphasis in original)).

²⁵ See Elhauge, *supra* note 3.

²⁶ See Brief for the United States and Federal Trade Commission as *Amici Curiae* Supporting Petitioner, *Verizon Communications, Inc v Law Office of Curtis V. Trinko LLP*, No. 02-682 (docketed US Sup. Ct. Dec. 13, 2002).

²⁷ See S Salop, *supra* note 19.

aggressive competition (or actions by customers to support rival firms, or complaints to competition authorities, etc.) will meet with an immediate response by the dominant firm. In such cases there may be no additional profits resulting from the dominant firm's conduct, but it may serve to insulate an existing dominant position from future erosion. This also exposes a related problem: that the dominant firm's current prices may *already* be above the competitive level. In this case, the absence of higher prices as a result of the exclusionary conduct could falsely show an absence of exclusionary effect on the grounds that no sacrifice occurred (a variant of the "cellophane fallacy").

Finally, although one of the main benefits of the profit sacrifice standard is said to be its objectivity,²⁸ it is argued that the test would in practice be highly subjective and speculative. In its most basic form, the profit sacrifice test asks a court to assess the dominant firm's likely conduct in the hypothetical absence of an ability to raise prices. This is hypothetical, speculative, and uncertain. Different outcomes could be imagined on the basis of the same set of facts.

The no economic sense test as a variant of profit sacrifice. Criticism of the profit sacrifice test has led the DOJ to argue for a variant of it: the "no economic sense" test. The DOJ has argued in recent antitrust cases that it is relevant to ask whether the conduct would make economic sense for the defendant but for its tendency to eliminate or lessen competition. According to the Department, conduct is not exclusionary or predatory if it would not make economic sense for the defendant but for its tendency to eliminate or lessen competition.²⁹ The DOJ contends that this type of "sacrifice" is a more accurate measure for exclusionary abuses than profit sacrifice, as it entails a choice between a business strategy that would make no business sense but for the probability that the conduct would create or maintain monopoly power.³⁰

The no economic sense test certainly addresses some of the criticisms of the profit sacrifice test. In particular, it does not characterize as unlawful every departure from short-run profit maximisation. This would permit investments that confer long-term benefit by allowing a firm to retain exclusive control over its inventions, something that could in theory be regarded as suspect under the profit sacrifice standard. But it is clear in some instances, particularly those involving network effects, that the elimination of competition, and the survival of a single competitor, is beneficial. Investments in network effects of this kind would only make economic sense if rivals are eliminated. It is not clear how such cases would be treated under the no economic sense test, but they could in theory result in a finding of exclusionary conduct. (Again, however, one would hope that common sense would prevail in this instance.)

A further problem is that the no economic sense test involves an assessment of the range of options that were open to the company at the time it embarked on a particular course

²⁸ See, e.g., Mark Patterson, "The Sacrifice of Profits in Non-Price Predation", 18 *Antitrust* 37 (2003).

²⁹ Brief for the United States and Federal Trade Commission, *supra* note 26.

³⁰ *Ibid.*

of conduct. In most cases, the best evidence of a company's options will be its business plans. Assessing whether a course of conduct made sense only if competitors were eliminated on the basis of such plans is extremely difficult in practice. For example, assume that a firm enters a new market in which initial capital costs are very high, and assume that it needs to acquire scale and scope economies and learning experience to reduce costs and achieve profitability, i.e., the firm needs to acquire volume. There is no effective way in this scenario of distinguishing between volume growth that is justified in itself and volume growth that is predicated, in whole or in part, on the elimination of a rival. It may be that, in this instance, the firm would pass the no economic sense test on the basis that there was a reasonably anticipated non-exclusionary reason for its strategy (even if that turned out to be wrong). But this is not obvious and, even if it were, this approach runs the risk of being under-inclusive by allowing exclusionary conduct in the vital early stages of a new market to go unchecked. Of course, these types of cases are difficult under any test, but the point is that, in this regard, the no economic sense test does not appear to have any unique advantages over the profit sacrifice test, or any of the others discussed here.

B. Equally Efficient Competitor Test

Elements. Exclusionary conduct has also been defined as conduct that would exclude an equally efficient rival firm. This definition was originally proposed by Judge Posner in his seminal book, *Antitrust Law*. The latest edition of the book offers the following definition of exclusionary conduct:³¹

“[T]he plaintiff must first prove that the defendant has monopoly power and second that the challenged practice is likely in the circumstances to exclude from the defendant's market an equally or more efficient competitor. The defendant can rebut by proving that although it is a monopolist and the challenged practice is exclusionary, the practice is, on balance, efficient ... [P]ractices that will only exclude less efficient firms, such as a monopolist's dropping his price nearer to (but not below) its costs, are not actionable, because we want to encourage efficiency. Only when monopoly power is used to discourage equally or more efficient firms and thus perpetuate a monopoly not supported by superior efficiency should the law step in. Even then, it should be alert to the possibility that the exclusionary effect of the monopolist's practice is offset by efficiency gains.”

The equally efficient competitor test certainly has some basis under Article 82. For example, the *AKZO* predatory pricing rules are grounded in the economic insight that a profit-maximizing dominant firm should be allowed to price down to the level of its average variable costs. This applies even if the dominant firm's costs are lower than those of rivals. Similarly, the test usually applied in margin squeeze cases – whether the dominant firm's own downstream arm could trade profitably if it had to pay the same input prices as third parties –

³¹ Posner, *supra* note 18, pp. 194–96.

relies on an equally efficient competitor test. Indeed, in *Bronner*, Advocate General Jacobs made clear that “the primary purpose of Article [82] is to prevent distortion of competition – and in particular to safeguard the interests of consumers – rather than to protect the position of particular competitors”.³² Consumers are generally best served by the most efficient firms, i.e., those with the lowest costs.

Criticisms of the equally efficient competitor test. A number of criticisms can be made of the equally efficient competitor test. First, examining whether a firm with similar levels of efficiency compared to the dominant firm will generally be of limited relevance where firms compete on the basis of differentiated products. In this circumstance, the products’ perceived qualities will typically be a more important parameter of competition than relative efficiency levels.

Second, less efficient competitors can, in theory, enhance consumer welfare when the increased competition they bring in the market benefits consumers more than the cost of their relative inefficiency.³³ For this reason, the duties imposed on dominant firms under Article 82 are not limited to equally efficient competitors, but, exceptionally, may include duties towards less efficient firms. Under the *CEWAL* line of case law, unconditional price cuts that remain above the dominant firm’s average total costs may be abusive in certain circumstances. Rules seeking to place restrictions on unconditional above-cost price cuts can be criticized, mainly on the grounds that they are in practice likely to chill desirable competition, but it is undeniable that a number of existing rules under Article 82 assume that less efficient firms can confer a net benefit on consumer welfare. This suggests that the “equally efficient rival” test could not be unreservedly accepted under Article 82.

A third problem concerns the definition of equal efficiency where the dominant firm has a first mover or some other cost advantage over new entrants, or where rivals have not yet reached their minimum efficient scale. For example, in the area of conditional above-cost pricing schemes (e.g., loyalty rebates), much of the current uncertainty in the law stems from how to treat economies of scale for purposes of defining an “equally efficient firm”. The objection in such cases is usually that the dominant firm’s large volume of past sales gives it a scale or scope advantage over rivals and that, by extending this advantage to marginal units and customers, the dominant firm can sometimes offer prices at the margin that a rival only competing for the marginal units cannot match. While there is some merit in the view that only the most efficient firm should serve a customer, the Commission has taken the opposite approach in several cases.

Fourth, for certain types of abuses, the concept of equal efficiency is of limited use when assessing the legality of conduct. For example, in the case of false declarations by a

³² See Opinion of Advocate General Jacobs in Case C-7/97, *Oscar Bronner GmbH & Co KG v Mediaprint Zeitungs- und Zeitschriftenverlag GmbH & Co KG, Mediaprint Zeitungsvertriebsgesellschaft mbH & Co KG and Mediaprint Anzeigengesellschaft mbH & Co KG* [1998] ECR I-7791, para. 58.

³³ See, e.g., Armstrong and Vickers, *supra* note 8. See also Aaron Edlin, “Stopping Above-Cost Predatory Pricing”, 111 *Yale Law Journal* 941 (2002).

dominant firm to regulatory approval agencies, or concealment of essential patents within the context of standard setting organizations, rivals' relative efficiency will be of little relevance if the action in question materially limits their access to the market. Of course, a less efficient firm is, all things being equal, likely to be more adversely affected by conduct of this kind by a dominant firm than an equally efficient one, but this issue goes more to the effects of the practice rather than the definition of operational rules as to when certain conduct is abusive or not.

Finally, the equally efficient competitor test may require complex balancing exercises in some cases where the conduct would harm an equally efficient firm, but generates efficiencies sufficient to offset this harm. Of course, efficiencies, if asserted, would also need to be assessed under any other test used for exclusionary abuses, but the point is that the outcome of the equally efficient competitor test may not always be predictable by a firm at the time when it embarks on a particular course of action.³⁴

C. Consumer Welfare Test

Elements. The third test seeks to shift the focus away from the economic motivation for the alleged exclusionary conduct, and from the relative efficiency of competitors, towards an assessment of whether the dominant firm's practices had, or are likely to have, a material adverse effect on consumer welfare.³⁵ Under this test, exclusionary conduct would violate Article 82 if "it reduces competition without creating a sufficient improvement in performance to fully offset these potential adverse effects on prices and thereby prevent consumer harm".³⁶ In other words, only conduct that produces *net* anticompetitive effects would be regarded as exclusionary.

An analysis of whether the conduct causes net harm to consumer welfare would take account of all available information relevant to the likely effects of conduct on

³⁴ Another efficiency-based test, proposed by Professor Elhauge, focuses on whether the alleged exclusionary conduct increases the firm's dominance because it enhances its own efficiency or only because it limits rivals' production. As he explains: "The proper monopolisation standard should instead focus on whether the alleged exclusionary conduct succeeds in furthering monopoly power (1) only if the monopolist has improved its own efficiency or (2) by impairing rival efficiency whether or not it enhances monopolist efficiency ... which would permit the former conduct and prohibit the latter." Elhauge, *supra* note 3, at 253. This test certainly has certain advantages over some of the other tests. In particular, it avoids complex *ex post* balancing acts where conduct is both exclusionary and efficient. It also treats efficiency-enhancing conduct by a dominant firm as presumptively lawful, whereas in certain situations under the profit sacrifice test it might not be (e.g., long-term investments in intellectual property or in tangible assets). Vague phrases such as "competition on the merits" and "normal competition" are also avoided under this test. But use of this test as an operational rule remains untested in practice. It would still need to be decided whether conduct is efficiency-enhancing or efficiency-reducing, which is often complex. Moreover, the articulation of the test by Elhauge focuses mainly on refusals to deal where the tradeoff between short-term static efficiency and long-term dynamic efficiency is probably clearer (i.e., with dynamic efficiency generally being considered more important). It is not clear how it would apply in other situations where the tradeoffs to be made are less capable of measurement. In any event, Elhauge's test has been endorsed from the OECD: see Organisation for Economic Cooperation and Development, "Competition on the Merits", Background Note, 9 May 2005, para. 65.

³⁵ See the references to Gavil, Salop and Dolmans, *supra* note 19.

³⁶ Salop, *supra* note 19.

consumers. The most relevant evidence is output and prices, but quality and innovation may also play a role. There is some divergence among proponents of the consumer welfare test regarding whether efficiencies should be assessed on the basis of whether they simply outweigh any inefficiencies,³⁷ or whether they should be subject to a more detailed proportionality inquiry.³⁸ The latter has two elements. First, it would have to be shown that any harm caused by the dominant firm's conduct is necessary to achieve the overall efficiencies. Second, it would have to be assessed whether the harm caused to competition is disproportionate when compared to any benefits that it brings.

The consumer welfare test certainly has some pedigree in the case law in Europe and elsewhere. In the various *Microsoft* proceedings, the US Court of Appeals and the Commission each essentially applied a consumer harm standard to the various practices alleged.³⁹ The Court of Appeals elaborated a multi-stage analysis of the various alleged exclusionary practices. First, the plaintiff has to show that consumers would be harmed. Second, if such harm is shown, the defendant may offer a pro-competitive justification for its conduct. Third, the pro-competitive justification can be rebutted by the plaintiff, or its positive impact on consumers can be shown to be outweighed by its negative effects on consumers.⁴⁰ On the facts, the Court performed little actual balancing, since it was clear, on the evidence, that most of Microsoft's conduct was overwhelmingly anticompetitive or pro-competitive. For example, regarding the claim that Microsoft had deceived Java developers about the Windows-specific nature of the tools, the Court noted that no efficiency justification had been advanced by Microsoft.

A more explicit balancing exercise was undertaken by the Commission in the European *Microsoft* case. The Commission found that, in relation to the tying of Windows Media Player (WMP) with the Windows operating system (OS), Microsoft had "not submitted adequate evidence to the effect that tying WMP is objectively justified by pro-competitive effects which would outweigh the distortion of competition caused by it ... [W]hat Microsoft presents as the benefits of tying could be achieved in the absence of Microsoft tying WMP with Windows."⁴¹ In particular, the Commission found that: (1) ease of use could be achieved without tying (OEMs could do the bundling at no cost to Microsoft);⁴² (2) distribution efficiencies were minor and did not outweigh distortion of competition;⁴³ (3) there was no evidence of technically superior performance due to code integration of

³⁷ See Gavil, *supra* note 19.

³⁸ See Phillip E. Areeda and Herbert Hovenkamp, *Antitrust Law*, 2nd ed., Aspen Publishers, 2002, para. 651a.

³⁹ See *United States v Microsoft*, 253 F.3d 34, 59 (D.C. Cir. 2001); and Case COMP/C-3/37.792, *Microsoft*, Commission Decision of 24 March 2004, not yet published.

⁴⁰ *Microsoft*, 253 F.3d at 59.

⁴¹ Case COMP/C-3/37.792, *Microsoft*, *supra* note 39, para. 970.

⁴² *Ibid.*, para. 970.

⁴³ *Ibid.*, paras. 956 *et seq.*

WMP with the OS;⁴⁴ and (4) platform efficiency (i.e., the desire to keep applications focused on Microsoft interfaces) was not a recognized efficiency.⁴⁵

More generally, the consumer welfare test, if accepted, would unify the principles concerning mergers and other agreements with those under Article 82. Cooperative agreements between firms that restrict competition are subject to an express balancing act under Article 81(3), including an assessment of whether the anticompetitive effects are necessary and proportionate to achieve the alleged efficiencies. The Commission's Guidelines on Article 81 provide that "for an agreement to be restrictive by effect it must affect actual or potential competition to such an extent that on the relevant market negative effects on prices, output, innovation or the variety or quality of goods and services can be expected within a reasonable degree of probability".⁴⁶ Similarly, efficiencies under EC merger control are subject to the conditions that they: (1) benefit consumers; (2) result from the merger; and (3) are verifiable. A sliding scale is also applied, i.e., mergers with the greatest scope for causing consumer harm also require the most compelling evidence of counterbalancing efficiencies.⁴⁷

Criticism of the consumer welfare test. The consumer welfare test presents a number of difficulties. While balancing pro-competitive and anticompetitive effects may be appropriate when firms choose to conclude an agreement – in particular when, as under the merger control rules, that agreement is subject to mandatory prior approval – judging unilateral conduct in the same way is precarious and might lead to haphazard outcomes. A firm embarking on a course of unilateral conduct *ex ante* may be unsure as to where the balance between pro-competitive and anticompetitive aspects lies and when such effects will materialize. Much would depend on the effect of a practice on the dominant firm's rivals, which the dominant firm cannot generally be expected to know. Moreover, what a firm expects *ex ante* may of course turn out to be different from what occurs *ex post*. These problems are most likely to be acute in markets in which technology evolves rapidly and where new entry is a strong feature, since actual market outcomes may differ materially from many firms' expectations.

Proponents of the consumer harm test have responded to these criticisms with several clarifications. First, they argue that any balancing would not turn courts and competition authorities into central planners, i.e., comparing the harm to consumer welfare with the benefits to producer welfare. Second, they say that courts and competition authorities would not be required to apply sophisticated quantitative techniques to measure the probability and weight of certain effects. Instead, they would apply a "preponderance of evidence" approach to determine whether the benefits and harm are each proven by the evidence and, if so, to compare which is greater. Third, proponents argue that firms would be

⁴⁴ *Ibid.*, para. 958.

⁴⁵ *Ibid.*, para. 962.

⁴⁶ See Guidelines on the application of Article 81(3) of the Treaty, 2004 OJ C101/97, para. 24.

⁴⁷ See Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, 2004 OJ C31/5, paras. 80-86.

judged not *ex post*, but by reference to the types of effects that were reasonably foreseeable *ex ante*, even if they turned out to be wrong. Finally, issues of uncertainty are said to be exaggerated. Most cases, they say, can be resolved at an early stage without the need for complex balancing exercises, either because there is no material harm to consumers or because it is clear that the conduct in question is overwhelmingly harmful or beneficial. But even with these clarifications, it is clear that the consumer harm test would likely present significant complexities in many cases, and it certainly would not be easy for a dominant firm to apply *ex ante*.

D. Limiting Production to the Prejudice of Consumers

Elements. Article 82(b) states that, where a firm is dominant, “limiting production, markets or technical development to the prejudice of consumers” is illegal. Unlawful foreclosure or handicapping of competitors, by which competition is reduced still further, “limit production” in this sense. Limiting production is the most frequent and important category of abuse in practice, since it broadly covers any type of exclusionary conduct that limits rivals’ possibilities and causes harm to consumers. And just as firms can compete in a myriad of ways, so too they can seek to exclude rivals through a multiplicity of strategies. The vast majority of infringement decisions under Article 82 have concerned exclusionary abuses and, therefore, Article 82(b).

Article 82(b) captures the key feature of exclusionary conduct, namely, that it makes competitors’ products or services less attractive or less available, rather than simply making the dominant company’s product better or more available. Offering better or cheaper products must generally be legal, however great the difficulties it causes to rivals. In contrast, creating difficulties for competitors in other ways is not. In basic terms, the application of these principles to the most common pricing and non-pricing abuses is relatively straightforward. The bare wording of Article 82(b) does not of course solve every problem or question, but it at least provides some satisfactory underlying principles, as well as consistency.

Take the example of dominant patent holders in the area of pharmaceuticals impeding generic rivals’ market access through changing product registration documents. Under generic substitution legislation in the EU, less expensive generic drugs can (and, in some cases, must) automatically be substituted for branded equivalents. This rule, however, does not necessarily apply to generics of different dosages, different formulations (e.g., instant for continuous release), or different delivery systems (e.g., capsules for tablets). Observers have noted that by withdrawing a particular version of a branded drug, for which there are approved generic substitutes, in favour of another version, for which there are not, the extent of generic substitution can be decreased (or eliminated), thereby extending the life cycle of the branded monopoly drug. The withdrawal of a branded drug to which a generic applicant has referred and relied in its own application for approval would potentially extend the life cycle further (i.e., in the absence of data on which to refer, the generic manufacturer would need to conduct its own clinical trials albeit with a decreased incentive to do so).

Such a fact pattern would be analyzed as follows under the “limiting production” test:

- The first step in analyzing the conduct is to assess its impact on generic competition, i.e., whether in fact there is a *prima facie* case of “limiting production”. If the impact of the conduct is to seriously restrict the scope of generic competition, then the focus turns to the evaluation of the pro-competitive justifications for the conduct. A number of pro-competitive justifications can be imagined (e.g., safety/quality concerns).
- Where the issue concerns the replacement of an existing product with a new dosage or method of administration, the second step is to consider whether the new replacement product is advantageous relative to the replaced product, i.e., whether there is a *prima facie* case of “prejudice to consumers”. If there is no such advantage, it might be presumed that the only reason for the introduction of the new version and the discontinuation of the old version is to limit generic competition. Conduct of this kind is likely to be regarded as anticompetitive.
- Assuming that the new formulation has advantages relative to the original product, the focus then shifts to whether there are legitimate reasons why the branded company would not offer both the new and the old product, thereby allowing the new product to compete on the merits with generic versions of the original product. Among these might be diseconomies of scope in producing the two products, including manufacturing diseconomies, additional inventory costs, etc. Arguments may be raised that the limited withdrawal of the old product (i.e., withdrawal from only certain markets) suggests that anticompetitive motives rather than diseconomies are driving the decision.
- Fourth, in assessing whether such reasons are sufficient to justify eliminating the original product, a useful starting point is to ask whether the same decision would have been taken in the absence of generic competition. If the answer is yes, then it can be presumed that the costs of supporting two products are not outweighed by the consumer benefits measured as the revenue from the continued sale of the original product, thereby providing a legitimate business justification for its discontinuance. If the answer is no, then the question becomes whether the volume of the original product sold in the face of generic competition and competition from the new formulation is so low as to make it uneconomical to continue to offer it. That is, whether standing alone it can be demonstrated that the original product’s revenue does not justify its continued production and sale. (It is certainly a legitimate business justification to discontinue a product if the product is losing money.) If, on the other hand, but for the effect on generic competition, it would have been profitable for the branded company to continue offering the original product alongside the new formulation, discontinuance of that product will likely be found on balance to be anticompetitive. Evidence that both products are sold profitably in other

countries might tend to contradict an assertion that it is unprofitable to continue to sell both products.

- Finally, in addition to objective economic evidence, courts and the antitrust enforcement agencies will also consider evidence of the subjective intent of the branded company in pulling the version of the product subject to generic competition. Thus, if there are internal memoranda, correspondence, e-mails etc. which suggest that the motivation for the decision to pull the original product is to reduce generic competition, these documents will be considered good evidence that the conduct is on balance anticompetitive notwithstanding any proffered legitimate business justifications. Provided the evidence is reasonably clear and unambiguous, it should inform the assessment of the motivation for the withdrawal or amendment of the registration documentation.

Criticisms. The “limiting production” test can be criticized as lacking the necessary specificity for it to be useful as an operational rule. The test still begs the question of when “limiting” is legal and when it is not. The added requirement that “limiting” is only prohibited if it causes prejudice to consumers is a vital clarification, but it still rather begs the question. However, the other proposed tests are equally beset by the same problems and, arguably, even more so. A second problem is that there are various exceptions to the rule that limiting rivals’ production is legal unless consumers are also harmed. Normally, an above cost price is legal since any “limitation” is the result of greater efficiency, i.e., lower costs. But as noted earlier, the Community Courts have held in *CEWAL* that above-cost price cuts may be abusive in certain circumstances. Again, however, these criticisms are probably more accurately directed at the application of the case law rather than the underlying rationale of the limiting production test. Indeed, the logic of the limiting production test is that preventing a dominant firm from discounting down to its marginal cost of production (or some proxy) would itself cause “prejudice to consumers”.

D. Efficiency Defences

Role in Article 82 cases. A central issue arising from the application of the various proposed tests for exclusionary conduct concerns the role of efficiencies in the assessment of conduct with a mixture of exclusionary and efficiency effects. Failure to pass the “no economic sense” test implicitly accepts that the conduct lacks a business justification other than exclusion. Equally, the consumer welfare test requires consideration of whether the harm caused by a practice is offset by efficiencies. Proponents of the equally-efficient competitor test also accept that conduct which harms equally-efficient competitors may have offsetting efficiency benefits. Finally, the “limiting production” test has an express limb concerning harm to consumers. In sum, the role of efficiencies is directly or indirectly relevant to the principal exclusionary abuse tests that have been proposed.

Although Article 82 does not contain an exemption clause similar to Article 81(3), it is well established that “objective justification” can immunize conduct that would otherwise be an abuse under Article 82.⁴⁸ Objective justification has a number of different facets under Article 82: (1) situations in which the dominant firm’s conduct is objectively necessary because of factors external to the dominant firm’s conduct (e.g., safety concerns); (2) situations in which the dominant firm takes defensive measures to protect its commercial interests (e.g., meeting competition); and (3) situations in which the dominant firm’s conduct is justified by efficiencies. Category (3) is focused on here since it is the most complex and important in practice.

At least in theory, it is accepted that conduct that would otherwise be regarded as exclusionary may be justified by the fact that it creates offsetting efficiency benefits. In the area of predatory pricing, price cuts may be introduced to increase demand for the dominant firm’s products. For example, short-term promotional offers are intended to allow consumers to become familiar with a product in the hope that, when they do, they will, recognizing the product’s quality, pay a higher price once the promotional phase ends. Loss-leading has a similar rationale in that price cuts on certain products are offered in order to increase demand for other (complementary) products. Price cuts may also be intended to expand the market or increase efficiency in other ways, such as by acquiring learning experience to reduce costs over time or by creating network effects. A slightly different defence is that, in situations of excess capacity, the maximum market price may not exceed any firm’s relevant costs, in which case the least inefficient option is to sell below cost for a period until the market corrects itself.⁴⁹

Objective justification is also a central issue in the case of exclusive dealing, loyalty rebates, and other vertical restraints. Such restraints may be motivated by the need to recover fixed costs more efficiently, the need to provide optimal incentives to retailers, and the need to ensure that customer-specific investments by the dominant firm are adequately protected.⁵⁰ Many of the same justifications underpin price discrimination by a dominant firm, which should generally be presumed to be efficient where it expands output more than in situations in which uniform prices apply.⁵¹ The same comment can be made in respect of tying/bundling, which is almost always motivated by some efficiency considerations (though

⁴⁸ See, e.g., Case 40/70, *Sirena Srl v Eda Srl and others* [1971] ECR 69, para. 17; Case 24/67, *Parke, Davis and Co v Probel, Reese, Beintema-Interpharm and Centrafarm* [1968] ECR 55; Case 78/70, *Deutsche Grammophon Gesellschaft mbH v Metro-SB-Großmärkte GmbH & Co KG* [1971] ECR 487; Case 395/87, *Ministère public v Jean-Louis Tournier* [1989] ECR 2521; Case 27/76, *United Brands Company and United Brands Continentaal BV v Commission* [1978] ECR 207; Case 77/77, *Benzine en Petroleum Handelsmaatschappij BV and others v Commission* [1978] ECR 1513, paras. 33-34; Case 311/84, *Centre belge d’études de marché/Télémarketing (CBEM) v SA Compagnie luxembourgeoise de télédiffusion (CLT) and Information publicité Benelux (IPB)* [1985] ECR 3261; *Magill TV Guide/ITP, BBC and RTE*, 1989 OJ L78/43; *Eurofix-Bauco v Hilti*, 1988 OJ L65/19; Case T-83/91, *Tetra Pak International SA v Commission* [1994] ECR II-755; Case T-228/97, *Irish Sugar plc v Commission* [1999] ECR II-2969; Case C-163/99, *Portugal v Commission* [2001] ECR I-2613.

⁴⁹ See O’Donoghue and Padilla, *supra* note 2, Chapter 5, section 5.6.

⁵⁰ *Ibid.*, Chapter 7.

⁵¹ *Ibid.*, Chapter 11.

it may create strong foreclosure too). In essence, all of these defences seek to put forward explanations of why the conduct in question is efficient or justified by some legitimate consideration other than the dominant firm's interest in excluding competitors.

Conditions for an efficiency defence as per the Discussion Paper. Proof of efficiencies requires a number of different steps, now outlined in detail in DG Competition's Discussion Paper on Article 82.⁵² According to this document, efficiencies may lead to a finding that Article 82 does not apply if four cumulative conditions are satisfied. These conditions essentially mirror those applicable under Article 81(3). First, the dominant firm must show that the conduct was undertaken to improve the production or distribution of products or to promote technical or economic progress (e.g., by improving the quality of its product or by obtaining specific cost reductions), or to generate another efficiency. Such claims must be substantiated, though the evidence may be less demanding in the case of qualitative efficiencies such as improvements in distribution.

Second, the dominant firm must show that the conduct is indispensable to achieve the alleged efficiencies. It is for the dominant company to demonstrate that there are no other economically practicable and less anticompetitive alternatives to achieve the claimed efficiencies, taking into account the market conditions and business realities facing the dominant company. The dominant company is not required to consider hypothetical or theoretical alternatives. The Commission will only contest the claim where it is reasonably clear that there are realistic and attainable alternatives, when viewed in the overall context of the dominant firm's conduct and the market realities faced by the dominant firm at the time it made the relevant decision. The dominant company must explain and demonstrate why seemingly realistic and less restrictive alternatives would be significantly less efficient.

Third, the dominant company needs to show that efficiencies brought about by the conduct concerned outweigh the likely negative effects on competition and in particular the likely harm to consumers that the conduct might otherwise have. This will be the case when the Commission, on the basis of sufficient evidence, is in a position to conclude that the efficiencies generated by the conduct are likely to enhance the ability and incentive of the dominant company to act pro-competitively for the benefit of consumers.

The fourth condition makes clear that it is not sufficient for the efficiencies to outweigh the negative effects on competition: on balance, consumers must also benefit from the conduct concerned. This reflects the consideration that Article 82 protects competition on the market as a means of enhancing consumer welfare and of ensuring an efficient allocation of resources. This requires that the pass-on of benefits must at least compensate consumers for any actual or likely negative impact caused to them by the conduct concerned. If consumers in an affected relevant market are worse off following the *prima facie* abusive conduct, the conduct cannot be justified on efficiency grounds. In making this assessment, the

⁵² See *DG Competition discussion paper on the application of Article 82 of the Treaty to exclusionary abuses* (Dec. 2005), <http://ec.europa.eu/comm/competition/antitrust/art82/discpaper2005.pdf>, paras. 84 *et seq.*

Commission states that it must be take into account that the value of a gain for consumers in the future is not worth the same as a present gain for consumers. In general, the later the efficiencies are expected to materialize in the future, the less weight the Commission or national authorities can assign to them. This implies that, to be considered as a countervailing factor, the efficiencies must arise in the short-term.

The incentive on the part of the dominant company to pass efficiency gains on to consumers is often related to the existence of competitive pressure from the remaining firms in the market and from potential entry. This incentive may often be already small as a result of the dominant position. The greater the actual or likely negative effects on competition, the more the Commission or national authorities have to be sure that the claimed efficiencies are substantial, likely to be realized, and to be passed on, to a sufficient degree, to the consumer. It is therefore highly unlikely that *prima facie* abusive conduct of a dominant company with a market position approaching that of a monopoly, or with a similar level of market power, can be justified on the ground that efficiency gains would be sufficient to outweigh its actual or likely anticompetitive effects and would benefit consumers. Similarly, in a market where demand is very inelastic it is highly unlikely that abusive conduct of a dominant company strengthening its dominant position can be justified on the ground that efficiency gains would be sufficient to counteract the actual or likely anticompetitive effects and would benefit consumers.

The final condition is that competition in respect of a substantial part of the products concerned must not be eliminated. The Discussion Paper states that when competition is eliminated the competitive process is brought to an end and short-term efficiency gains are outweighed by longer-term losses stemming *inter alia* from expenditures incurred by the dominant company to maintain its position (rent seeking), misallocation of resources, reduced innovation, and higher prices. This recognizes the fact that rivalry between undertakings is an essential driver of economic efficiency, including dynamic efficiencies in the shape of innovation.

Ultimately, according to the Commission, the protection of rivalry and the competitive process is given priority over possible pro-competitive efficiency gains. Thus, it is highly unlikely that abusive conduct of a dominant company with a market position approaching that of a monopoly could be justified on the ground that efficiency gains would be sufficient to counteract its actual or likely anticompetitive effects. This accords with the sliding scale applied to efficiencies under EC merger control rules. By way of guidance, the Discussion Paper suggests that a 75% market share would substantially eliminate competition in circumstances where there is no effective competition from other actual competitors in the market (e.g., because they have higher costs or because they face capacity constraints).

Evaluating the approach to efficiency defences under Article 82 EC. The explicit recognition of a potential efficiency defence under Article 82 is clearly welcome, since a good deal of unilateral conduct will have a mixture of positive and negative effects on consumers. But significant difficulties remain.

A first point is that, despite the general recognition of objective justification in the case law, there are very few cases under Article 82 in which objective justification has actually been accepted by courts and competition authorities. This may reflect the fact that the basis for the defence put forward in several cases was not strong enough, but more likely suggests that there is something of a disconnect between theory and practice on objective justification. Efficiency defences have typically been rejected with cursory analysis by the Community institutions and without any indication of the analytical framework they have in mind – including most recently by the Court of First Instance in *Wanadoo*.⁵³ This deficiency should be addressed, since a defence that is recognized in theory, but not in practice, is the same as no defence.

A second point is that, although the theory of balancing pro-competitive and anticompetitive effects sounds straightforward, it is often anything but. In theory, the exercise is easy: the amount of the benefits (increased consumer welfare) is compared with welfare loss caused by the exclusion of rivals (e.g., reduced consumer surplus or deadweight loss). Whichever is larger determines the outcome. But in practice it may not be easy, or indeed possible, for a dominant firm to make such detailed assessments at the time it decides on its commercial strategy, in particular if this involves detailed knowledge of the effects of a particular practice on rivals and more generally on consumer welfare. One commentator summarizes these practical concerns as follows:⁵⁴

“The problem, however, is that neither economic actors nor law enforcement entities are omniscient. Given real world limitations, market-wide balancing tests that seek to assess the benefits and competitive harms of exclusionary conduct are intractable for courts and antitrust agencies, and even more so for firms trying to decide in real time what conduct is permitted and what is prohibited. Prospective defendants cannot be expected to know in real time, *ex ante*, whether their efficiency-generating conduct will cause disproportionate harm to their rivals or consumers because, in order to know that, the defendants would have to know more than they can be expected to know about consumer demand, their rivals’ costs and prospects for innovation and for mitigation of harm, future entry conditions, and the like. From the perspective of the defendants, therefore, a balancing test would likely either be ignored, impose excessive transaction costs (a kind of tax on entrepreneurship), or result in excessive caution. There is little

⁵³ See Case T-340, *France Télécom v Commission*, judgment of 30 January 2007, not yet reported. The case concerned predatory pricing. The CFI held that, in the case of pricing below average variable cost (AVC), the “only interest which the undertaking may have in applying such prices is that of eliminating competitors”. (para. 197). This formulation would appear to exclude the possibility that prices below AVC may be non-exclusionary/efficient in certain circumstances. Recent economics literature has raised the possibility that pricing below AVC may have valid business justification in certain circumstances. Reasons suggested include network effects and learning-by-doing efficiencies. In such cases, recovery of the investment in below-cost sales stems from efficiency-enhancing factors (e.g., higher product quality or lower cost) rather than from increased profits through eliminating or disciplining a rival. See Patrick Bolton, Joseph F. Brodley, and Michael H. Riordan, “Predatory Pricing: Strategic Theory and Legal Policy” 88(8) *Georgetown Law Journal* 2239 (2000).

⁵⁴ See A. Douglas Melamed, “Exclusionary Conduct Under the Antitrust Laws: Balancing, Sacrifice, and Refusals to Deal” 20 *Berkeley Technology Law Journal* 1249 (2005).

reason to expect that a balancing test would create optimal *ex ante* incentives for marketplace behaviour.”

Third, it is questionable whether it is correct in law to require the dominant firm to show that the efficiencies outweigh the anticompetitive effects. Article 2 of Regulation 1/2003 provides that “the burden of proving an infringement of ... Article 82 ... shall rest on the party or the authority alleging the infringement”. In *SYFAIT*, Advocate General Jacobs made clear that proof of objective justification means that “certain types of conduct on the part of a dominant undertaking do not fall within the category of abuse at all”.⁵⁵ It is true that Article 2 of Regulation 1/2003 places the burden of proving the benefit of the conditions of Article 81(3) on the defendant, but it clearly does not apply the same principle to Article 82 and objective justification. In these circumstances, it should be for a plaintiff or competition authority to show that the anticompetitive effects outweigh the efficiencies, since, otherwise, no abuse has been proven. The dominant firm should simply bear the initial burden of producing colourable evidence to substantiate the efficiencies claimed (mainly because only it has access to such evidence).⁵⁶ The legal burden should then shift to the plaintiff or competition authority.

Fourth, a particular problem arises because the last condition of the efficiency defence under Article 82 – i.e., the condition that the conduct must not “substantially eliminate competition” – is in practice likely to preclude the availability of the defence. Under Article 82, an efficiency defence would be raised in circumstances where, first, a firm is already dominant and, second, its conduct has been found to have an actual or likely exclusionary effect on competition. Although the Community institutions have made clear that dominance does not necessarily mean that competition is “substantially eliminated”,⁵⁷ a finding of dominance *and* material foreclosure effect under Article 82 may, for practical purposes, mean that competition is substantially eliminated. But even then, the conduct in question may still enhance consumer welfare overall. In other words, there appears to be a logical contradiction between the substantive test for abuse and the availability of an efficiency defence: because of the addition of the “substantial elimination of competition”

⁵⁵ See Opinion of Advocate General Jacobs in Case C-53/03, *Synetairismos Farmakopoion Aitolias & Akarnanias (Syfait) and Others v GlaxoSmithKline plc and GlaxoSmithKline AEVE* [2005] ECR I-4609, para. 53.

⁵⁶ See Joined Cases C-204/00 P et al., *Aalborg Portland A/S and Others v Commission* [2004] ECR I-123, paras. 78-79 (“[I]t should be for the party or the authority alleging an infringement of the competition rules to prove the existence thereof and it should be for the undertaking or the association of undertakings invoking the benefit of a defence against a finding of an infringement to demonstrate that the conditions for applying such defence are satisfied, so that the authority will then have to resort to other evidence. Although according to those principles the legal burden of proof is borne either by the Commission or by the undertaking or association concerned the factual evidence on which a party relies may be of such a kind as to require the other party to provide an explanation or justification, failing which it is permissible to conclude that the burden of proof has been discharged.”).

⁵⁷ See Commission Notice – Guidelines on the application of Article 81(3) of the Treaty, 2004 OJ C101/97, para. 106; Joined Cases T-191/98 and T-212/98 to T-214/98, *Atlantic Container Line AB and Others v Commission* [2003] ECR II-3275, para. 939 (“As the concept of eliminating competition is narrower than that of the existence or acquisition of a dominant position, an undertaking holding such a position is capable of benefiting from an exemption.”).

condition, the former seems to preclude the latter. It is not clear why the Discussion Paper proposes to transpose the conditions for exemption under Article 81(3) to the efficiency defence under Article 82. The most likely reason is consistency, but the Commission has very rarely exempted under Article 81 arrangements that created dominance (except, perhaps, in the case of revolutionary new technologies and markets).

Fifth, many economists question whether balancing anticompetitive effects is meaningful where those effects are a function of a restriction that is indispensable to achieve the stated efficiency.⁵⁸ For example, if exclusive dealing is indispensable to achieve an efficiency (e.g., to justify a customer-specific investment), the source of the anticompetitive concern is the same as the source of the efficiency. And yet, under the Discussion Paper's fourth condition for an efficiency defence – no elimination of competition – an efficient clause would probably be condemned in this instance. A related problem is the suggestion in the Discussion Paper that an efficiency defence will generally be unavailable at market shares in excess of 75%. It is not clear why this statement was added: either conduct is efficient or it is not. Choosing a 75% upper limit is therefore arbitrary and pointless. Thus, in formulating an efficiency defence under Article 82, the Commission would appear to have followed the wording of Article 81(3) for no good reason other than general notions of consistency (despite the wording of the two Articles being clearly (and in my view, deliberately, different). A sounder position is simply to apply a sliding scale (as occurs under merger control laws) whereby the greater the market power harm, the greater the need for offsetting consumer benefits.

A final important point is that the scope and availability of an efficiency defence cannot be looked at in isolation from the substantive rules that apply for specific practices. For example, the non-discrimination clause in Article 82(c) has sometimes been applied in a mechanical fashion, with little regard for the many legitimate reasons why firms charge different prices or offer different terms. The effect of this rule may be to require dominant firms to put forward efficiency justifications for everyday business decisions. But most differences in prices or terms result from the relative skills and bargaining power of customers and do not have (or need) a formal efficiency justification beyond this. It makes no sense to require a dominant firm to provide an elaborate explanation for something as innocuous as other firms' negotiation skills or bargaining power. The same could be said of conditional discount schemes. The broad (and arguably vague) rules historically applied by the Commission in respect of such practices – whether the discounts have a “fidelity-building” effect – require dominant firms to offer efficiency justifications for many practices that have a simple, obvious, and pro-competitive logic. Applying a detailed efficiency justification test in every instance to such practices is unnecessary and wrong.

⁵⁸ See *Selective Price Cuts And Fidelity Rebates*, Economic Discussion paper prepared by RBB for the Office of Fair Trading, July 2005, paras. 4.146 *et seq.*

IV. Assessment Of The Various Tests For Exclusionary Conduct

The various attempts at verbalizing a general test for exclusionary conduct deserve enormous credit. Most importantly, they all recognize a number of elementary, but fundamental, points. In the first place, they show the need for a unified definition of exclusionary conduct. A range of disparate tests that depend on how the conduct happened to be classified would be haphazard, intellectually incoherent, and would lead to differing outcomes. Second, these general tests all recognize the most fundamental point: that it is analytically wrong to equate harm to competitors with unlawful exclusion, since legitimate competition has the same effect, but is positively encouraged. Thus, each test recognizes that unilateral conduct must have some *inherent* element of unlawful exclusion before it can even begin to be considered abusive. While unlawful exclusion and competition often look similar in appearance, the issue of disentangling them cannot be ducked. In particular, it is not simply a question of comparing whatever harm to rivals the conduct *happens* to cause against any offsetting benefits, since, as noted, this could impugn competition itself.

Another point that emerges from the foregoing is that the principal tests are much closer in terms of their basic articulation of the problem and solution than their proponents appear to consider. (Proponents' willingness to identify fundamental differences between the tests is in part a function of the usual dialectic that occurs in these situations: a proposed test will always look more compelling by identifying "fatal" flaws in competing ideas.) In essence, each test seeks to identify conduct that harms rivals for reasons other than the dominant firm's superior efficiency and also makes provision for the possibility that consumers can benefit from efficiencies that offset any exclusion.

That said, some of the tests clearly fare better than others in terms of their usefulness. Although the equally-efficient rival test has a clear pedigree in certain Article 82 case law (particularly in predatory pricing and margin squeeze cases), a number of difficulties remain. First, the Community institutions have not consistently followed this test, even in pricing abuse cases. As noted, above-cost price cuts may be illegal under Article 82 in exceptional circumstances. The Article 82 Discussion Paper also clearly contradicts this general test in several places. First, it suggests that conduct that harms competitors who are not yet as efficient, but who might become so, could be regarded as abusive.⁵⁹ Second, its treatment of above-cost conditional rebate practices clearly applies a test that is *not* based on an equally-efficient competitor, but seeks to modify that test by applying it only to a fraction of market output known as the "contestable" share.⁶⁰ Third, the as-efficient competitor test is clearly less useful – and some would argue useless – where firms compete by offering differentiated products. Fourth, it is not clear how the equally-efficient competitor test should be applied where the dominant firm has activities in multiple related markets (creating

⁵⁹ Discussion Paper, *supra* note 52, para. 67.

⁶⁰ *Ibid.*, paras. 153 *et seq.*

economies of scope/common costs) whereas rivals are stand-alone producers of one product. In these circumstances, rivals may be as efficient in one market but much less efficient overall. As noted above, the Discussion Paper seeks to compensate for problems of this kind by assessing the as-efficient competitor test over a smaller fraction of market output. However, unfortunately this *sounds* like regulation. Finally, the equally-efficient competitor test is of limited use in the case of non-price abuses, except perhaps to assess possible anti-competitive effects. There is some basis in economic theory for saying that less-efficient competitors can improve consumer welfare in certain circumstances. But applying an equally-efficient competitor test with so many possible exceptions may legitimately lead one to wonder whether the exception in fact would become the rule.

The consumer harm test undoubtedly asks the correct theoretical question for assessing unilateral conduct: does it cause net harm to consumers? It also has some pedigree in the decisional practice and case law under Article 82 – most recently *Microsoft* – and is consistent with the overall assessment of anticompetitive effects under Article 81 and the substantive analysis under EC merger control. But whether all unilateral conduct should be subject to such an overarching inquiry is questionable. What unilateral conduct a firm can engage in without violating the law should be subject to clear rules in all but exceptional cases, without the need to balance exclusionary effects against pro-competitive aspects. It is true of course that not all firms are dominant so the point should not be exaggerated; however, it is routine, in my practical experience, for firms with market shares as low as 30% to assume as a matter of risk management that they could be regarded as dominant.

Although proponents of the consumer harm test have made its operational features as useful as possible (and made clear that the assessment should focus on the situation *ex ante*, not *ex post*), complex and precarious balancing acts are still likely to be necessary in marginal cases, where the cost of error is also likely to be high. It also bears emphasis that the vast majority of enforcement is not done in courts or before competition agencies, but in a private sphere where business firms and their advisors scrutinize everyday practices for compatibility with competition laws. My experience in private practice for the last decade or so gives me very little confidence that a consumer welfare test can be easily applied by firms in real time. Moreover, if issues of proportionality come into play, economics contributes very little by way of predictability and the outcomes will represent matters of policy rather than precision.

Of course it might be argued that much the same exercise is sometimes conducted under Article 81 and EC merger control. But cases involving agreements are different in the sense that the firms can always choose not to conclude an agreement, or to structure a different one, or to amend some aspect of their agreement to comply with objections under competition law (e.g., by offering a merger remedy). The firms are also much more likely to have detailed knowledge of the effect of an agreement on their output and to be able to quantify the synergies created by cooperation. Indeed, this is the primary motivation for merger activity and forms of horizontal cooperation. The same cannot generally be said of

most unilateral conduct. The quantitative techniques used in merger control to assess the price effects of a merger are much more difficult to apply to the unilateral conduct of a single firm and, again, it is reasonable to ask whether firms making everyday business decisions should be subject to such burdens. Finally, the counterfactual comparison of the state of competition in the absence of the agreement is also generally clearer in the case of agreements because the agreement will coordinate the activities of firms that previously had independent activities in respect of the matters subject to the agreement.

Both the profit sacrifice and the no economic sense tests are useful in that they seek to move the debate on abusive conduct away from a subjective assessment of what is competition on the merits towards a more objective measure of whether conduct is profit maximizing or economically rational but for its ability to exclude. But the criticisms of both tests are compelling, and several fundamental conceptual questions remain unanswered in respect of these tests. First, it is not clear how the tests would apply where the sacrifice and recoupment occur simultaneously. For example, a margin squeeze does not imply a direct loss on each unit sold as in the case of predation, since a loss of sales by raising the upstream price may be compensated for by downstream volume gains. It is of course true that there is an *opportunity cost* on each unit not sold to the downstream competitor (by raising the input price, the dominant firm may reduce the size of the downstream market and therefore sell less upstream output), but it is not clear how this would fare under profit sacrifice/no economic sense.

Second, in monopoly maintenance cases, there may be no overall profit sacrifice/increase, leading to a false negative finding that no exclusionary conduct has taken place.⁶¹ Third, there are good reasons to believe that the profit sacrifice/no economic sense tests would also be difficult to implement in practice because they require a comparison against a market in which the dominant firm had no power over price (or some other but-for benchmark). The experience of the US courts applying a similar test in the *American Airlines* case shows the complexities involved (although some of these are a function of the complex nature of hub and spoke versus route pair competition in the airline sector). Indeed, some commentators have suggested that it is not even clear whether the sacrifice test is a single unified substantive standard for assessing all exclusionary conduct or simply a more objective measure of the defendant's intent, or the likely effects of a practice. As Sir John Vickers notes, "while the sacrifice test might be useful in assessing wilfulness or intent, it does not naturally yield a substantive standard of what behaviour is exclusionary. There is no escape from the fundamental question of what is [exclusionary]".⁶² In other words, the sacrifice test may, at best, constitute a useful characterization of certain types of abuses – in particular, pricing abuses – it is not, in itself, capable of identifying exclusionary conduct and clearly distinguishing it from legitimate conduct. At the very least, however, it is reasonable to assume that the profit sacrifice/no economic sense tests remain tied to a number of open questions that would likely further complicate Article 82 in the short to medium term.

⁶¹ See Salop, *supra* note 19.

⁶² See Vickers, *supra* note 5.

This leads to the conclusion that the “limiting production” test under Article 82(b) is probably the best test overall. First, it is expressly based, as it should be, on the words of the EC Treaty, and does not require the Commission or the Community Courts to invent new tests not stated anywhere in the Treaty.

Second, it captures the two fundamental insights of any sensible definition of exclusionary conduct. The first is that it ensures that only conduct that results in output limitation (or “limiting production”) is considered exclusionary. All exclusionary conduct results in the limitation of either the dominant firm’s production, or, more likely, that of competitors (either because rivals are forced to exit the market or remain in the market but face marginalization due to increases in their costs caused by the dominant firm’s strategic actions). Although the Community Courts do not always refer to specific clauses of Article 82 in their judgments, multiple judgments have confirmed that Article 82(b) captures both types of limitation, i.e., it prohibits a dominant enterprise from limiting the production, marketing or development of its competitors, as well as its own.⁶³ The Commission has also applied Article 82(b) in its seminal decision in *Microsoft*,⁶⁴ where Microsoft’s conduct was characterized as limiting innovation to the prejudice of consumers. The second key insight captured in Article 82(b) for defining exclusionary conduct is that the only output limitation of interest under Article 82 is that which causes prejudice to consumers. Article 82(b) makes it clear that a dominant company may limit its rivals’ possibilities if no prejudice to consumers results, such as by offering better products or lower prices. Of course, this simple formulation does not answer every question or cater for every nuance but it at least allows a consistent frame of reference.

Third, the emphasis on “prejudice to consumers” in Article 82(b) would expressly allow for efficiency defences for conduct that limits rivals’ production. The status of such defences is not clear under the profit sacrifice test or equally efficient competitor test.

⁶³ See, e.g., Joined Cases 40 to 48, 50, 54 to 56, 111, 113 and 114-73, *Coöperatieve Vereniging “Suiker Unie” UA and others v Commission* [1975] ECR 1663, paras. 399, 482-83, and in particular paras. 523-27; Case 41/83, *Italy v Commission (British Telecommunications)* [1985] ECR 873; Case 311/84, *Centre belge d’études de marché - Télémarketing (CBEM) v SA Compagnie luxembourgeoise de télédiffusion (CLT) and Information publicité Benelux (IPB)* [1985] ECR 3261, para. 26; Case 53/87, *Consorzio italiano della componentistica di ricambio per autoveicoli and Maxicar v Régie nationale des usines Renault* [1988] ECR 6039; Case 238/87, *AB Volvo v Erik Veng (UK) Ltd* [1988] ECR 6211; Joined Cases C-241/91 P, *Radio Telefís Éireann (RTE) and Independent Television Publications Ltd (ITP) v Commission (Magill)* [1995] ECR I-743, para. 54; Case C-41/90, *Klaus Höfner and Fritz Elsner v Macrotron GmbH* [1991] ECR I-1979, para. 30; Case C-55/96, *Job Centre coop arl* [1997] ECR I-7119, paras. 31-36; and Case C-258/98, *Giovanni Carra and Others* [2000] ECR I-4217. For commentary, see John Temple Lang, “Abuse of Dominant Positions in European Community Law, Present and Future: Some Aspects”, in Barry Hawk, ed., *Fifth Fordham Corporate Law Institute, Law & Business*, 1979, pp. 52, 60; John Temple Lang, “Anticompetitive Non-Pricing Abuses Under European and National Antitrust Law”, in Barry Hawk, ed., 2003 *Fordham Corporate Law Institute*, Juris Publication Inc., 2004, pp. 235-340; Christopher Bellamy and Graham Child, *European Community Law of Competition*, 2nd ed., Sweet & Maxwell, 1978, pp. 754-55; Lenaert Ritter, David Braun and Francis Rawlinson, *EC Competition Law—A Practitioner’s Guide*, 2nd ed., Kluwer, 2000, pp. 362-63; Michel Waelbroeck and Aldo Frignani, *European Competition Law*, Transnational Publishers Inc, 1999, p. 551; Pierre Mercier, Olivier Mach, Hubert Gilliéron and Simon Affolter, *Grands Principes du Droit de la Concurrence: Droit Communautaire: Droit Suisse, Dossiers de Droit Europeen No. 7*, Helbing Lichtenhahn Verlag/Éditions Bruylant, 1999, pp. 260-65.

⁶⁴ See *Microsoft*, *supra* note 39, Section 5.3.1.3.1 (“Microsoft’s refusal to supply limits technical development to the prejudice of consumers”) and paras. 693 *et seq.*

For example, an exclusive dealing obligation by a dominant firm will usually limit rivals' production or access to the market, but it may have a valid defence if the dominant firm is making a substantial customer-specific investment and needs some assurance that the customer will buy from it to justify the investment. Pricing below cost may also have a consumer benefit in limited circumstances. Promotional pricing is legitimate where a new product requires consumer familiarity before customers can appreciate its enhanced qualities. Customer familiarity with the product in question during the promotional pricing phase may render them loyal and therefore willing to pay a higher price in the future because of the product's added qualities. In such circumstances, the low price is intended to allow customers to try the product and see if they like it. Higher future prices do not depend on competitors' exclusion, but on the product's enhanced characteristics over existing products.

Article 82(b) also has a clearer normative content for defining exclusionary conduct than any of broad definitions used by the Community institutions. "Normal competition," as per *Hoffmann-La Roche*, is a vague phrase, not least because the Commission has rejected the notion that a common practice within an industry would necessarily constitute "normal competition" if carried out by a dominant firm.⁶⁵ "Competition on the merits," and "genuine undistorted competition" are also vague, since not all competition on the basis of price, quality, and functionality is allowed under Article 82. And, as noted above, the term "special responsibility" is simply an overall label for conduct that is abusive if carried out by a dominant firm. Article 82(b) is also more precise and certain than saying that each practice should be judged according to its positive and negative effects on consumer welfare. Economists sometimes underestimate the importance of legal certainty. This general principle of Community law requires that firms should, to the extent possible, be able to judge whether their conduct is legal or not when they decide to embark on a particular course of conduct.⁶⁶

Fourth, to the extent necessary or useful, Article 82(b) is sufficiently flexible to incorporate elements of the other proposed tests. Although these tests have no clear legal basis under EU competition law, they may be useful in order to verify the "limiting production" test. In particular, Article 82(b) does not prevent the use of the profit sacrifice, equally efficient competitor, or consumer welfare tests where they are valid and useful. Moreover, in circumstances where each test is said to exclude the application of the other tests, and all tests remain essentially untested under Article 82, it is important that Article 82(b) should be relied upon as the basic test for defining exclusionary conduct. This applies not least because economists can and do change their views or evolve them over time.

⁶⁵ *Ibid.*, footnote 877 (citing Case 322/81, *NV Nederlandsche Banden Industrie Michelin v Commission* [1983] ECR 3461, para. 57; Case T-111/96, *ITT Promedia NV v Commission* [1998] ECR II-2937, para. 139).

⁶⁶ See Takis Tridimas, *The General Principles of EC Law*, Oxford University Press, 1999, pp. 165–66; John Temple Lang, "Legal Certainty and Legitimate Expectations as General Principles of Law", in Ulf Bernitz and Joakim Nergelius, eds., *General Principles of European Community Law*, Kluwer Law International, 2000, pp. 163–84. For non-competition cases, see Case C-313/99, *Gerard Mulligan and others v Minister of Agriculture and Food, Ireland and Attorney General* [2002] ECR I-5719; Case C-63/93, *Fintan Duff, Liam Finlay, Thomas Julian, James Lyons, Catherine Moloney, Michael McCarthy, Patrick McCarthy, James O'Regan, Patrick O'Donovan v Minister for Agriculture and Food and Attorney General* [1996] ECR I-569, paras. 19–20.

Finally, to the extent relevant, the limiting production test is also similar to the test proposed by the leading treatise on US antitrust law for defining exclusionary conduct.⁶⁷

⁶⁷ See Areeda and Hovenkamp, *supra* note 38, para. 651a (defining exclusionary conduct as acts that “(1) are reasonably capable of creating, enlarging, or prolonging monopoly power *by impairing the opportunities of rivals*; and (2) that either (2a) do not benefit consumers at all, or (2b) are unnecessary for the particular consumer benefits that the acts produce, or (2c) produce harms disproportionate to the resulting benefits”) (emphasis added).

O’Donoghue, “Verbalizing a General Test for Exclusionary Conduct under Article 82 EC”, in Ehlermann and Marquis, *European Competition Law Annual 2007: A Reformed Approach to Article 82 EC*, forthcoming 2008.