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***A Reformed Approach to Article 82 EC
and the US Practice:
An Overall Appreciation***

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(“A reformed approach to Article 82 and the US practice: an overall appreciation”)

Introduction

Claus originally asked me to provide an overall “appreciation” of the Commission’s new draft guidelines on Article 82. It turns out, as we all know, that the draft guidelines are so new as not yet to have come into existence, but exist they surely will – indeed must – or else a great opportunity will have been missed by the Commission. It is in fact much easier to discuss non-existent guidelines than actual ones since, as with *per se* approaches to antitrust, one is less trammelled by facts. And I hope, but did not risk checking with Claus, that one can respectably get away with submitting a much shorter written contribution in advance of the Workshop than would otherwise have been appropriate.¹

This minuscule paper has four parts. The first offers a brief appreciation (in both senses) of the Commission’s draft Guidelines on the assessment of non-horizontal mergers, and their relevance to the Article 82 guidelines to come. Next are some comments on the threshold of dominance, where the staff discussion paper of December 2005 may inadvertently have created an unfortunately over-interventionist impression. Third, I offer some remarks about possible guiding principles such as consumer harm, the sacrifice (or “but for”) test and the “as-efficient competitor” standard. Finally, in view of the reference in the remit of this panel to US practice, which is largely for David Meyer to discuss, I will say a word on one transatlantic issue: comparative institutional dynamics.

The draft non-horizontal merger Guidelines

The Commission’s draft non-horizontal merger Guidelines, published in February 2007, are relevant to the future guidelines on Article 82 because the two need to be consistent. Indeed, the economics of how non-horizontal mergers can lessen competition (or “significantly impede effective competition”, if you will) are closely related to the economics of

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¹ I discuss abuse and dominance, respectively, at greater length in “Abuse of market power”, 115 *Economic Journal*, 244 (2005) and “Market power in competition cases”, 2 *European Competition Journal* 3 (2006).

exclusionary abuses. There are several features of the draft Guidelines that I hope will be echoed in the guidelines to come on Article 82.

First, the draft non-horizontal merger Guidelines are explicitly consumer-oriented throughout.²

Second, competitor protection is pithily rejected: “the fact that a merger affects competitors is not in and of itself a problem” (paragraph 16). Accordingly, “foreclosure” is not necessarily a problem. The concern is about *anticompetitive* foreclosure – i.e., foreclosure leading to consumer detriment (see paragraph 18).

Third, the draft Guidelines are clear that non-horizontal mergers provide substantial scope for efficiencies (paragraph 13). The same is also true of a range of vertical practices other than mergers.

Fourth, the draft Guidelines set out the principal theories of harm to competition. Thus, for example, section IV.A explains how vertical mergers may lessen competition to the detriment of consumers by means of (i) input foreclosure and (ii) customer foreclosure.

Fifth, the draft Guidelines identify some of the crucial questions of fact that theories of harm to competition must face. A good example is the statement in paragraph 111 that “[i]t is only when a sufficiently large fraction of market output is affected by foreclosure resulting from the merger that the merger may significantly impede effective competition”.³

In sum, the approach to merger appraisal reflected in the draft guidelines is to state theories of harm to competition and consumers, then to see whether the market facts fit those theories, and then to make an overall assessment, keeping in mind possible efficiencies, of the likely overall impact on competition and consumers. There is a lot to be said for approaching Article 82 cases in very much the same way.

Approach to dominance

Whatever one’s concept of abuse, it can happen only in the presence of substantial market power. Absent collusion, a firm can have substantial market power only if it has a large share of a market that is well-defined in an economic sense.

² With the term “consumer” encompassing both intermediate and final consumers.

³ This is said in a section on conglomerate mergers but the point is surely general, and indeed paragraph 73 on vertical mergers has more or less the same form of words.

The first of these statements does not itself determine whether dominance analysis has value because the propositions (a) “If no dominance, then no abuse”, and (b) “If abuse, then dominance”, are logically equivalent. In practice, however, (a) wins, and dominance analysis should continue to come first in casework. That is not least because, again as with mergers, it allows the efficient screening out of relatively unproblematic cases. In the area of Article 82 this seems especially important to do. If and when abuse analysis is reached, dominance findings should remain centre stage, for an “abuse” with a tenuous nexus to market power is probably not abuse.

Within dominance analysis, market definition and market share analysis have their place so long as it is remembered that substitutability is a matter of degree,⁴ and that a large market share is a necessary but not a sufficient condition for substantial market power. So a market share that is not large is a good indicator of an absence of dominance, and hence of an absence of abuse.

It was therefore a bit surprising that the Commission Staff Discussion Paper of December 2005 flirted with market shares as low as 25%. Having stressed helpfully that market power “may derive from several factors which, taken separately, are not necessarily determinative”, the Discussion Paper spoke of (single-firm) dominance as being: (i) “very likely” with a share persistently above 50% provided that rivals have much smaller shares, (ii) “more likely” with a 40-50% share than below 40%, but (iii) “not likely” below 25%.

A firm with 25% of an over-broad “market” could be dominant, but that is a reason to define markets well, not a reason why guidelines need to discuss the possibility of (single-firm) dominance where a firm’s market share is only 25%. So on market shares, which could anyway do with de-emphasis, why not simply say that dominance is more likely above 50% than below, and that it is not likely below 40%, provided that the market is well-defined? Anyhow, I suspect that most (good) cases will be in territory well north of 50%, and will have evidence of dominance much more compelling than market share figures alone can be.

Approach to abuse

The discussion above of the draft non-horizontal merger Guidelines identified five features that I hope will be echoed in the Article 82 guidelines:

- the consumer *leitmotiv*;
- explicit recognition that the task is not to condemn foreclosure but to distinguish anticompetitive from pro-competitive foreclosure;

⁴ For an elaboration of this point, see the 2006 paper cited *supra* note 1.

- allowing clear scope for efficiency defences (objective justification in Article 82 terms) and, where appropriate, balancing;
- clarity about theories of harm to competition and consumers; and
- a corresponding indication of key factual issues in cases.

In the context of exclusionary conduct under Article 82, the second of these points is the classic and inescapable issue of what is, and what is not, “competition on the merits”. At least three types of general standards have been debated: (a) the sacrifice/“but for” test, (b) the “as-efficient competitor” test, and (c) the consumer harm test.⁵ Each comes in various specifications, for example according to whether the test is seen as necessary and/or sufficient for a finding of exclusionary abuse.

Traces of all three standards can be found in the (relatively well-developed) case law on predatory pricing. The cost benchmarks can be related to the “as-efficient competitor” test. Below-avoidable-cost pricing entails short-run sacrifice. Subsequent consumer harm follows if there is recoupment, which under *Brooke Group* must be shown in US law, but which has not generally been recognized as a condition of abuse in EC law. Provided that recoupment is interpreted broadly – e.g., so as to include other-market recoupment via reputation effects – it might be good practice for the Commission to address it explicitly in cases. Even where the likelihood of recoupment could reasonably be inferred from dominance, there would be little harm in saying that, and it would underline the ultimate consumer orientation of the Commission’s competition policy.

The sacrifice/“but for” test has a certain intuitive appeal, but if it is to have a central role in guidelines, at least three issues need to be addressed. The first is circularity. It would obviously be unhelpful simply to say that conduct is anticompetitive if-and-or-only-if it entails profit sacrifice but for its anticompetitive effect. That would leave the fundamental issue – the meaning of “anti-competitive” – hanging in mid-air. How to bring it down to earth? Second is the point that not all abuse entails profit sacrifice even in the short run. Third is the question of the counterfactual: sacrifice relative to what? Not full-blown short-run profit-maximization, presumably. But then what?

The question of the counterfactual must also be addressed by standards cast in terms of consumer harm. Failure to maximize consumer well-being cannot be the litmus test of abuse. But it would certainly seem wrong for conduct to be considered abusive if consumers would probably do no worse with that conduct than with what the firm would reasonably do if the conduct were prohibited.

⁵ These are discussed at greater length in the 2005 paper cited *supra* note 1.

The “as-efficient competitor” standard avoids some of these difficulties, but not others. In essence, this standard says that conduct by a dominant firm is abusive if, without objective justification, it would tend to foreclose firms no less efficient than the dominant firm (at operating the business in question). One main line of price squeeze case law, for example, seems to accord with this principle. In short, this standard says that the foreclosure that is abusive is that of as-efficient competitors. Such foreclosure is more than likely to be anti-consumer. A difficulty, however, is that under theories of “divide-and-rule” exclusion, a dominant firm might, for example, operate a series of exclusive contracts precisely to deny rivals economies of scale and thus to remain more efficient than those rivals in operating each *incremental* unit of business. This needs to be allowed for. The “as-efficient competitor” standard is not a panacea.

The fact that the question of what is competition on the merits is not easy is all the more reason squarely to address it in the guidelines. Likewise in cases, it seems far preferable to state and test theories of harm to competition and consumers against the facts than to condemn conduct for its form.

Institutional dynamics

At the outset I stressed the importance of the Commission taking the initiative by way of preparing guidelines towards a reformed approach to Article 82. Otherwise, there is a serious risk of inertia in the context of EC institutional dynamics, or lack thereof. The interpretation of US antitrust law in the light of new understanding has undergone considerable change in certain periods, notably (but not only) the treatment of non-price vertical restraints in the 1970s. (That flexibility, depending on whether and how it is exercised, has pros and cons.) But the US institutional setting is perhaps more open to change. The US agencies for the most part bring cases in court rather than taking administrative decisions (though the FTC may pursue administrative proceedings). Most US cases, including a number that have shaped the law, stem from private actions. And US judges openly disagree with each other.

By contrast, apart from the fact that the European Court of Justice does not always share the Opinion of the Advocate General, the Community Courts present a unanimous front. So too, incidentally, does the European Central Bank, unlike the US Federal Open Market Committee and (more so) the Monetary Policy Committee of the Bank of England. This may be natural and even desirable, given that the EC consists of national Member States, but a source of institutional dynamics may be lost, or at least obscured, making it all the more important for the Commission to take the lead.

The Courts’ readiness to accept a reformed approach to Article 82 is of course a great unknown. Few signs are to be found in this year’s judgments from the CFI in *Wanadoo* and from the ECJ in *British Airways*. On the other hand, the CFI in September in the Spanish *GlaxoSmithKline* case rejected formalistic argument in an Article 81 case, as had AG Jacobs

in the Greek *GSK* case concerning Article 82. And the CFI merger judgments in 2002 gave considerable impetus to a reformed approach to the ECMR following the Commission's launch of its policy review in that area.

Whatever may emerge from *Microsoft*, the Commission needs to press the Article 82 review to a conclusion in the shape of guidelines and of course casework. Say what you do, and do what you say.