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The application of Article 82 EC to tie-in agreements

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Summary

Abusive behaviour by dominant undertakings is regulated in Article 82 EC. One of the ways to abuse a dominant position is through tying or bundling, and Article 82(d) states that:

“making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.”

Tying can take different forms, but its essence is that the seller supplies the consumer with a product or a service on the condition that he or she also obtains something else, and thereby “ties” two or more products together. The practice is often criticized on the grounds that it takes away the purchaser’s freedom of choice, forecloses competitors, and enables companies to extend their monopoly into the market of the tied product. Tying is however not always harmful, since as a result of the practice a number of benefits can be achieved for both customers and producers. This is one of the reasons why the Commission’s and the Community Courts’ hostile treatment of tying has been so criticized.

Tying has only been dealt with in a small number of cases in the EC, where the most important ones are *Hilti*, *Tetra Pak II* and *Microsoft*. Prior to *Microsoft*, a *per se* approach was consistently applied in all tying cases. The test when assessing tying cases was threefold, and a finding of market power, separate products and coercion was enough for a tying practice to be considered abusive. It appears as though the Commission and the Courts have been focusing on the form when assessing tying arrangements, rather than the actual effects of the practice. Since tying can actually have pro-competitive effects, a *per se* prohibition seems rather outdated and scholars have therefore been arguing that a *rule of reason* approach would be more appropriate.

In *Microsoft* it seems as though the Commission has listened to the arguments put forward. A new analytical framework was applied in the Commission’s decision, where the actual foreclosure effect was assessed. This suggests a move towards a *rule of reason* approach by the Commission. Still, the *Microsoft* case differs from earlier tying cases since it deals with technological tying. This makes it hard to predict whether the Commission’s approach was a change in attitude towards tying, or just valid for this particular case.

Nonetheless, it is obvious that the last years' criticism against the application of Article 82 EC has been heard. As a reaction, the Commission issued "*The DG Competition discussion paper on the application of Article 82 EC to exclusionary abuses*", in 2005. The purpose of the Discussion Paper was to revise the application of Article 82 EC, including the approach towards tying. When Neelie Kroes spoke about the Article 82 revision at Fordham, she said that it is important that the exercise of market power is assessed based on its effects in the market. She also said that aggressive competition is good, as long as it ultimately benefits the consumers. Despite these intentions the *Discussion Paper* is to a large extent a restatement of the case law of the Community courts and the Commission. It is not the radical move towards a more economics-based *rule of reason* approach that some might have expected. Hopefully the next step in the Commission's revision will be some kind of guidelines that will help clarify the unclear approach towards tying in the EC.

Preface

Thank you,

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Abbreviations

CFI	Court of First Instance
DTI	Department of Trade and Industry
EAGCP	Economic Advisory Group for Competition Policy
EC	European Community
ECJ	European Court of Justice
EU	European Union
GCLC	Global Competition Law Centre
OS	Operating System
PC	Personal Computer
WMP	Windows Media Player

1 Introduction

1.1 Purpose

The number one concern for competition law is the problems that will arise when one or several companies possess market power. The fear is that it provides the undertaking with the possibility to restrict output and raise prices, which will ultimately be to the customers' disadvantage.¹ In its application of Article 82 EC over the years, the Commission has frequently been accused of using the article, not only to protect the competitive process, but rather the competitors.² In reaction to this critique, the Commission decided that a revision of Article 82 EC was necessary. As a result, "*The DG Competition discussion paper on the application of Article 82 of the Treaty to exclusionary abuses*", was issued in December 2005. The purpose of the discussion paper has not been to provide guidelines for the interpretation of Article 82, but rather to investigate how the article has been applied over the years. After a discussion around this subject, hopefully some much needed guidelines on this matter will follow.

One way for a company to abuse its dominant position is through tying. Article 82(d) EC states that: "*making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts*" may be an abuse of dominance.

There are three leading cases on tying in EC competition law: *Hilti*, *Tetra Pak II* and *Microsoft*. In all of these cases the Commission has found the companies guilty of abusive tying. When the Commission issued its decision in the *Microsoft* case, it generated a new interest for tying abuses and article 82(d) EC. This decision, together with the Commission's discussion paper, has made the discussion around the approach towards tying more vivid than ever. Many experts are giving voice to the request for a more economics-based analysis in tying cases. There is also a demand that the law is being used more in line with how it was intended to. Today the critics say that in the application of the article, track has been lost of its original aim, and that instead of protecting the competitive process and the consumers, it tends to protect companies from being excluded from the market. For the purpose of this paper I have investigated the approach towards tying in the EC. There are three questions in focus in this thesis: First of all: Do we have a clear and coherent approach towards tying in the EC today? Secondly: How should tying be treated in the context of Article 82(d)? And at last: Which effect can be expected from the Commission's discussion paper?

¹ Whish, p. 21.

² Ibid, p. 149.

1.2 Disposition

This paper starts by a general introduction to Article 82 EC as well as the identification and definition of the relevant provisions for its application to abuses. The second part consists of a further explanation of the concept of tying and bundling and some of the reasons for companies to engage in these practices. In the third part, the existing case law on the matter will be presented briefly, before the more extensive analysis of the three major cases; *Hilti*, *Tetra Pak II* and *Microsoft*. At last I will identify and try to analyse the Commission's approach in the Discussion paper from 2005. Based on the findings in the case law and the Commission's discussion paper, conclusions will be drawn in the analysis to define where the EC law is heading regarding tying abuses.

1.3 Delimitation

The purpose of this thesis is to examine how tying and bundling is being treated under Article 82(d). Except from the first part of this paper, where I will treat the general conditions for the application of Article 82, I will only focus on tying and bundling in relation to this article.

Some of the cases in this paper involve more than one abuse under Article 82. For the above-mentioned reasons, I have limited the analysis to the parts of the judgments and decisions that concern paragraph (d).

When discussing tying and bundling, even through a legal perspective, some economic analysis is inevitable for the understanding of the concepts and the effects of these practices. The debate around the reform of Article 82 has to a great extent been based on a request for an economic analysis in the abuse cases as a factor to assess their effects. Therefore, even though I am not an economist, some economic facts and reflections will be presented in this paper. For these parts the DTI Economics paper has been a valuable source for me in, as well as the GCLC Research paper and the Report by the EAGCP.

1.4 Method and material

The method that I have used for this thesis is the traditional legal method. For my research I have studied books, articles, research papers, Commission decisions and judgments from the Community courts. There are quite a lot of books dealing with Article 82 and tying and these have been a great source of information for me for the first part of this paper. They give a good introduction to Article 82 and the general provisions for its application. They have also provided some guidance to the case law, since most of the case law on tying is rather old.

When it comes to the more recent Microsoft case, I have found valuable information in articles published in various legal journals. Still, in my opinion, an overall problem when it comes to the case law is the lack of actual criticism of the Commission decisions and Community court judgments. Most authors fail to actually analyse them, instead they deliver a description of the outcome. In order to actually understand the status of tying in the EC, I believe that it is important to break down the judgments and analyse the approach taken in each case.

Some of the publications that I have found have been of particular value to me. The *DTI Economics paper no. 1* by Barry Nalebuff has been a great source for me in order to understand the economic aspects of tying and bundling. The *Report by the EAGCP* and the *GCLC Research papers on Article 82 EC* have provided me with invaluable information about the tying approach in the EC, both historically and currently.

As for the Commission's discussion paper it is fairly new and not many comments by well renowned scholars have been published. Nevertheless, I have been able to find some comments in legal journals and I have also analysed the paper in the light of the existing case law.

2 Abuse of a dominant position

2.1 The objectives of Article 82

Article 3(1)(g) EC sets down that there shall be a system in the Community “ensuring that competition in the internal market is not distorted”. Article 82 EC is a central provision of this system and states that:

Any abuse by one or more undertakings of a dominant position within the common market or in a substantial part of it shall be prohibited as incompatible with the common market in so far as it may affect trade between Member States. Such abuse may, in particular, consist in:

- a) directly or indirectly imposing unfair purchase or selling prices or unfair trading conditions*
- b) limiting production, markets or technical development to the prejudice of consumers*
- c) applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage*
- d) making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.*

The essence of Article 82 EC is the control of market power. The article should be applied to a single, dominant company that abuses its market power in one of the ways that is provided in the article. However, the list is not exhaustive, it only gives examples of what can constitute such abuse. This was clarified by the ECJ in *Continental Can*³.

According to the first phrase of the article, the dominant position can be held not only by one undertaking, but also several together.⁴ The objective of Article 82 EC is to protect the competitive process, even though this is not a goal in itself. The competitors should have the possibility to compete on the merits, since ultimately this will benefit the consumers. The protection of the competitive process is motivated by the idea that it is in the consumers best interest that companies are forced to compete. This will lead to the best quality in products and the lowest prices.⁵

Article 82 does not prohibit market power or monopoly *per se*. It is the behaviour of the company with market power that is the object of the policy and not its existence in itself. As the wording of the article clearly states, it is the *abuse* of market power that is prohibited. A company in a dominant

³ Case 6/72 *Europemballage Corporation and Continental Can v. Commission* para. 26.

⁴ Craig and De Búrca, p. 992.

⁵ Eilmansberger, p. 133ff.

position has a special responsibility not to allow its conduct to impair undistorted competition on the common market. As we shall see later in this paper, this responsibility becomes greater and the finding of dominance more likely, the more market shares a company has.⁶

In order for Article 82 EC to be applicable in the first place, the company has to have a dominant position on the market. The fact that a company is dominant is not an offence in itself, but it imposes a special responsibility on the dominant company, not to distort competition on the common market.⁷

2.2 Establishing dominance

2.2.1 Relevant market

2.2.1.1 The product market

The first step when determining whether a company holds a dominant position on the market is to define the relevant market. Article 82 EC speaks of:

“a dominant position within the common market or in a substantial part of it”.

The definition of the relevant market is twofold; both the product market and the geographical market must be defined, in order to establish which companies impose a competitive constraint on the company that is under investigation. In the EU, the most important source for this identification is the Commission’s *Notice on the Definition of the Relevant Market for the Purposes of Community Competition Law*⁸. “The Notice” is based on the case law from the ECJ and the CFI, as well as the Commission’s decisions and provides guidelines for the techniques that may be used when defining markets. It is however important to keep in mind that the Notice is not a legal instrument, and should therefore only be seen as advisory.

The first time the ECJ heard an appeal on the application of Article 82 EC was in *Continental Can*⁹ in 1973. The Court emphasized in this judgment the importance of defining the relevant product market in such cases. Since then, the Court has repeated this importance in several of its following judgments. It follows from the ECJ’s case law, that the central issue when defining the relevant market is whether products or services are

⁶ Whish, p. 194.

⁷ Ibid, p. 189.

⁸ Commission Notice on the definition of relevant market for the purposes of Community competition law, OJ C 372/5 [1997].

⁹ Case 6/72 *Europemballage Corporation and Continental Can v. Commission*.

interchangeable. For example, a copy machine can be replaced by another copy machine from another manufacturer, a car can be replaced by another car and so on. In theory this might sound easy, but the scope of a product market is often subject to discussion, since ultimately it is a matter of interpretation.

According to paragraph 13 of the Notice, there are three main competitive constraints; demand substitutability, supply substitutability and potential competition. When determining the relevant market, it is the demand substitutability that is of importance because it tells us which products the consumer sees as substitutes. To determine whether certain products are within the same market, the Notice introduces the SSNIP test. It originally comes from the US competition law and stands for Small but Significant Non-transitory Increase in Price. The idea of the test is a hypothetical question. If the seller of product A should increase the price, would buyers then switch to another supplier of product A, or would they even switch to product B? If the answer to this question is yes, this suggests that the market is at least as wide as product A. If they will even switch to product B, this suggests that the market includes both A and B.

2.2.1.2 The geographic market

The geographic market refers to a physical area. It can be for example the EU or a part of the EU, such as a country. It was in *United Brands*¹⁰ that the ECJ declared for the first time that the geographical market should be defined. The Commission's Notice and the SSNIP test provide help also when defining the geographical market. If a supplier in Sweden raises the price, will the buyer switch to a supplier in Denmark instead? If a company can raise its prices without losing any customers, this indicates that the market is worth monopolizing. Therefore, the SSNIP test is also called the "hypothetical monopolist test".¹¹

2.2.2 Market power

The next step is to establish that the company has a dominant position. The word dominance is abstract, but when it is used in a commercial context it refers to a position of substantial power for an undertaking in relation to a specific product market and within a relevant geographic market, which both must be defined.¹² In the EC, the term dominant position is a legal concept that has been developed by the Commission and the courts. It should be separated from the economists' perception of the same term.¹³ How the concept of dominance should be defined was considered thoroughly by the ECJ for the first time in *United Brands*¹⁴. The ECJ started

¹⁰ Case 27/76 *United Brands v. Commission*.

¹¹ For a more extensive discussion on the relevant market, see Whish, p. 23-48 and Bishop and Walker p. 82-131.

¹² Goyder, p. 268.

¹³ Korah, 2004, p. 94.

¹⁴ Case 27/76 *United Brands v. Commission*.

by saying that in order to determine whether a company has a dominant position on the market in question, it is necessary to define this market from both the standpoint of the product and from the geographic point of view.¹⁵ Subsequently the following definition was laid down:

“The dominant position referred to in this article relates to a position of economic strength enjoyed by an undertaking which enables it to prevent effective competition being maintained on the relevant market by giving it the power to behave to an appreciable extent independently of its competitors, customers and ultimately of its consumers.”¹⁶

In this judgment the ECJ sets down two conditions for a dominant position: the ability to prevent competition and the ability to behave independently. Which questions their relation to each other, as he does not consider it to be clear. However he seems to be of the opinion that the central issue is the company’s ability to act independently on the market.¹⁷ A large number of companies possess market power to a certain degree. However the reference to a company’s ability to behave independently to an appreciable extent indicates that the target of the article is not the minimal amount of market power that most companies enjoy.¹⁸

2.2.2.1 Market shares

Not long after the *United Brands* judgment the Court developed this definition even more in *Hoffmann-La Roche*¹⁹. It quoted its own definition from *United Brands* and then went on to the question of market shares:

“The existence of a dominant position may derive from several factors which, taken separately, are not necessarily determinative but among these factors a highly important one is the existence of very large market shares.”²⁰

A company’s market share is an important tool for assessing market power. There is no specific share of the market that automatically gives a company a dominant position. Still, the ECJ said in *Hoffmann-La Roche* that very large market shares are in themselves evidence of the existence of a dominant position.²¹ There are a few general guidelines to keep in mind for establishing dominance. A company that holds less than 25% of the market share is very unlikely to be considered to be in a dominant position. This can be concluded by analogy from the *Merger Regulation*²², which states that:

¹⁵ Case 27/76 *United Brands v. Commission*, para 10.

¹⁶ *Ibid*, para 65.

¹⁷ Whish, p. 152f.

¹⁸ Geradin, Hofer, Louis, Petit and Walker, GCLC Research Papers, p. 9.

¹⁹ Case 85/76 *Hoffmann-La Roche v. Commission*.

²⁰ *Ibid*, para 39.

²¹ *Ibid*, para. 41.

²² Council Regulation 4064/89 of 21 December 1989 on the control of concentrations between undertakings [1989] OJ L395/1.

“concentrations where the market share of the undertakings concerned does not exceed 25% either in the common market or in a substantial part of it are presumed to be compatible with the common market”.²³

Even though the scope and purpose of the *Merger Regulation* and Article 82 EC are substantially different, there is no reason to believe that the concept of a dominant position should differ in these two cases.²⁴ Even up to 40%, the risk for a single company to be considered dominant is almost non-existent. Very small market shares can even be a definitive indicator of a lack of dominance. In *Metro II*²⁵ the ECJ made it quite clear that there can be no question of dominance where the market share is 10% or less.

On the other end of the scale we have companies with very large shares of the market. In *Hoffmann-La Roche* the ECJ said that this could in itself be the evidence of a dominant position. However we have to keep two things in mind; First of all there are exceptional circumstances where large market shares do not necessarily mean that a firm is dominant, and secondly, the market share must exist for some time.²⁶ In the *AKZO* judgment the ECJ developed its reasoning from *Hoffmann-La Roche* and said that a market share of 50% or more could be considered very large. If there are no exceptional circumstances, the company will be presumed to be dominant. The company will then have the burden to prove the opposite.²⁷ The larger the market share a company has, the more likely it will be found dominant. When looking at market shares, it is relevant to compare the company with the largest share to its competitors on the market. The smaller their shares are, the more likely it is that the largest company will be found dominant.²⁸

2.2.2.2 Super-dominance

In *Tetra Pak*²⁹ the ECJ said that the special responsibility that a dominant company enjoys must be considered in the light of the special circumstances of each case. Depending on how dominant a company is, what is found to be an abuse in one case might not necessarily be so in another case. The larger the degree of market power is, the more onerous the dominant company's obligations become.³⁰ When companies exceed 90% of the market they become what is called super-dominant. This means that they have an even larger obligation not to engage in practices such as tying, predatory pricing and refusal to deal. It might also be useful for the companies to be aware of this, since the risk that they will be considered to

²³ Ibid, para. 15.

²⁴ Faull and Nikpay, p. 124.

²⁵ Case 75/84 *Metro II* [1986] ECR 3021.

²⁶ Whish, p. 181.

²⁷ Case C-62/86 *AKZO v. Commission* [1991] ECR I-3359.

²⁸ Whish, p. 182.

²⁹ Case C-334/94P *Tetra Pak v. Commission*.

³⁰ Whish, p. 189.

abuse their position is very large when they reach this amount of dominance.³¹

2.2.2.3 Collective dominance

Article 82 refers to abuse by “*one or more undertakings*”. This wording implies that the article is addressed also to several companies that hold a dominant position together. Three elements are required for a collective dominant position. First of all the undertakings that occupy the collective dominant position must be independent from each other. Secondly they must be united by economic links. And thirdly, they must hold together a dominant position with this economic link.³² The fact that Article 82 is applicable also to collective dominance, was established by the ECJ in *Compagnie Maritime Belge*.³³

2.2.2.4 Barriers to entry

Another important element in determining whether a company holds a dominant position is the existence of barriers to entering the market. The Commission and the Community courts have not pronounced a general definition of what constitutes a barrier to entry, but through their judgments and decisions they have adopted quite a wide approach. This has led to the criticism that the market power of some undertakings has been exaggerated.³⁴ On the other hand, others think that it is a broad concept, and should therefore include almost anything that makes it difficult for a new company to enter the market.³⁵

Barriers to entry can either be costs that the company will have, such as legal or administrative barriers, or sunk costs of entry, which means costs that cannot be recovered if entering the market fails. On the other hand, barriers to entry are also costs that will fall on the consumers, such as a high cost for switching to a competitor. A final example of a barrier to entry is the behaviour of a firm holding a dominant position. A threat to engage in a price war or to expand output are examples of what can scare away new entrants and thereby amount to a barrier to entry.³⁶

³¹ Goyder, p. 272.

³² Faull and Nikpay, p. 138f.

³³ Case 395/96P *Compagnie Maritime Belge Transports SA v. Commission*

³⁴ Faull and Nikpay, p. 128.

³⁵ Craig and De Búrca, p. 1003.

³⁶ Faull and Nikpay, p. 128ff.

3 Tying and bundling as a way of abusing a dominant position

3.1 The concept of a tie-in agreement

Article 82(d) EC states as an example of an abusive exploitation:

“making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.”

This practice is also called tying or bundling, and can apply to both products and services. The essence of this practice is that the seller supplies the consumer with a product or service, on the condition that he or she also obtains something else from the seller, thereby “tying” two or more products together. The problem with tying, as far as competition is concerned, is that a company that is dominant in one market can use this position to strengthen its position also in another market. By leveraging its dominant position into this second market, the company can interfere with competition and create barriers to entry for other companies.

Tying can take different forms. The seller can through a contract demand that the customer obtains the tied product in order to be supplied with the tying product. If the seller is dominant in this market, then the customer might not have the possibility to take the business somewhere else. Instead of forcing the customer to obtain several products, the seller can also offer a price reduction, which induces the customers to buy several products together, and hereby create an economic tie.³⁷ Finally products may also be technologically tied. In this case components are integrated in a way that makes it either impossible or unpractical for the consumer to separate them.³⁸

A company in general has to be dominant in one market in order to successfully impose a tie. If the customers are not dependant on the company for the supply of a specific product, they can easily turn to another seller of the same product. However even if a company is dominant, not all tying that occurs is illegal. The concept is widespread in our society and can actually apply to almost everything we buy. Shoes are sold in pairs, when renting a room at a hotel, breakfast is often included in the price, when you buy a car it comes with tyres and so on. To know if a tie is illegal, the most important question is whether the products are separated or not.³⁹ This question will be treated further under chapter 4.3.

³⁷ Jones and Sufrin, p. 452f.

³⁸ Ahlborn, Bailey & Crossley, p. 168.

³⁹ Jones and Sufrin, p. 452f.

To better understand what a tie-in agreement really is, a more thorough explanation is necessary. Tying and bundling can have similar effects to competition, but they are in fact two different concepts. I will therefore separate them in this chapter for the purpose of explaining them, however in the rest of this analysis they will be treated together since a separation is not required for the purpose of my analysis.

3.1.1 Pure bundling

There are two types of bundling, pure and mixed. Pure bundling is the simplest case of a bundle and exists when two or more products are sold together only and cannot be bought separately. Furthermore they are offered at a fixed proportion, for example one steering wheel and four tyres as part of a car. This type of bundle is rare to see forced on a customer, since it is only natural that the market will provide what the customers want. Therefore, if a customer wishes to buy certain products separately, the seller tends to offer this, even if the price may not be very attractive. However by offering individual products at a sufficiently high price, in practice this means that they are only sold as a pure bundle.⁴⁰

3.1.2 Mixed bundling

In a mixed bundle the products are offered both as a package and individually, although if purchased together they are offered at a discount. The discount is crucial for an offer to be classified as a bundle. If there is no discount when buying the products as a package, then it is not considered to be a bundle. The discount can also be referred to the volume, for example if buying a package with two sets of a product is cheaper than buying them separately.⁴¹

3.1.3 Tying

The term tying is used in two ways. First of all it can be a form of mixed bundling, or a so-called static tie. In this case, to buy product A the customer must also buy B. What differs this type of tie from a bundle is that it is possible to buy product B without also buying product A. The customer therefore has two possibilities: either to buy only B, or A+B as a package. This type of tie is achieved through exclusivity arrangements, which are upheld either through a contract or through technological compatibility.

The second type of tying is a form of pure bundle, a dynamic tie. The way this tie works is that a customer who wants to purchase product A, must also buy product B. The difference from a bundle here is that the quantity that

⁴⁰ Nalebuff, 2003, p. 13f

⁴¹ Nalebuff, 2003, p. 14f.

the customer is required to buy of B differs between the customers. An example of a static tie can be a customer who buys a photocopy machine and is required to also buy the supply of papers from the same seller. Basically this is a way to price discriminate between customers, by charging different prices depending on how valuable product B is to them.⁴²

3.2 Why bundle and tie?

Bundling is often criticized on the grounds that it takes away the purchaser's freedom of choice, it forecloses competitors, and enables companies to extend their monopoly into the market of the tied product.⁴³ Economists on the other hand, argue that this is not always the case, and that there are several benefits to be achieved, both for customers and producers, by tying one product to another.⁴⁴

3.2.1 Efficiency reasons

The incentives to bundle can be separated into two groups: efficiency reasons and strategic reasons. Even though separated, the two tend to overlap and efficiency reasons can also be strategic, since the increase in efficiency can create a strategic advantage over the competition. There are several efficiency reasons for a company to bundle or tie, however the purpose of all of them is to reduce the costs and improve the quality.⁴⁵ Basically what a company wants is to achieve economies of scale or scope. One way to do this is for the company to use its resources for producing large volumes. By doing so, the more the company produces the cheaper every product will get. The same resources can also be used for different products, resulting in lower production costs than if the same resource would be used separately for both products.

One of the most common reasons for tying is probably cost saving. A manufacturer of for example a copying machine might also sell copying paper, ink and spare parts. If all of these products are delivered at the same time to the customer, the seller might be able to reduce costs, and thereby lower the prices for the customers. This enables economies of scale to be achieved.⁴⁶ Tying can also reduce costs that the customer would otherwise have, searching for the most appropriate combination of products to satisfy a complex need. Software technologies, for example, such as toolbars, modem support, power management and sound, used to be offered as stand-

⁴² Nalebuff, 2003, p. 15f.

⁴³ Whish, p. 659.

⁴⁴ See for example Korah in *An Introductory Guide to EC Competition Law and Practice*, Nalebuff in *DTI Economics Paper No. 1 on tying and bundling*, and Ahlborn, Bailey and Crossley in the *GCLC Research Papers*.

⁴⁵ Nalebuff, 2003, p. 18.

⁴⁶ Whish, p. 659.

alone products. Today they are offered as an integrated and bundled part of the operating system and are a response to customers demand for easier and bundled software.⁴⁷ Another reason might be to ensure the efficiency of a product. The seller can therefore tie it with consumables to make sure that the parts that are used together are compatible. A third reason for tying is for the seller to be able to discriminate between the customers. A company faces a dilemma when setting a price for a product that has to apply to all customers in the market. If the price is too high, it loses customers. If on the other hand the price is too low, the company gives away profits from customers who would have been willing to pay a higher price.⁴⁸

Consequently, the seller might wish to engage in price discrimination by charging the customers different prices. The customers who value the product the highest and who need it the most, will have to pay a higher price. One way to do this is to tie in a consumable. As an example the manufacturer of a copying-machine can tie-in photocopying paper and let the customers who use the machine the most pay a higher price than the low-volume users. This way the tie works as a substitute for putting a meter on the machine.⁴⁹

3.2.2 Strategic reasons

The strategic reasons for bundling are several and in the following section some of the most common ones will be presented. One strategic reason to bundle is to undercut rivals. When a company has rivals in the market, there will always be a reason to cut prices. By bundling prices the double marginalisation effect will be eliminated and the company can reduce its prices.⁵⁰ Bundling can also be an effective entry-deterrent strategy for a company that has market power in two goods. By bundling them together the company can make it harder for a rival to enter the market. It also allows the company to defend both its products without having to price any one of them low.⁵¹ Bundling can also be a way to mitigate costs if another company enters the market. If the first company offers products A and B as a bundle and the second company offers only A, this can be used as a way for the competing firms to differentiate themselves. If both companies only offered product A, the profit would just be competed away. By bundling they can divide the market between them and attract different customers.⁵² There can be competitive advantages to gain by bundling. The idea is that a multi-product company can offer more variety to the customers than a single product company. If products are sold individually in the market, the customers can get variety by freely mixing and matching. But if the products are offered as a bundle, the best way to get variety is to purchase the bundle. For example a ski resort can offer a bundle of several mountains

⁴⁷ Ahlborn, Bailey & Crossley, p. 171.

⁴⁸ Nalebuff, 2003, p. 34.

⁴⁹ Whish, p. 659f.

⁵⁰ Nalebuff, 2003, p. 39f.

⁵¹ Ibid, 2003, p. 42.

⁵² Ibid, 2003, p. 45.

together in one multi-mountain pass. Another example is cable television companies, where the customers will look to the channel options offered by each company.⁵³ Finally bundles can also be used in the game against consumers. It can disguise the real prices and attract consumers who perhaps do not always realize the relationship between the bundled price and the price for each product separately.⁵⁴

3.3 The economic analysis of tying

Over the years the attitude towards tying has changed a lot. With the help of research by economists it has developed from a quite hostile attitude where tying was only treated as a way to restrict competition. Today, as we have seen above, economists agree that there can be many pro-competitive reasons for companies to engage in the practice. An understanding of the economic effects of tying is important to understand the competition authorities legal approach towards the practice. Below follows an explanation of how the economic approach has developed from its original hostile approach, via a per se legality approach, and into what it is today.

3.3.1 The classical tying approach

The economic analysis of tying can be divided into three phases, where the first one is the classical tying approach. This approach was based on leverage theories and was very hostile against tying. The basic idea of this theory was that the primary goal of tying was to restrict competition. A company with a dominant position in market A could through tying obtain a second dominant position in market B.⁵⁵

3.3.2 The Chicago school approach

This rather simplistic approach to tying was later challenged by a new approach, called the Chicago school. In short the Chicago school claimed that tying conduct produced many benefits from a social view, at no competition cost, and it should therefore be treated as per se legal.⁵⁶

The Chicago school challenged the classical approach on two important points. The first one was the idea that tying first of all was anti-competitive. The supporters of the Chicago School argued that the underlying drive for tying had to be efficiencies, rather than the restriction of competition. They pointed to the several benefits arising from this practice, which we have seen in chapter 3.2 of this paper, such as reduction in production and

⁵³ Ibid, 2003, p. 49.

⁵⁴ Ibid, 2003, p. 61.

⁵⁵ Ahlborn, Bailey and Crossley, p. 169f.

⁵⁶ Ahlborn, Evans and Padilla, p. 319.

distribution costs, reduction in transaction costs, product improvement, quality assurance and lower prices.⁵⁷

The second point that was challenged was the claim that tying was motivated by an attempt to earn a second monopoly profit in the tied market. According to the supporters of the Chicago School approach, a company that enjoyed a monopoly in one market could not generally increase its profit by monopolising a second market. Instead this could lead to reduced profits. This idea is called “*the single monopoly profit theorem*” and according to this idea, the motivation for companies to engage in tying or bundling is efficiency considerations rather than the possibility to secure a greater profit by leveraging their monopoly from one market to another.

What the single monopoly profit theorem says is that monopolists cannot secure greater profits by only leveraging their monopoly from one market to another, they must be engaged in tying and bundling to improve quality or lower costs.⁵⁸ The single monopoly profit theorem applies to cases where the demands for the bundled goods are both independent and complementary. The meaning of an independent demand is that the quantity demanded by consumers of one good is independent of the price of the second good. If the producer ties a competitively supplied good to a monopolistically supplied good, it is basically the same as establishing a tax on the monopolistically supplied good. It will reduce consumption of the monopoly good unless the consumers like the tied good and it is priced competitively. If the demand for the two products were instead complementary, and the products were consumed with fixed proportions, then the monopolist could only profit from the tied good being competitively supplied, since all of the monopoly rents available in the two markets could be captured by a monopoly in one of these.⁵⁹

3.3.3 Post-Chicago theories

The Chicago school contributed to the tying doctrine by introducing the efficiency motivations in the antitrust analysis. It made the competition authorities understand that tying and bundling behaviour could be procompetitive by reducing cost or improving quality. However in the 1990’s economic literature showed that the single monopoly profit theorem was not as correct as first assumed. In its most extreme form, the theorem depends on the assumption that the tied market is perfectly competitive. When this is not true, the theorem may fail.⁶⁰

The Post-Chicago economists developed a number of models to try to understand the competitive implications of tying and bundling when the structure of the tied market is oligopolistic rather than perfectly

⁵⁷ Ahlborn, Bailey and Crossley, p. 170f.

⁵⁸ Ahlborn, Evans and Padilla, p. 323.

⁵⁹ Ahlborn, Bailey and Crossley, p. 173f.

⁶⁰ Ahlborn, Evans and Padilla, p. 324f.

competitive.⁶¹ The models that have been developed so far raise objections against the Chicago school's conclusion that tying should be legal per se. On the other hand it does not either suggest a per se prohibition of the practice. Instead it establishes a theoretical possibility of anticompetitive tying. But it does not conclude that tying is anticompetitive in general or that it is likely to be anticompetitive in practice. Instead it acknowledges that tying can in many circumstances be welfare enhancing, including in situations where the single monopoly profits theorem fails.⁶²

⁶¹ Ahlborn, Bailey and Crossley, p. 174.

⁶² Ahlborn, Evans and Padilla, p. 328f.

4 Case law analysis

The case law concerning tying and bundling in the EC is not very extensive, but there are some important cases that provide us with guidelines of how Article 82(d) EC has been applied by the Commission and the Community courts over the years. In the following chapter I will give an outline of these cases. It starts with a brief presentation of each case, and then a more thorough analysis will follow of the three most important cases, *Hilti*, *Tetra Pak II* and *Microsoft*. The grouping in this chapter is borrowed from the *GCLC Research Papers*, and is based on the nature of the tie-in agreement. Since I feel that it supplies a very good overview, I have chosen to use the same classification here.

4.1 Contractual ties

Tying practices are often imposed by contractual means. The basic idea of this concept is that in order to enter into a contract to buy product A, the customer is required to also enter into another contract for product B.⁶³ The question of contractual ties has been treated in the four following cases.

4.1.1 Hilti⁶⁴

The Hilti case concerned temporal tying of consumables. Hilti was a company that specialized in nail guns and consumables such as nails, cartridges and cartridge strips. They were dominant in the market for nail guns. Two companies, Eurofix and Bauco, turned to the Commission since they felt that Hilti was in breach of Article 82 EC. They were both small companies that specialized in supplying nails for Hilti nail guns. They accused Hilti of trying to exclude them from the market for nails by using a number of measures, one of which was tying cartridge strips and nails together. This practice made it difficult for other companies to sell their nails. Hilti argued that the motivation for this practice was concern for quality and safety. The argument was rejected and the Commission found Hilti to be in breach of art 82. Hilti appealed the decision, but both the CFI and the ECJ upheld the Commission's decision.

⁶³ Ahlborn, Bailey and Crossley, p. 168.

⁶⁴ Commission decision of 22 December 1987, *Eurofix-Bauco v. Hilti*, (1988) OJ L65/19, Case T-30/89 *Hilti AG v. Commission* [1991] ECR II-1439, Case 53/92P *Hilti AG v. Commission* [1994] ECR I-667.

4.1.2 Napier Brown/British Sugar⁶⁵

British Sugar had a monopoly in the production of beet sugar in the United Kingdom. Napier Brown was a merchant that bought and resold sugar. Napier Brown turned to the Commission alleging that British Sugar was using a number of abusive practices to exclude other companies from the market. One of these was to only offer its sugar at “delivered prices”. This was in fact a way of tying the supply of sugar and the delivery service together, and thereby excluding other delivery companies from this market. The Commission found this practice to be an abuse of art. 82, since it eliminated all competition in the delivery service of the product.

In this case the Commission followed the classical *per se* approach in three steps, which was satisfied by a finding of market power, separate products and coercion. There was no explicit consideration of whether the behaviour actually resulted in foreclosure on the tied market. The possibility of objective justifications was acknowledged, but did not seem to have any relevance in practice.⁶⁶

4.1.3 Alsatel⁶⁷

The “tribunal de grande instance” in Strasbourg referred this case to the ECJ for a preliminary ruling regarding the interpretation of Article 82.

Alsatel was a company that provided telecommunications. The case concerned an “after sales” tying, where the customers through a contract were obligated to deal exclusively with Alsatel for any changes, moves, extensions, putting lines into service and, in general, any modifications of the installation. In practice that obligation meant that the customers were prohibited from dealing with another supplier of equipment throughout the duration of the contract. The question to the Court was whether, in view of Alsatel's major share of the regional market, the contracts drawn up by it was evidence of its abuse of a dominant position. The Court said that:

“Although the obligation imposed on customers to deal exclusively with the installer as regards any modification of the installation may be justified by the fact that the equipment remains the property of the installer, the fact that the price of the supplements to the contract entailed by those modifications is not determined but is unilaterally fixed by the installer and the automatic renewal of the contract for a 15-year term if as a result of those modifications the rental is increased by more than 25% may constitute unfair trading conditions prohibited as abusive practices by Article [82] of

⁶⁵ Commission decision of 18 July 1988, *Napier Brown-British Sugar*, (1988) OJ L284/41.

⁶⁶ Ahlborn, Bailey and Crossley, p. 192.

⁶⁷ Case 247/86 *Société Alsacienne et Lorraine de Télécommunications et d'Electronique (Alsatel) v. SA Novasam* [1988] ECR 5987.

the Treaty if all the conditions for the application of that provision are met.”⁶⁸

The Court went on to say that while a very large market share may be important evidence for the existence of a dominant position, that factor does not separately indicate a dominant position, but has to be considered together with other factors.

An interesting fact to note in this case is that the Court did not mention anything about a requirement to assess the effects of the alleged abusive practice.⁶⁹

4.1.4 Tetra Pak II⁷⁰

The Tetra Pak II case is quite similar to *Hilti*. Elopak filed a complaint against Tetra Pak with the Commission for engaging in abusive trading practices and thereby abusing its dominant position. One of these abusive practices was the tying of the purchase of its carton packaging machines to the purchase of cartons. By doing this Tetra Pak reserved for itself the right to supply and repair equipment and spare parts. If the customers failed to comply with these conditions, Tetra Pak withheld guarantees on the equipment. The Commission found Tetra Pak to be in a dominant position and the behaviour to be abusive since it strengthened its dominant position on the market. Both the CFI and the ECJ upheld the decision.

4.2 Discounts which are equivalent to tie-ins

This practice is a form of bundled discount, where the main problem with a tie-in agreement is not present, namely that the customer is unable to buy the products separately. However in these cases the price for the bundle of products is set so that it would be highly uneconomical for the customer to buy the products separately. The consequence of this is basically a situation where the customer cannot choose, but is forced to buy the bundle.⁷¹ In the following three cases the effects of such discounts has been evaluated.

⁶⁸ Ibid, para 10.

⁶⁹ Ahlborn, Bailey and Crossley, p. 188.

⁷⁰ Commission decision of 24 July 1991, *Tetra Pak II*, (1992) OJ L72/1, Case T-83/91 *Tetra Pak v. Commission* [1994] ECR II-755, Case C-333/94P *Tetra Pak International SA v. Commission* [1996] ECR I-5951.

⁷¹ Ahlborn, Bailey and Crossley, p. 189.

4.2.1 Hoffmann-La Roche⁷²

In *Hoffmann-La Roche* the case was primarily about “loyalty” discounts. Roche concluded agreements with their customers, which gave them discounts if they bought most of, or their entire, vitamin supply from Roche. The Commission found Roche to be in breach of Article 82, since they had a dominant position on the vitamin market and abused this position through their behaviour.

The ECJ came to the same conclusion, and said that when applying fidelity rebates, the purpose is in fact to apply dissimilar conditions to equivalent transactions and thereby discriminate between the customers. According to Jones and Sufrin, the ECJ seems to suggest in its judgment that discounts and rebates that induce customers to buy exclusively from a dominant company are abuses that are prohibited *per se*.⁷³ To quote the judgment;

*“An undertaking which is in a dominant position on a market and ties purchasers – even if it does so at their request – by an obligation or promise on their part to obtain all or most of their requirements exclusively from the said undertaking abuses its dominant position within the meaning of article [82] of the Treaty, whether the obligation in question is stipulated without further qualification or whether it is undertaken in consideration of the grant of a rebate.”*⁷⁴

In this case, the Court also took the opportunity for the first time to give a general definition of what constitutes “abusive conduct”⁷⁵;

*“The concept of abuse is an objective concept relating to the behaviour of an undertaking in a dominant position which is such as to influence the structure of a market where, as a result of the very presence of the undertaking in question, the degree of competition is weakened and which, through recourse to methods different from those which condition normal competition in products or services on the basis of the transactions of commercial operators, has the effect of hindering the maintenance of the degree of competition still existing in the market or the growth of that competition.”*⁷⁶

In other words it is the conduct of an undertaking, which has such a dominant position that it is able to influence the market structure and thereby weaken competition.

⁷² Case 85/76 *Hoffmann-La Roche v. Commission* [1979] ECR 461.

⁷³ Jones and Sufrin, p. 450.

⁷⁴ Case 85/76 *Hoffmann-La Roche v. Commission*, para. 89

⁷⁵ Goyder, p. 292.

⁷⁶ Case 85/76 *Hoffmann-La Roche v. Commission*, para. 91.

4.2.2 Michelin⁷⁷

The Commission declared that Michelin infringed Article 82 by tying tyre dealers to itself through individual discounts that were based on sales targets. The Court of Justice disagreed on some points and said that the Commission had not succeeded in showing that Michelin had applied unequal criteria and thereby discriminated between its customers. The ECJ also said in the *Michelin* case:

“A finding that an undertaking has a dominant position is not in itself a recrimination but simply means that, irrespectively of the reasons for which it has such a dominant position, the undertaking concerned has a special responsibility not to allow its conduct to impair genuine undistorted competition on the market.”⁷⁸

It had already been said frequently that it is not illegal for a firm to enjoy a dominant position. However this was the first time that the ECJ spoke about a special responsibility for such a company. This responsibility has since then been repeated in several judgments.⁷⁹

4.2.3 La Poste⁸⁰

The Belgian post operator La Poste had a monopoly over the delivery of business-to-private mail. The company applied preferential tariffs for this service, if the customers also used their business-to-business service. The Commission found this to be an illegal tying arrangement, since it prevented competitors from accessing the Belgian market for postal services that were not covered by the statutory monopoly. It also stated that:

“A policy of tying applied by an undertaking in a monopoly position in order to exclude an active competitor in a neighbouring market not covered by the monopoly must be regarded as a very serious infringement.”⁸¹

⁷⁷ Commission decision of 7 October 1981, *Nederlandsche Banden-Industrie Michelin* (1981) OJ L353/33, Case T-203/01 *Michelin v. Commission* [2003] ECR I, Case 322/81 *NV Nederlandsche Banden Industrie Michelin v. Commission* [1983] ECR 3461.

⁷⁸ Case 322/81 *Michelin v. Commission*, para 57.

⁷⁹ Korah, 2004, p. 116.

⁸⁰ Commission decision of 5 December 2001, *De Poste–La Poste* (2002) OJ L61/32.

⁸¹ *Ibid*, para. 86.

4.3 Technological tie-ins

A technological tie is when a product is designed to function only together with the producer's own complementary product. A product might also be bundled into another product and thereby included, as we shall see in the Microsoft case. There are legitimate reasons for this practice, such as to ensure the engineering of a better product. But it might also be an attempt from the producer to avoid competition.⁸² The concept of technological tying is quite new, and the Commission has been criticized for not having the technical competence to understand its effects and thereby make a correct assessment of such a practice.

4.3.1 IBM⁸³

Technological tying first became a concern in the EU with the IBM case. IBM held a dominant position in the common market for the supply of the central processing unit (CPU) and the operating system for the System/370. As a result of this IBM could control the market for all products compatible with the System/370. The Commission objected to the integration of memory devices with the CPU and the bundling with the basic software applications. The case was however settled informally, since IBM agreed to offer its System/370 either without memory devices, or at least the minimum capacity required for testing.⁸⁴ Not long after the IBM case had been settled, the integration of the CPU and main memory devices became standard practice in the computer industry.⁸⁵

4.3.2 Microsoft⁸⁶

In *Microsoft* the tying of Windows Media Player with Windows PC Operating System was found to be an abuse. The Commission decided that the two were separate products and by tying them together, the customers did not have a choice as to whether acquire WMP with the OS or not. This closed the market for competitors, since it put competing products at a disadvantage. *Microsoft* differs from earlier tying cases since the Commission at least raised the question of objective justification and thus abandoned the per se approach that had been applied in former cases.⁸⁷

⁸² Gaynor, p. 1.

⁸³ *The Community v. International Business Machines Corporation*, EC Commission Notice of 1 August 1984 [1984].

⁸⁴ Ahlborn, Bailey and Crossley, p. 190.

⁸⁵ Ahlborn, Evans and Padilla, p. 310.

⁸⁶ Case COMP/C-3/37.792 Commission decision of March 2004 *Microsoft*.

⁸⁷ Ahlborn, Bailey and Crossley, p. 197.

4.4 Leading tying cases

The approach of EC competition law towards tying is particularly shown by three cases: *Hilti*, *Tetra Pak II* and *Microsoft*. They give a good picture of the reasoning around tying and bundling in EC competition law by both the Commission and the Community courts, and they also illustrate the problems that exist in this area. The Commission decisions in both *Hilti* and *Tetra Pak II* have been criticized for treating tying as per se illegal. The general opinion seems to be that there is a lack of analysis of the effects of the alleged abuses, as well as an economic assessment. Also the question of objective justifications has not been seriously analyzed in the cases, neither by the Commission nor the Community courts. With the *Microsoft* decision however, as we shall see below, the Commission has deviated from this original approach and applied a different test.⁸⁸

4.4.1 Hilti

Hilti specialized in the manufacture and distribution of nail guns and cartridge strips, for which it had a patent. The company also supplied nails to be used in the nail guns, but these were not protected by patent. Eurofix and Bauco were two small companies that specialized in supplying nails compatible with Hilti nail guns. In 1982 they complained to the Commission that Hilti was infringing Article 82 of the Treaty by following a number of practices to ensure that customers who bought its cartridges also bought nails from Hilti, and not from independent suppliers. These practices were; refusing to provide independent dealers or distributors with cartridge strips unless they also bought a complement of nails; inducing its independent dealers to cut off the supplies of cartridge strips to independent nail producers; reducing discounts for customers who bought nails from independent nail producers; refusing to grant licences for other companies to manufacture or import cartridge strips.

The Commission found that nail guns, cartridge strips and nails constituted three separate relevant product markets. This definition was based on the fact that from a supply view, nails and cartridge strips were produced with different technologies and often by different firms. Even though from a demand side, customers often needed both cartridge strips and nails, they were not necessarily purchased together and in equal quantities. Hilti's policy of tying the sale of nails to its patented cartridge strips created a significant barrier to entry to the market for Hilti-compatible nails for other nail makers.⁸⁹ As far as dominance was concerned, the Commission found that Hilti was in a dominant position in all three markets. The Commission also held that because of Hilti's large market share, independent manufacturers of nails and cartridge strips had to manufacture products that were compatible with Hilti tools if they wanted to be able to achieve the

⁸⁸ Ahlborn, Bailey and Crossley, p. 197.

⁸⁹ Commission decision *Eurofix-Bauco v. Hilti*, para. 55-65

economies of scale necessary to be both competitive and profitable. Otherwise they could only produce for a small segment of the market.⁹⁰ The Commission continued its reasoning by saying that:

“In fact Hilti’s commercial behaviour /.../ is witness to its ability to act independently of, and without due regard to, either competitors or customers on the relevant markets in question. In addition, Hilti’s pricing policy /.../ reflects its ability to determine, or at least to have an appreciable influence on the conditions under which competition will develop. This behaviour and its economic consequences would not normally be seen where a company was facing real competitive pressure.”⁹¹

Hilti tried to justify its commercial behaviour by referring to safety reasons, saying that nails made by certain independent nail makers did not meet the desired standard. The actions taken were therefore motivated by the desire to ensure the safe and reliable operation of its products, and not a method to reach a commercial advantage. The Commission rejected this and pointed out that Hilti had never taken any appropriate measures to come to terms with these safety concerns. Therefore its argument concerning safety was not considered an objective justification for its behaviour.⁹²

Hilti appealed to the CFI, on the grounds that it did not hold a dominant position and that its behaviour was objectively justified, but without success. For the question of the relevant product market, the CFI agreed with the Commission and said that nail guns, cartridge strips and nails constituted three specific markets. As the Commission, it pointed to the fact that there are independent producers of nails, and also of nails for use in nail guns.⁹³ The CFI said that considering nail guns, cartridge strips and nails as forming an invisible whole *“is in practice tantamount to permitting producers of nail guns to exclude the use of consumables other than their own branded products in their tools”⁹⁴*.

According to Dolmans and Graf the Court’s statement means that if there is a demand to acquire the tied product from a different source than the tying product, the dominant company is obligated to give its customers the choice to do so. This is irrespective of whether the products are complements to each other, or connected in some way by a natural link or commercial usage.⁹⁵ Rousseva has also commented on the CFI’s statement. She is quite critical towards it since she feels that this would in fact suggest that products cannot be sold jointly by a dominant undertaking even if they are linked by nature or by their commercial usage.⁹⁶

⁹⁰ Ibid, para. 70.

⁹¹ Ibid, para. 71.

⁹² Ibid, para. 87-93.

⁹³ Case T-30/89 *Hilti AG v, Commission*, para. 67-68.

⁹⁴ Ibid, para. 68.

⁹⁵ Dolmans and Graf, p. 229.

⁹⁶ Rousseva, p. 603.

Regarding the question of whether Hilti held a dominant position on the market for nails, it had been proved by the Commission that Hilti had a market share of around 70% to 80% in the relevant market for nails. The CFI referred to the judgment in AKZO, where it was established that such a market share in itself is a clear indication of a dominant position, and consequently found no reason to deviate from the Commission's view that Hilti was dominant in the market for nails.⁹⁷ Lastly the CFI stated that Hilti's argument for objective justification could not be accepted on the same grounds as were referred to by the Commission. Hilti had at no time approached the authorities for a ruling that the use of other manufacturer's nails in Hilti tools was dangerous.⁹⁸ Hilti's appeal was therefore rejected by the CFI. Also the ECJ upheld the Commission's decision.

⁹⁷ Case T-30/89 *Hilti AG v. Commission*, para. 92.

⁹⁸ *Ibid*, para. 115.

4.4.2 Tetra Pak II

In 1983 Elopak filed a complaint with the Commission against Tetra Pak, a manufacturer of machines for packaging liquid and semi-liquid foods in cartons, for engaging in trading practices which were abusive for a company in a dominant position. The abusive practices were; the tying of the purchase of its carton packaging machines to the purchase of cartons, requiring purchasers to use only Tetra Pak's maintenance and repair services, and withholding guarantees on the equipment if the purchasers failed to comply with these conditions.

Tetra Pak tried to defend itself by claiming that by its nature and commercial usage, the machines, the packaging, the cartons and the service were part of an indivisible whole. Tetra Pak also said that in any event the tying of the machines and cartons was justified for technical reasons, considerations of product liability and health, and by the need to protect its reputation. The high technology of its machines demanded that only specifically designed cartons were used in them. Because of this, a "natural link" existed between the machines and the cartons, and thus there could be no breach of Article 82.

There are two main issues in Tetra Pak II:

1. the issue of dominance in the aseptic markets as well as the non-aseptic markets and;
2. whether the machines and the cartons form separate markets.

On the issue of the relevant market, the Commission came to a different conclusion than Tetra Pak and identified four separate relevant markets: aseptic packaging machines, aseptic cartons, non-aseptic packaging machines and non-aseptic cartons. To support its definition it said;

*".../although types of packaging as diverse as glass bottles, plastic bottles, plastic bags, metal tins, aseptic cartons, non-aseptic cartons, etc., form part of what is commonly known in the broad sense of the term as the packaging market for the liquid foods, this is not the "relevant market" within the meaning of Article [82], since these different types of packaging compete with each other only in the long term. In the short, and probably even the medium term, the conditions of supply and demand are such that the elasticity of substitution for products in relation to prices is almost zero."*⁹⁹

On the aseptic market Tetra Pak held a very strong, almost monopolistic position with market shares of around 90% for both machines and cartons. However on the non-aseptic market the position was much weaker with market shares that, at the most, only amounted to around 50%. In some countries it was even as low as 30%. There was no doubt that Tetra Pak was

⁹⁹ Commission decision of 24 July 1991, *Tetra Pak II*, para. 93.

dominant on the aseptic markets. On the other hand, when assessing its position on the non-aseptic markets, the Commission could not come to the same conclusion and consequently said the following:

“Even though it cannot therefore be considered that Tetra Pak enjoys a position on the non-aseptic markets which allows it to behave as independently as on the aseptic markets, it is certain that it is far less affected by market forces than any of its competitors.”¹⁰⁰

The Commission continued and said that on the non-aseptic markets the existence of a dominant position was less clear-cut if considered in isolation. Still, it said that the ECJ has recognized market shares smaller than in this case, as constituting a dominant position. It also said that the market shares in some of the Member States were such that undoubtedly a dominant position existed, even if the markets were considered in isolation.¹⁰¹ Finally it said in the conclusion;

“The Commission takes the view that, by taking advantage of its dominant and virtually monopolistic position on the so-called aseptic markets in machines and cartons intended for the packaging of liquid foodstuffs, Tetra Pak has committed and continues to commit abuses within the meaning of Article [82], both on these aseptic markets and on the neighbouring markets in non-aseptic equipment and cartons.”¹⁰²

Tetra Pak appealed to both the CFI and the ECJ, claiming that it did not have a dominant position in the common market or a substantial part of it, and that its conduct did not constitute an abuse within the meaning of Article 82. Both courts upheld the Commission’s decision. The CFI said in its judgment;

“It follows from all the above considerations that, in the circumstances of this case, Tetra Pak’s practices on the non-aseptic markets are liable to be caught by Article [82] of the Treaty without its being necessary to establish the existence of a dominant position on those markets taken in isolation, since that undertaking’s leading position on the non-aseptic markets, combined with the close associative links between those markets and the aseptic markets, gave Tetra Pak freedom of conduct compared with the other economic operators on the non-aseptic markets, such as to impose on it a special responsibility under Article [82] to maintain genuine undistorted competition on those markets.”¹⁰³

Applying Article 82 to a case with distinct markets, where the abuse is taking place on the non-dominant market and producing effects on the neighbouring dominant market, can only be justified by special

¹⁰⁰ Ibid, para. 101.

¹⁰¹ Ibid, para. 104.

¹⁰² Ibid, para. 169.

¹⁰³ Case T-83/91 *Tetra Pak v. Commission*, para. 122.

circumstances. The circumstances taken into account by the CFI were the following: Tetra Pak held 78% of the overall market in packaging in both aseptic and non-aseptic cartons, which was more than seven times more than its closest competitor.¹⁰⁴ Tetra Pak was also the leading company in the non-aseptic sector.¹⁰⁵ Furthermore Tetra Pak's quasi-monopolistic position on the aseptic markets made it the favoured supplier of non-aseptic systems.¹⁰⁶ Lastly the CFI concluded that because of the situations on the different markets and the close associative links between them, the application of Article 82 was justified.¹⁰⁷ These circumstances were upheld by the Court of Justice, who also said that given Tetra Pak's almost complete domination of the aseptic markets, the company could also count on a favoured status on the non-aseptic markets, and thereby it could concentrate its efforts on the non-aseptic market by acting independently of the other economic operators.¹⁰⁸

The Commission does not really establish a dominant position in the non-aseptic market in its decision. Instead it seems to be saying that a non-dominant company's conduct on a market can be caught as an abuse, if the company is dominant in another, separate but neighbouring, market.¹⁰⁹ From *AKZO* we have learned that market shares of 50% and more should be taken as an indication of a very strong position on the market.¹¹⁰ In this case it seems as though the Commission has let the super dominant position in the aseptic market rub off on the non-aseptic market. The reasoning of the Commission in this part of its decision has been quite criticized in the doctrine by various authors. Korah says that the Commission relied in its decision on the associative links between the aseptic and the non-aseptic markets, in order to condemn conduct on the non-aseptic markets that actually had effect only on the non-aseptic markets.¹¹¹

Levy discusses the fact that Tetra Pak was found to be infringing Article 82 in the non-aseptic market where it was not dominant, and what effects this will have. He comes to the conclusion that the scope of the Tetra Pak II judgment is quite limited for five reasons. First of all the abusive conduct was practiced on a product market neighbouring the market of dominance. Second, there were close links between the two markets. Third, Tetra Pak was active on both markets, and on the market where it was not dominant it still had a much stronger position than any of its rivals. Fourth, a large amount of Tetra Pak's customers operated on both markets. Fifth, since Tetra Pak was dominant on the aseptic market, it could focus its competitive efforts on the neighbouring, non-aseptic market. He concludes that these factors together should only occur very rarely. Therefore the judgment in

¹⁰⁴ Ibid, para. 118.

¹⁰⁵ Ibid, para. 119.

¹⁰⁶ Ibid, para. 121.

¹⁰⁷ Ibid, para. 122.

¹⁰⁸ Ibid, para. 29.

¹⁰⁹ Jones and Sufrin, p. 375.

¹¹⁰ Case 62/86 *AKZO v. Commission*.

¹¹¹ Korah, 1997, p. 99.

Tetra Pak II should only in exceptional circumstances prevent a company with a dominant position in one market, from competing aggressively on another market. Especially when the other market is unrelated.¹¹²

As far as concerns the tying of the machines and cartons, Tetra Pak argued that this practice was justified in the light of commercial usage and the nature of the products. The Commission on the other hand held the opposite, and both Community Courts agreed. This finding was based on the fact that there were independent manufacturers who specialized in manufacturing cartons for use in machines manufactured by others. The CFI said that tied sales of machinery and cartons were not in accordance with commercial usage, since such sales were not a general rule in neither the aseptic nor the non-aseptic sector.¹¹³ These factors were taken as an indication that the two products were separate. Even if commercial usage could be shown it was not enough to justify a tying by an undertaking in a dominant position, the CFI said, since *“even a usage which is acceptable in a normal situation, on a competitive market, cannot be accepted in the case of a market where competition is already restricted.”*¹¹⁴ The ECJ upheld the CFI’s reasoning also in this part of the appeal, by stating that the list of abusive practices in Article 82 was not exhaustive, and so:

*“Consequently, even where tied sales of two products are in accordance with commercial usage or there is a natural link between the two products in question, such sales may still constitute abuse within the meaning of Article [82] unless they are objectively justified.”*¹¹⁵

Korah criticizes the Commission’s decision, as well as the judgments of the Courts for lack of reasoning. The conclusions may have been right, she says, but it is concerning that neither of them have considered the objections to or commercial justifications for a tie, or whether it was proportionate. It is true that the list of potentially abusive practices in Article 82 is not exhaustive. Still, in this case the Court extended Article 82 to tying products that were not dominated, without giving any reason. The Court simply referred to the CFI’s observation that there were independent suppliers of non-aseptic cartons and that the list in Article 82 was not exhaustive.¹¹⁶

Rousseva comments on the separate-product test in Tetra Pak II, and whether the tying was justified. If the products sold together are not in different product markets there is no tying at all. On the other hand she points out that the text of Article 82 does not say that the finding that the products are distinct is an indication of abuse. Still, the Commission and the Community Courts’ analyses tend to be limited to the carrying out of this test.

¹¹² Levy, p. 109.

¹¹³ Case T-83/91 *Tetra Pak v. Commission*, para. 82.

¹¹⁴ *Ibid*, para. 137.

¹¹⁵ Case C-333/94P *Tetra Pak International SA v. Commission*, para. 37.

¹¹⁶ Korah, 1997, p. 101.

*“Commercial or efficiency explanations for joint sales of distinct products have not been accepted where the supplier is in a dominant position”, she says.*¹¹⁷

In Tetra Pak II it was obvious that there was a demand for the tied products since they were complementary. What we can learn from Tetra Pak II according to Rousseva is that an existing demand for using two products together is not enough to justify a tie, as long as there is also a demand for purchasing the tied products separately from different suppliers or in different quantities.¹¹⁸

¹¹⁷ Rousseva, p. 602.

¹¹⁸ Ibid, p. 603.

4.4.3 Microsoft

In 1998 Sun Microsystems made an application to the Commission for the initiation of proceedings against Microsoft. According to Sun Microsystems, Microsoft held a dominant position as a supplier of PC operating systems. By reserving for itself information that was necessary to create software products that could interoperate with the PC operating systems, Microsoft infringed Article 82 of the Treaty. Following this application, the Commission launched an investigation against Microsoft that especially concerned the incorporation of a software product called “Windows Media Player” (WMP) into its PC operating system.¹¹⁹ This tying practice was found to be an abuse of Article 82 (d) and Microsoft was fined €497 million by the Commission. In addition to this, Microsoft was required to provide its customers with a version of its operating system without WMP.

In the decision four conditions were set up by the Commission for a tie to be prohibited under Article 82 EC: *1) the undertaking concerned should be dominant in the tying product market; 2) the tying and tied goods should be two separate products; 3) the undertaking concerned should not give customers a choice to obtain the tying product without the tied product; and 4) the tying should foreclose competition.*¹²⁰

Microsoft did not contest the fact that it held a dominant position in the market for operating systems for PC’s. The Commission referred to AG Fennelly’s statement from *Compagnie Maritime Belge*, where he talked about the concept of “superdominance” and stressed the special responsibility that a company in a position of overwhelming dominance has:

*“Microsoft, with its market shares of over 90%, occupies almost the whole market – it therefore approaches a position of complete monopoly, and can be said to hold an overwhelmingly dominant position.”*¹²¹

For the purpose of defining the relevant product market, the Commission started by saying that: *“A relevant product market comprises all those products and/or services which are regarded as interchangeable or substitutable by the consumer, by reason of the products’ characteristics, their prices and their intended use/.../.”*¹²²

The Commission then came to the conclusion that the markets for the client PC operating systems and the one for streaming media players were two separate ones. The existence of stand-alone media player software that can be installed on a PC was seen as a proof of this fact.

¹¹⁹ Commission decision of 24 March 2004, *Microsoft*, para. 3-5.

¹²⁰ *Ibid*, para. 794.

¹²¹ *Ibid*, para. 435.

¹²² *Ibid*, para. 321.

Microsoft contested this and argued that client PC's would not be shipped without the multimedia function of playing audio and video content.¹²³ The Commission rejected the objection.

As for the question of abuse, the Commission referred to the ECJ's judgment in *Michelin* and said that a dominant position is not in itself an abuse of the competition rules. Nevertheless, it brings about a special responsibility not to engage in conduct that may distort competition.¹²⁴

The Commission devoted quite some time in its decision analysing the Article 82 requirement, that purchasers are forced to acquire the tied product along with the tying product. In its defence, Microsoft argued that in fact WMP was given away for free with the operative system. The Commission did not accept this argument on the grounds that a fee for the WMP could be hidden in the bundled price. It also said that that in any event this was immaterial, since the main concern was the foreclosure effects. By tying WMP with Windows, Microsoft took advantage of its dominant position in this market. The WMP was built into the PC before being delivered to the end customer, and Microsoft did not provide for any means to remove it. Hereby the customers were deprived of their choice as to whether acquire the WMP or not.

The Commission decision argues that because of Microsoft's dominance on the market with Windows OS, the bundling of WMP will give it such an advantage over other media player manufacturers that they will not be able to compete. If WMP becomes the industry standard, content providers and software developers will increasingly produce content exclusively in WMP format and as a result competing products will be driven out of the market. Along with this comes the fear that Microsoft will acquire control over other related markets, such as media delivery software and digital rights management technology.¹²⁵

Völcker notes in his examination of the judgment, that the Commission has analyzed both the actual and the projected foreclosure effects of Microsoft's behaviour. This might, in his opinion, be a way to avoid that the CFI takes a different approach in an appeal considering the specifics of the software industry. Another remark made by Völcker is that although the Commission rejects the efficiency defences made by Microsoft, it still makes a very thorough examination of the arguments put forward by the company. He says that maybe this is also an attempt to make the decision appeal-proof. Another possible explanation is that the Commission has decided to at least be open to efficiency justifications in Article 82 cases.¹²⁶

¹²³ Ibid, para. 404.

¹²⁴ Ibid, para. 542.

¹²⁵ Völcker, 2005, p, 1711.

¹²⁶ Ibid, p. 1712.

The decision in the Microsoft case has been subject to several comments in the doctrine, not just by Völcker, and has put new fuel into the debate on the subject of tying and Article 82(2)(d) EC. Not everyone questions the Commission's reasoning in the case. Some authors think that the Commission has acted correctly in its decision.

According to Dolmans and Graf the *Microsoft* decision is a textbook case for a tying abuse.¹²⁷ Based on the case law of the Commission and the ECJ, they have identified five elements that need to be fulfilled in order to establish a tying abuse under Article 82(2)(d) EC: *dominance of the seller in the market for the tying product; existence of a tied product that is separate from the tying product; coercion, meaning that the customers are forced to buy the tied product together with the tying product; a restrictive effect on competition for the tied product; and absence of an objective and proportionate justification for the coercion.*¹²⁸

They find all of these conditions to be fulfilled in the Commission decision. As for the effect on competition, they say that there is an interdependency between all the different elements in the digital distribution chain, and the demand for each element in the chain is influenced by the usage of other elements in the chain. Microsoft's tying had the effect of distorting these network effects to the company's advantage.¹²⁹

Evans and Padilla disagree with Dolmans and Graf. They attack the Commission's decision on two relevant points. The first one is the acknowledgement by the Commission that Microsoft's practice did not in fact lead to a classical tying case, where foreclosure is a result of the fact that consumers would take a competing product if they were given the choice to do so. Instead foreclosure is a result of content providers standardising on WMP and thereby forcing customers to use it, since eventually content will be available only for WMP. The problem in the Commission's view, they say, is that Microsoft has an advantage in distributing its technology that others do not have. However they do not see how the standard remedy for tying would solve this problem, since almost all computer manufacturers and consumers most likely will continue to chose the version of Windows that includes WMP.¹³⁰

The second interesting point of criticism from Evans and Padilla concerns the separate products test used by the Commission in its decision. The test says that AB is not a single product if there is a market for B separately. On this ground PC OS and WMP were found to be separate products, since there are independent manufacturers of media players. Evans and Padilla argue that with this application of the test there are bound to be absurd results. They present several examples of products that we do not see as

¹²⁷ Dolmans and Graf, p. 238.

¹²⁸ Ibid, p. 225.

¹²⁹ Ibid, p. 240.

¹³⁰ Evans and Padilla, p. 505.

separate products, such as shoes with laces, mobile phones with SIM cards, computers with hard drives etc. They say that every product for which there is an aftermarket with spare parts would be defined as separate products rather than one single product with this analysis. In their view the Commission appears to be applying an extension of tying law to a large amount of products that are built from different components or based on technological integration of new features.¹³¹

Furthermore also Pardolesi and Renda are sceptic towards the Commission's approach. When investigating the different conditions for an illegal tie under Article 82(2)(d) they find that the foreclosure effect is hard to prove. They particularly question the Commission's claim that Microsoft could rule out competitors just by integrating WMP in its OS, since there are many ways for a competitor to bring a media player to the market. The most common one seem to be direct download from the Web, where it only takes a few minutes to download. Most users also keep more than one media player on their computer, since it only takes up negligible space on the hard disk. Moreover the existing media players support different formats. To stream an audiovisual file, a special media player might be required. However if the user does not have this particular media player it can easily be downloaded from the Web and streaming will then be possible. It is one of the reasons why most users end up with more than one media player on their computer. This practice shows that commercial agreements between the producers of media players and the content producers are the key for a media players commercial success. Following this reasoning, Pardolesi and Renda find it difficult to imagine that Microsoft's tying conduct would have the effect of actually determining competitors' exit from the market.¹³² Finally they find it worrying that the Commission has not treated the issue of consumer harm in the decision, and that a technological integration case has been treated exactly as an old-fashioned tying claim.¹³³

¹³¹ Ibid, p. 511f.

¹³² Ibid, p. 559.

¹³³ Ibid, p. 564.

5 The EC tying approach

There are different approaches to take for competition authorities when making a legal analysis of a practice, such as tying. The *per se approach* includes both per se prohibition and per se legality. Per se prohibition is reserved for conduct that is manifestly anticompetitive and amount to nearly absolute prohibitions. Per se legality means that tying will automatically be regarded as legal provided that certain criteria are satisfied. These rules are normally reserved for those situations where economic theory and experience indicate that the risk of harming competition is so rare that it is unnecessary to weigh the pro-competitive and anti-competitive effects of the conduct against each other. The *modified per se approach* is an extension of this first approach, and is used in those cases where a simple assessment of the market has been done. The *rule of reason approach* means that the legality is determined through a case-by-case application. All of the circumstances in a case are examined before deciding whether a tie should be prohibited because it imposes an unreasonable constraint on competition, or permitted on account of its beneficial effects.¹³⁴

The case law shows that the Commission has been quite hostile towards tying because of its concern that other companies might be excluded from the market. It fears that a tie will enable a company that is dominant in one market, to extend its market power into a second market and thereby exclude other companies from the second market.¹³⁵ The economics of ties and monopoly profits are complex and neither the Commission nor the Courts have really addressed the issue. Arguments about systems and quality have been dismissed and their policy seems to have been more about the protection of small firms and competitors, rather than efficiency and free competition.¹³⁶

5.1 From per se approach...

Prior to the Microsoft case, the Commission and the European Courts have consistently applied a *per se* prohibition approach to tying, without ever really considering whether the tying in question was actually harmful for consumers. It appears as though they have been focusing on the form when assessing tying arrangements, rather than the effects of the practice.¹³⁷ Ahlborn, Evans and Padilla present two possible reasons why tying has been treated as per se prohibited for so long in the EC. The first one is that it has taken longer for new developments in economic theory to affect competition policy. The old pre-Chicago school considerations still rule, even though

¹³⁴ Ahlborn, Bailey and Crossley, p. 177.

¹³⁵ Korah, 2004, p. 140.

¹³⁶ Jones and Sufrin, p. 462.

¹³⁷ Ahlborn, Bailey and Crossley, p. 185f.

they are sometimes presented as post-Chicago reasoning. The second reason is the “special responsibility” that EC competition law imposes on dominant companies, not to allow their conduct to impair undistorted competition. This makes the finding of an abuse easier, in particular where a dominant company has an efficient behaviour, and no assessment to find out the effects of the dominant company’s behaviour seems to be necessary.¹³⁸ The test that has been applied in the *per se* approach has been a three-step test, where a finding of: (1) *market power*, (2) *separate products* and (3) *coercion* has been enough for a tying practice to be abusive.

Dominance in the market for the tying product has been established in all tying cases as we have seen earlier in this paper. One criticism however, and perhaps an explanation for this, is that in some of the cases the market has been defined so narrowly that a finding of dominance was inevitable.¹³⁹ This was the case in for example *Hilti*, where Hilti-compatible nails were found to be a separate market.

In all tying cases there has been a tendency to focus on whether the products supplied together are separate or not. That the products are separate is a prerequisite for a tying to exist, still it does not automatically mean that it is an abuse. Even so, the Commission’s and the Community courts’ analyses has been limited to this separate products test. Commercial or efficiency explanations have not been accepted, as we have seen in both *Hilti* and *Tetra Pak II*. What follows from those cases is that as long as there is a demand for acquiring products separately, a demand for using the products together is not sufficient to justify a tie.¹⁴⁰ Once it is shown that the products or services that are tied together are in different markets, a dominant undertaking cannot rely on the words about nature and commercial usage in Article 82 (d).¹⁴¹

In both *Hilti* and *Tetra Pak II* the element of coercion was satisfied by the establishment that the policies by the dominant companies, or the contractual obligations, left the customers without a choice as to their sources when acquiring products.¹⁴²

Economists agree that tying in many cases can be pro-competitive. Therefore the *per se* prohibition that has been applied in the EC for so long seems inappropriate.¹⁴³

¹³⁸ Ahlborn, Evans and Padilla, p. 317.

¹³⁹ Ahlborn, Bailey and Crossley, p. 192.

¹⁴⁰ Rouseva, p. 602f.

¹⁴¹ Jones and Sufrin, p. 461.

¹⁴² Ahlborn, Bailey and Crossley, p. 193.

¹⁴³ Korah, 2004, p. 146.

5.2 ...to rule of reason

The rule of reason approach has been promoted by leading scholars in both economy and competition law for a long time. Ahlborn, Evans and Padilla deliver a number of arguments in favour of this approach. First of all they argue that since tying is so common in competitive markets, it must provide efficiencies. Secondly, even though anticompetitive effects can occur under certain circumstances, market dominance is just one of the necessary conditions. Thirdly they say that no economic theory finds that market power or dominance is a sufficient condition on its own, for a tying to have anticompetitive effects. Fourthly, a factual analysis must be made to determine if a tying has anticompetitive effects. Economic theory only says that tying *might be* anticompetitive. Fifthly, a factual analysis must also be made to determine if a tying has pro-competitive effects, since also in this aspect economic theory only says that tying *might be* efficient. And at last, a rule of reason analysis is the appropriate framework for conducting the factual analysis described in the above points.¹⁴⁴

Also the EAGCP group find the *per se* approach inadequate. In their report they argue in favour of a more economics-based approach to Article 82, and say that such an approach will naturally lend itself to a *rule of reason* approach to competition policy. This follows since careful considerations of the specifics of each case are needed, and such a requirement can hardly be satisfied under *per se* rules.¹⁴⁵

After consistently applying a *per se* prohibition, it seems as though with the Microsoft case the Commission has changed its analytical framework somewhat and abandoned the outdated approach. A different test, consisting of four steps, was applied when the Commission delivered its decision.¹⁴⁶ The new test formulated by the Commission consisted of (1) *dominance*, (2) *separate products*, (3) *coercion* and (4) *foreclosure*.

Despite this new test though, the position in Microsoft is basically the same as in earlier cases. What differs is that the Commission made an extensive examination of the actual foreclosure effects resulting from Microsoft's behaviour and also considered the efficiency defences put forward by the company.¹⁴⁷ This suggests that a rule of reason approach was applied in the case. The introduction of the foreclosure requirement indicates that the Commission felt that a more extensive analysis was required in this case. It also stated in its decision that there were circumstances in the specific case that made it necessary to examine the effects that the tying of WMP had on competition. In earlier, classical tying cases, the foreclosure effect has been considered satisfied only by demonstrating the bundling of a separate product with a dominant product. In this case the circumstances were

¹⁴⁴ Ahlborn, Evans and Padilla, p. 289.

¹⁴⁵ Report by the EAGCP, p. 3.

¹⁴⁶ Ahlborn, Bailey and Crossley, p. 194.

¹⁴⁷ Völcker, 2005, p. 1712.

somewhat different since the customers had the possibility to download media players for free. Therefore the Commission concluded that the practice had to be analysed further to see whether it would actually foreclose competition.¹⁴⁸

Still, a problem with comparing *Microsoft* with the earlier tying cases is that it deals with technological integration. The Commission decision does not tell us whether the four-step test applied is intended for all tying cases or just the ones that regard technological tying. This makes the new rule of reason approach quite unstable still, and it remains to be seen if the Commission and the Courts will revert to a *per se* prohibition approach.¹⁴⁹

5.3 Objective justifications

Objective justifications have been raised by the dominant companies in several cases, without any success. Hilti referred to safety reasons, saying that independent nail makers did not meet the desired standard. Tetra Pak argued that the tying of the machines and cartons was justified by commercial usage and the nature of the products. Neither of these objections were accepted, and therefore it has been questioned whether a company can ever have success in arguing objective justifications in a tying case. Due to the small number of tying cases in the EC it is difficult to say whether the threshold for an objective justification is particularly high, or whether in the few cases where justifications have been put forward by dominant companies, they simply have not been supported by facts.¹⁵⁰

In *Microsoft* the Commission for the first time analysed thoroughly the justifications made by the dominant company, even though in the end they were rejected. It appears as the Commission in this case tried to show that tying is capable of objective justification. It seems to follow from the *Microsoft* judgment that a dominant undertaking must show that the tying arrangement in question is indispensable for it to compete on the merits, and as a result it is in fact pro-competitive.¹⁵¹

¹⁴⁸ Commission decision of 24 March 2004, *Microsoft*, para. 841.

¹⁴⁹ Ahlborn, Bailey and Crossley, p. 197.

¹⁵⁰ Ahlborn, Evans and Padilla, p. 314.

¹⁵¹ Ahlborn, Bailey and Crossley, p. 196.

5.4 Economic reasoning

The *rule of reason* approach goes hand in hand with the economics-based approach towards Article 82 that so many critics call for. The authors of the EAGCP Report argue that such an approach focuses on improved consumer welfare, and as a result it avoids confusing the protection of competition with the protection of competitors. A careful examination of how competition works in each particular market is necessary in order to evaluate how specific company strategies affect consumer welfare.¹⁵² Depending on the nature of competition and the market, bundling can have exclusionary effects or pro-competitive effects and should therefore be analyzed in the light of the practice.¹⁵³

After many years of debating this lack, the Commission decided to investigate and reform the application of Article 82. Neelie Kroes emphasized in her speech in 2005 that the objective of Article 82 is the protection of competition on the market as a means of enhancing consumer welfare. She also talked about the importance of a foreclosure effect as a result of a dominant company's behaviour, and that this foreclosure should be market distorting and not only affect one or two competitors.¹⁵⁴

¹⁵² Report by the EAGCP, p. 2.

¹⁵³ Ibid, p. 41.

¹⁵⁴ Speech by Neelie Kroes at Fordham in 2005.

6 The Commission's discussion paper

In December 2005 the “DG Competition discussion paper on the application of Article 82 EC to exclusionary abuses”, hereafter called “the discussion paper”, was issued. The discussion paper has no legal value but is a way for the Commission to communicate how the rules should be interpreted.

The discussion paper starts by defining the concept of market definition and dominance. Thereafter it moves on to discuss different categories of exclusionary abuses, and this is where tying and bundling is treated. First of all a definition of tying and bundling is presented, as well as the possible anticompetitive effects that the practice can have. Foreclosure, price discrimination and higher prices are mentioned. Then four points are set up, demonstrating the elements that are usually required for a practice to be prohibited under Article 82(d): 1) the company concerned is dominant in the tying market; 2) the tying and the tied goods are two distinct products; 3) the tying practice is likely to have a market distorting foreclosure effect; 4) the tying practice is not justified objectively or by efficiencies.¹⁵⁵

The Discussion paper is, to a significant extent, a restatement of the case law of the Community courts and the Commission. It is not the radical move towards a more economics-based approach that some might have expected.¹⁵⁶

One thing that is new though, is that the discussion paper introduces a new form of tying, called technical tying, which occurs when the tied product is technically integrated in the tying product. Surely the Commission has been influenced by the Microsoft case, and feels a need to define this new phenomenon in the discussion paper. Akman sees a problem with this new concept, since it will be even harder to prove that two products that are physically integrated are in fact two separate products. It is also noted in the discussion paper that the customers' demand should determine whether or not two products are distinct. A difficulty with this could be that when a new product is introduced with integrated features, it will be impossible to know whether there would be a demand for these features separately. Also, it is worth noting that such an integration of different features could be seen as a natural or commercial link between the tied products and they would therefore fall outside the scope of Article 82(d). Based on this assessment the conclusion can be drawn that the approach from Tetra Pak II, that even a natural link or a commercial usage is not always enough to escape the tying prohibition in Article 82(d), is being reinforced¹⁵⁷

¹⁵⁵ DG Competition discussion paper, p. 55.

¹⁵⁶ Völcker 2006, p. 1428.

¹⁵⁷ Akman, p. 827.

Since the *Discussion Paper* was issued the public has now had the opportunity to comment on it. Both bigger law firms and companies has ventilated their views on the Commission's approach and these comments can now be found on the EU web page. Currently the Commission is reflecting on these comments and it has been said that further steps are to be expected in early 2007. However now it is April and no news has been reported so far. What the next step in the reformation of Article 82 will be is therefore unknown. It has been said that the purpose of the discussion paper is to revise the application of the article. Still no such signs can really be found in the *Discussion Paper* and therefore it remains to be seen what will come of it. Hopefully the Commission has taken note of the debate that has surrounded the tying cases over the last years, and the theories put forward by the Post-Chicago economists. This should in turn bring about a development towards a rule of reason approach and a case-by-case analysis where the special circumstances in each tying case are considered before a tying abuse is condemned abusive.

7 Analysis and concluding remarks

During the course of this paper I have tried to find the answers to three different questions relating to tying and Article 82(d). The first one is whether there is a clear and coherent approach towards tying in the EC. One of the difficulties when making this assessment is the fact that the case law on tying in the EC is not very extensive. Still, after having studied the few tying cases that exists, and in particular *Hilti* and *Tetra Pak II*, the approach by both the Commission and the Community courts seems quite obvious to me. In both these cases a three-step test has been applied. A finding of market power, separate products and coercion has been enough to find a tie abusive. The actual effects of the tie in question have not been investigated and in the cases where justifications have been raised these have generally been dismissed without much discussion. These factors together have suggested that tying has been *per se* prohibited in the EC, an approach that has been criticized by many commentators. Economists have stressed that tying actually is pro-competitive in many cases and therefore it would be more appropriate with a case to case analysis to decide whether a tying practice should be allowed or not.

However with the Microsoft decision the Commission seemed to be shifting its positions somewhat as a new test was applied. The Commission declared that dominance, separate products, coercion and foreclosure were the necessary elements for a tying practice to be found abusive. From a quite consistent *per se* illegality approach, the Commission now seems to consider the actual effects of the practice. The advantages that Microsoft would gain from integrating WMP into its operating system were analysed and considered so great that other media player manufacturers would not be able to compete and therefore driven out of the market. Whether this is a correct analysis or not can be discussed and here the opinions go apart. Still, the main point of this decision is rather that the Commission has actually focused on the effects of Microsoft's behaviour, which it has not done in earlier cases. Some commentators mean that this is an indication of a movement towards a more effects-based approach towards tying, meaning that the so criticized *per se* illegality approach has been abandoned for a *rule of reason* approach. Whether this is correct however, cannot be answered at this point, considering the special circumstances in the Microsoft case. It concerned technological tying and therefore some authors have argued that maybe the new approach is only valid in those special cases. Based on this I would say that the tying approach in the EC is at the moment rather unclear. It is possible that the debate around the outdated *per se* illegality has finally sunk in with the Commission but this remains to be seen with future tying decisions. Also the judgments from the CFI and possibly the ECJ might shed some light on this question.

My second question is how tying should be treated in the context of Article 82(d). When studying the case law I find it pretty obvious that both the Commission and the Community courts have treated tying with hostility, since in most cases it has been found to be illegal. The critique that has been brought against the view on tying in the EC is mostly based on the lack of both an economic perspective and the lack of an assessment of the consequences of the tying practice. Economists agree that tying in many situations can be good for competition. Certain tying practices can however also be anti-competitive, but this has to do with whether they foreclose other companies from the product market and thereby ultimately cause harm for competition. Another critique that has been brought against the tying policy in the EC is that the original subject for protection in the paragraph, the customer, has been put out of focus. Instead the companies and whether they are being foreclosed from the market is now the focus of protection.

Historically the authorities have had a tendency to look at tying only as a method to restrict competition. It has therefore been viewed as something that harms the consumers. However with the economic research that has been done, the attitude has changed over the last years. The Post-Chicago theories show that several efficiency reasons can be achieved through tying and bundling. The motives for companies to engage in the practice is not so much to restrict competition, but rather to save money and increase efficiency. The fact that so many companies engage in tying practices also indicates that it provides a lot of efficiencies. These circumstances make the *per se* approach inadequate when assessing tying practices, since it is a tool that is reserved for practices that are subject to absolute prohibitions. Under this approach all tying practices will be treated the same and focus will be on the form of the practice, not what the actual effects on competition are.

The fact that a tie can be both good and bad for competition suggests that it would be more suitable to look at the effects of the practice. The *rule of reason* approach would be a far better tool for this, since it separates the pro-competitive and anti-competitive practices from each other. It will also force the authorities to involve an economic reasoning when they evaluate individual cases. By using this approach, companies would be offered the ability to compete and at the same time competition in the Community would be protected since the tying practices that were actually harmful for competition would be detected and stopped. The Commission's reasoning in the Microsoft case is one step on the right way towards such a *rule of reason* approach, even though we still do not know what will be the consequences of that decision in the long run.

Another indication that the EC is moving towards a *rule of reason* approach is the Commission's discussion paper. Neelie Kroes said in her speech at Fordham that “./the exercise of market power must be assessed essentially on the basis of its effects in the market”.¹⁵⁸ She also said that aggressive competition is good, also by dominant companies. It is all right if it hurts competitors, as long as it ultimately benefits the consumers.¹⁵⁹

This discussion paper is, apart from the Commission's shift in attitude in *Microsoft*, another big change for tying law. The paper was issued in 2006 as a result of the debate that has surrounded the application of Article 82 during the last years. It is now time for a reform of the article, in the footsteps of the reformation of Article 81, and the expectations have been high. In her speech, Neelie Kroes marked that a shift towards a more effects based competition policy was necessary and that Article 82 should be used to protect the consumers. This indicates an abandonment of the *per se* illegality view on such practices as tying. Still, the approach taken in the discussion paper is not as radical as was hoped. It does not take a clear stand in favour of a *rule of reason* approach and an economics based analysis, but rather summarizes the Commission's and the Community courts' approach in tying cases. The outcome of the Commission's discussion paper is therefore quite hard to predict. Also, the Commission is still reflecting on the comments received by the public and what the next step will be is unknown.

Nevertheless, I believe that the discussion paper is just the start and that it will ultimately lead to more of a *rule of reason* approach. The comments received on the discussion paper, together with the debate on the tying approach will probably reveal a demand for a change in the current policy. Hopefully the outcome will be some kind of guidelines, where the tying policy is outlined. It will also be interesting to see how the Commission handles the next tying case that comes in front of it, and whether the approach in *Microsoft* will still be relevant.

¹⁵⁸ Speech by Neelie Kroes at Fordham in 2005.

¹⁵⁹ *Ibid.*

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