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The Law of Abuse
A more economic approach to article 82

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Summary

This thesis examines the objectives of Article 82 and the enforcement by the Commission and Court. The discrepancies are then analysed with reference to leading legal scholars. Finally, possible outlooks are scrutinized and weighed against the criticism towards the former application.

In December 2005, the DG Competition presented its Discussion Paper on the application of Article 82 of the Treaty to exclusionary Abuses, which is part of the present review of Article 82 and an important factor for the modernisation of the law of abuse.

Earlier in 2005, the Economic Advisory Group for Competition Policy presented its views on a more economic approach to Article 82, which concluded much of the criticism pointed at the previous application.

The policy on the application of article 82 of the EC Treaty has been subject to, above all, economical critique for some time. There has been a lack of consistency in the case law and the reasoning of the Court and the Commission has occasionally been difficult to follow. It has also been confusion on who is to be protected - consumers or competitors, and critical voices have said that it is actually dominance that is forbidden and that competition on merits is not possible. In order to turn the EC market into one of the most competitive and customer-orientated markets of the world, the Commission has decided to review and clarify its approach to Article 82.

There are essentially two approaches to the assessment of abuse of a dominant position. One is the form-based approach, which builds upon separate scrutiny of a previously defined practice. The other approach is the effects-based approach, in which the authorities focus on the specific circumstances of each case. Many economists advocate the effects-based approach, since it could lead to a more efficient application from an economic perspective. The main critique towards such an approach is that it might lead to a high degree of legal uncertainty and deprive Article 82 of legal status.

The Commission seems to, to some extent, have chosen the more effects-based economic approach, advocated by many economists. Such a new approach would be welcomed by many dominant companies, since where the Commission in the past has deemed a conduct as abusive where it just potentially would restrict competition, it will now as it seems, apply a more detailed analysis on the effects on the market of such conduct. In particular in the area concerning rebates, there seem to be a move away from the per se regulation which has been more or less the case in the past. New is also the view that the dominant company should have possibilities of objectively justifying its behaviour.

Many of the difficulties of the application of Article 82, however, seem to remain, for instance the problems of requiring necessary information on cost/price-calculation for the assessment of the efficiency of the undertaking.

Abbreviations

| | |
|-------|---|
| CFI | Court of First Instance |
| CMLR | Competition Market Law Review |
| DG | Directorate General |
| EAGCP | Economic Advisory Group for Competition Policy |
| EC | European Community |
| ECR | European Court Reports |
| EU | European Union |
| F e | For example |
| GCLC | Global Competition Law Centre |
| SSNIP | Small Significant Non-transitory Increase in Price |
| USA | United States of America |

1 Introduction

In the perfect transparent competitive market the competitors would have similar and very small market shares, there would be plenty of buyers and sellers for homogenous products and no barriers to market entry or exit. A market that by nature lives up to these parameters is, however, almost impossible to find and without control firms would in many cases most likely put their own interests before those of the consumers.¹ In the case of the EC an additional objective for the competition regulations is to create a single market for the whole union, built upon those ideals of perfect competition.²

One of the primary objectives of EC competition policy is to promote the Lisbon agenda strategy: to make of the EU “the most competitive and dynamic knowledge-based economy in the world” by 2010.³ Competition Commissioner Neelie Kroes has addressed the review work of article 82 of the Commission as a;

*“search for sensible “rules” that would enable us to reach preliminary conclusions about when conduct may exclude competition, yet at the same time allow companies to know when they are on safe ground. Such an approach would have the advantage of being based on solid economic thinking while at the same time giving clear indications to companies and maintaining workable enforcement rules.”*⁴

The appointment, in 2003, of a chief economist is a step by the Commission towards a more economic analysis of its competition policy and the EAGCP Report and the recently published Discussion Paper are important parts in the review of the application of article 82.

1.1 Purpose and Delimitations

This thesis aims at:

- defining the difficulties of the application of article 82 EC Treaty

¹ Albers Llorens, EC Competition Law and Policy, p 1

² See the XXIXth Report on Competition Policy, paras 2 and 3

³ As expressed by former European Commissioner for Competition Policy Mario Monti in a speech at the Center for European Reform in Brussels in October 2004, available at <http://www.eu.int/rapid/pressReleasesAction.do?reference=SPEECH/04/477&format=HTML&aged=0&language=EN&guiLanguage=en>, last visited on 2006-01-26

⁴ As expressed in a speech at Fordham Corporate Law Institute in New York in September 2005, available at <http://www.eu.int/rapid/pressReleasesAction.do?reference=SPEECH/05/537&format=HTML&aged=0&language=EN&guiLanguage=en>, last visited on 2006-01-26

- presenting an overview of the criticism put forward against the application of article 82
- examining solutions to the difficulties and evaluating these against the objectives of and the criticism on article 82

I have chosen to focus on exclusionary abuses and will therefore only briefly comment the exploitative forms of article 82 infringement. The reason for this is that the Commission in its Discussion Paper only discusses exclusion and the Discussion Paper serves as a base for my evaluation of the solutions to the difficulties.

Very detailed economic analysis has been made by scholars in the area of market definition, the effects of rebates and pricing. To be able to present a clear overview, which serves the comparative objective of this thesis, I have just briefly summarized these commentaries.

The notion of collective dominance and the difficulties surrounding it constitutes a special area of analysis and will, due to the limitations and purpose of the thesis, not be subject to detailed analysis within this thesis.

1.2 Method and Material

For the purpose of this thesis, I have studied the case law, legal literature and legal/economic commentaries, as well as the documents of the modernisations package of the Commission – a research method characterised as legal dogmatic.

I have used case law and legal literature, as for instance the comprehensive works of Craig & De Bùrca⁵, Faull & Nikpay⁶ or Whish⁷ to be able to present the base for and objectives of EC competition law.

For the discussion in chapters 3 and 4, I have used material written by the leading scholars on the field of competition law as well as economic commentaries, many of them found on the internet, for instance on the homepage of the European Union. The Discussion Paper of the Commission⁸ and the EAGCP Report⁹, which are available on the internet have served as basis for chapter 4, since these papers conclude the latest development and the relevant legal and economic views on the function of article 82.

⁵ Eu Law, Text Cases and Materials, Oxford University Press, 3d ed, 2003

⁶ EC Law of Competition, Oxford University Press, 1st ed, 1999

⁷ Competition Law, LexisNexisUK, 5th ed, 2003

⁸ Staff Discussion Paper -available at <http://europa.eu.int/comm/competition/antitrust/others/discpaper2005.pdf>

⁹ Report by the EAGCP "An economic approach to Article 82"

I have, to great extent used the research portal Elektra at the University of Konstanz and the German legal database Beck Online, to find the latest articles on the modernisation of article 82.

1.3 Disposition

In chapter 2, I try to elucidate the objectives of European competition policy and to explain the difficulties of the application of article 82 so far. The chapter is fundamental for understanding the criticism described in chapter 3. The chapters 2 and 3 shall give the reader an idea of why the Commission is currently reviewing its application of article 82. In chapter 4, I present solutions to the difficulties, as suggested by the Commission itself in its Discussion Paper and of the Economic Advisory Group for Competition Policy in its Report. These solutions are then commentated in comparison to the objectives and the criticism presented in chapters 2 and 3.

In chapter 5, I have added my own comments to the modernisation of article 82 EC Treaty.

2 Objectives, scheme and procedure of article 82

2.1 The objectives of article 82

The principal objectives of the EC Treaty are to find in article 2. By establishing a common market and common policies, a balanced and sustainable development of economic activities is to be reached. Mentioned are also concerns on employment, social protection, sustainable growth, protection of environment, high living standard and a high degree of competitiveness.

Competition law as a means of reaching the objectives of article 2 is mentioned in the following article 3.1(g). The activities of the Community shall include a system ensuring that competition is not distorted in the internal market.

Initially, the most important way of ensuring this, was to prevent private actors from replacing the public obstacles to inter-state trade.¹⁰ That the articles 81 and 82 form part of this system is clear not only by the formulations of the Treaty, but has also been confirmed in cases like *Continental Can*, which was the pioneer-case in the field.¹¹

Article 82 aims at controlling the activities of firms whose economic strength makes them less sensitive to the actions of competitive forces in a given market. The control covers the activities of dominant sellers, dominant buyers and situations of joint dominance.

Market power enjoyed by a firm can be dangerous in the sense that the firm might be able to operate inefficiently for long periods or charging higher prices than would be possible if there was more competition. This could lead to resources being used to produce things less wanted by the consumers, since higher prices reduce demand to a non-competitive level, a concern known by economists as “power over price”.¹²

The case law has revealed two different objectives of article 82. The first is to protect consumers and economy as a whole –which requires the balance between efficiencies/incentives and negative effects to be taken into consideration and the second is to protect competitors of the dominant

¹⁰ Wesseling, *The Modernisation of EC Antitrust Law*, p 48-49

¹¹ Case 6/72, *Europemballage Corporation and Continental Can Co Inc v Commission*: [1973] ECR 215

¹² Korah, *An Introductory Guide to EC Competition Law and Practice*, p 91 (hereinafter Korah)

firm.¹³ The tension between these two objectives is revealed through the case law and will be further discussed in chapter 3, on article 82 policy and its criticism in this essay.

2.2 Scheme and procedure of article 82

Article 82 provides:

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 other 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.*

From the above is to be read that the article applies to:

- only undertakings that hold a dominant position
- dominant position that is held within the common market or a substantial part of it
- undertakings that are part of the same economic group or linked by such economic links that a dominant position is held¹⁴
- abuses of such dominant position in so far as it affects trade between member states

Moreover, a-d can be read as follows:¹⁵

- (a) Covers exploitation. For instance, when the dominant undertaking takes advantage of its customers by charging excessive prices or impairing unfair terms.
- (b) Covers exclusionary conduct, such as foreclosure and other behaviour, which excludes from or prevents competitors to

¹³ Ibid., p 91

¹⁴ See Case 6/72, *Europemballage Corporation and Continental Can Co Inc v Commission*: [1973] ECR 215 paras 20-27 and the decision of CFI in Case T-68/89, “Flat Glass”, *Societa Italiano Vetro Spa v Commission*: [1992] ECR II-1403

¹⁵ Temple Lang & O’Donoghue, GCLC, p 39-40

enter a market. This is the most frequently used category of abuse.

- (c) Covers discrimination and is, arguably, often invoked under exclusionary behaviour.
- (d) Covers tying –but is not a per se prohibition.

Dominance is not illegal per se. It is the abuse of the dominance that is prohibited by the article.¹⁶ However, firms in dominant positions are underlying a special responsibility, not to allow their conduct to distort competition.¹⁷ Further, on, it seems like this special responsibility becomes greater if the firm is not merely found to be dominant but super-dominant.¹⁸ It has been questioned in the legal literature¹⁹, whether these special responsibilities are not leading to serious disincentives to dominance.

By contrast, to article 81, article 82 concerns unilateral behaviour. However more than one undertaking can be subject for scrutiny under the article when the dominance is joint or collective and the firms form an economic unit.

2.3 Determining dominance

The determination of dominance under article 82 traditionally involves a two-stage procedure.²⁰ First, it is necessary to determine the relevant market and secondly the power of the dominant firm thereon is to be assessed. There are scholars, who would like these steps to be taken not separate but in a joint analysis. This discussion will be highlighted in the chapters 3 and 4.

There are a number of issues arising from the concept of the relevant market and due to the limits of this essay, I will just mention some of particular relevance.

2.3.1 Relevant market

In the Commissions Notice on the Definition of the Relevant Market for the Purposes of Community Competition law,²¹ three dimensions of the market are described. These are the product, geographical and temporal dimensions.

¹⁶ See Case 6/72, *Europemballage Corporation and Continental Can Co Inc v Commission*: [1973] ECR 215, para 26

¹⁷ See Case 322/81 *Michelin v Commission* [1983] ECR 3461, para 57 and Case 85/

¹⁸ Whish, *Competition Law*, p 189-190

¹⁹ See Korah, p 116 f, 390 f, Whish, p 150 f, Jones and Sufrin, p 227 f, Faull and Nikpay, para 3.13-3.19

²⁰ Whish, p 152, see also Case 6/72 *Continental Can* [1973] ECR 215, paras 32 and 37

²¹ [1997] OJ C372/5

The product market shall be defined with regard to both the demand-side and supply-side substitutability. On the demand-side, the interchangeability is measured through the cross-elasticity of demand, while the supply substitution has been dependent on the possibilities to switch from the production of one product to another for the purpose of including the switched products in the same market.²² In the Group Exemption on Vertical Agreements,²³ the Commission has taken the view that the relevant product market shall be defined out of the products interchangeable to the consumers with regard to the price, intended use and characteristics of the product.

The geographical dimension is dependent upon the homogeneity of the conditions of competition for the product within the market where it is marketed. The effect of the economic power of the undertaking concerned must be possible to evaluate.²⁴ To be remembered is that it is only the abuse of the dominant position within the Common Market that infringes article 82.²⁵

The temporal dimension is mainly of importance for the market-definition in cases concerning seasonal goods, where demand is changing from season to season.²⁶

Since these dimensions on the definition alone do not take into account the possibility of competitive pressures from outside the defined market, there can also be of some importance to look at potential competition when defining the market where dominance shall be assessed.²⁷

In the Notice, the Commission shows signs on a new, less formalistic and more effect-oriented, approach to the definition. Besides the classical dimensions explained above, the Commission intends to adopt the, in the USA developed, SSNIP test. The relevant product market will, according to this test be defined through “the smallest set of products for which a small but significant and non-transitory increase in price (5 or 10%) by a hypothetical monopolist would be profitable”²⁸. If demand substitution is enough to make the price-increase unprofitable, a wider range of products is to be included. However, there are problems applying the SSNIP test. These will be commentated in the chapter on policy criticism below.²⁹

Another sign on effect-based approach in the Notice is the statement of the Commission to consider among other facts; barriers and costs for substitution, when deciding the relevant product market.³⁰

²² Faull and Nikpay, The EC Law of Competition, paras 1.138-1.140

²³ Reg 2790/99 on Vertical Distribution Agreements, Art 9

²⁴ Case 6/72 *Continental Can* [1973] ECR 215, paras 11 and 44

²⁵ Korah, p100

²⁶ Case 6/72 *Continental Can* [1973] ECR 215, paras 11 and 44

²⁷ Korah, p 96

²⁸ See <http://www.frg.eur.nl/rile/LL.M/CLE2.04.doc> (last visited on 4th Nov 2005)

²⁹ See chapter 4.2

³⁰ Craig and de Burca, EU Law, Text Cases and Materials, p 1001

2.3.2 Market power

The second step is the assessment of market power. This can be, and has been done in different ways. The legal definition of dominant position – which differs from the economic one, has been developed by the Commission and courts and has more or less stayed with the formula expressed in *United Brands* –where a dominant position is described as;

*"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 consumers."*³¹

The main indicators of market power have also been set of the Commission and courts, the most obvious one being the use of market share measurement. When an undertaking has a very large market share in the relevant market, it is likely that the Court will also find it dominant.³² A large market share does not per se indicate that the undertaking is dominant, as seen in *United Brands*, where the Court held that a market share of 40 and 45 per cent of the market did not on its own determine that the firm was dominant, but that the number and strength of the competitors had to be considered.³³ In the case, *United Brands* had a market share several times greater than the nearest competitor had and was therefore considered to be dominant. In the case *Hoffman-La Roche*, the Court established the fact that Hoffman-La Roche had very high market shares (75-87%) in a number of markets and considered therefore that no further examination was needed for determining dominance.³⁴ To be remembered, is of course also that an undertaking with a large market share will much more easily attract the Commissions' attention, and will potentially be "deemed" to special responsibility.

There is also a time factor involved when deciding dominance through market share measurement. When a company has a high market share over a period of time, it has been considered as strong evidence for dominance.³⁵ Whereas market shares held for short periods of time will probably not be sufficient evidence for the existence of a dominant position.

³¹ Case 27/76 *United Brands v Commission* [1978] ECR 207, para 65

³² Case 85/76 *Hoffman La Roche v Commission* [1979] ECR 461, para 24

³³ Case 27/76 *United Brands v Commission* [1978] ECR 207, paras 109 and 110

³⁴ Case 85/76 *Hoffman La Roche v Commission* [1979] ECR461, See also Case T-30/89 *Hilti v Commission* [1992] ECR II 1439 and Case T-83/91 *Tetra Pak International v Commission* [1994] ECR II 755

³⁵ See Case C-62/86 *AKZO Chemie BV v Commission* [1991] ECR I 3359 and Case 322/81 *Michelin v Commission* [1983] ECR 3461

The size, resources, degree of vertical integration and technological lead of the undertaking, are also factors that have been taken into account by the Court. In *Hoffman-La Roche*, the Court considered that the company had a turnover, which widely exceeded its competitors³⁶. In *Michelin*, the facts that Michelin was superior in investment and research and that the undertaking had an efficient and high qualitative service-network, were held as indicators of dominance.³⁷ The importance of vertical integration was stressed in *United Brands*. Since the company knew that they, irrespective of the market situation, were never to be forced to transport less than 2/3 of its average volumes of sales of bananas, it enjoyed commercial stability. This factor was taken into account for the finding of dominance.³⁸ Technological advantages, especially in the form of intellectual property rights, have also been held as indicators of dominance. This since such rights, often in combination with a large market share strengthens the lead over the competitors.³⁹

Considerations on size, resources, degree of vertical integration and technological lead of the undertaking, as mentioned above, are all factors that can be included as elements when analysing barriers to entry with the aim of determining dominance. The definition on barriers to entry will be further discussed in chapter 4.

2.4 Determining Abusive Behaviour

As mentioned above, dominance is not per se forbidden. The fact, however, that dominant firms cannot take certain steps that non-dominant firms can, makes it complicated to define what constitutes abusive behaviour. I will in this part of the essay just mention what types of abusive behaviour have been acknowledged by the Commission and Court and I will explain the difficulties closer in the chapter on policy criticism.

Some scholars have chosen to draw a strict line between exclusionary abuses –harming the competitive structure of the market and in the first place competitors and exploitative abuses, which are directly harmful to consumers.⁴⁰ This makes it easier to distinguish between the policies applied by the Commission, but has not always contributed to clarity. In the long run, exclusionary abuses can, of course, give the dominant firm the opportunity to exploit its position on the expense of the consumers. Abuse can also contain both exclusionary and exploitative elements. Therefore, I will in this paper not treat the types of abuses separately.

³⁶ Case 85/76 *Hoffman La Roche v Commission* [1979] ECR461, para 47

³⁷ Case 322/81 *Michelin v Commission* [1983] ECR 3461, paras 55 and 58-60

³⁸ Case 27/76 *United Brands v Commission* [1978] ECR 207, paras 70-81

³⁹ See Decision 88/501 of the Commission *Tetra Pak I* [1988] OJ L 272, para27

⁴⁰ Faull & Nikpay, para 3.117, Craig and deBurca, p 1007-1008

To keep in mind is that abuse is an objective concept and that lack of intent therefore cannot be put forward as a defence.⁴¹ However, the subjective element has been of certain relevance when the Commission has set the fines.⁴²

The concept of abuse has through the years, more or less been defined through the wide description in *Hoffman-LaRoche*.

*"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."*⁴³

The examples in article 82 are as mentioned above not exhaustive and there have been some forms added through the case law. I will now mention some of these cases and some of the examples on abuse in article 82.

2.4.1 Imposing unfair purchase or selling prices or other unfair trading conditions

A dominant firm may not set prices that are excessive in relation to the economic value of the products or services. Such behaviour is to be considered as abusive in accordance with article 82(a). However, this can be hard to prove in practice, since there are more or less impossible to trace production costs and other indirect costs. There can also be objective justification for the high prices. In cases like *General Motors*⁴⁴, the Court found the excessive prices temporary and objectively justified and that General Motors (who had administrative monopoly) had given an adequate explanation. General Motors had also lowered the prices to a "normal" level again, before the Commissions' intervention, a fact that probably was beneficial. In *United Brands*⁴⁵, the Court found that the Commission had failed on proving that the price was unfair although there were obvious shortcomings in the explanations of the company.⁴⁶

⁴¹ Case 85/76 *Hoffman La Roche v Commission* [1979] ECR 461, para 91

⁴² *Faull & Nikpay*, para 3.123

⁴³ Case 85/76 *Hoffman La Roche v Commission* [1979] ECR 461, para 91

⁴⁴ Case 26/75 *General Motors v Commission* [1975] ECR 1367, paras 11-24

⁴⁵ Case 27/76 *United Brands v Commission* [1978] ECR 207, paras 248-249

⁴⁶ *Ibid.*, para 264

United Brands had also imposed unfair conditions of sale on its distributors. In the general conditions of sale, United Brands had forbidden the resale to foreign dealers of bananas that were still green. This clause had as effect as to almost completely prohibiting exports. This in combination with the fact that United Brands had supplied its distributors with smaller quantities than those ordered to strengthen its economic hold on them and to prevent them from developing competitive response through exports in the Community market, amounted to abuse.⁴⁷

2.4.2 Limiting production, markets or technical development

This type of abuse is formally very hard to define, since the authorities applying competition rules do not have the means or possibilities to perform the kind of investigation necessary to decide if the company produces a lower level of output or innovation than a competitive environment would produce.⁴⁸ If a dominant company, however, suddenly stops producing a product or produces a lower output of innovation without objective justification, such as the coverage of losses generated from that specific product, and if the interruption harms the interests of the consumers, it is likely to constitute abuse of a dominant position within the meaning of article 82. A very clear example of such conduct was shown in *British Leyland*⁴⁹, where a car manufacturer in Great Britain refused to renew the licenses for left-hand drive cars. This was considered to be exploitative since the company thereby, and without objective justification, foreclosed the British market from parallel imports; a conduct that still is regarded blacklisted.

Another indicator on exploitative behaviour within the meaning of article 82(b) is if the dominant company, through its limited output, leaves a substantial amount of demand unsatisfied.⁵⁰ A more recent case illustrating such behaviour is *Re The 1998 Football World Cup*⁵¹. In this case, one of the ticket distributors –the French CFO, sold “blind tickets” (i.e. tickets for matches where the teams were not decided at the time of the purchase) only to consumers who could provide a postal address in France. The view of the Commission was that this practice, to the prejudice to consumers, limited the market for ticket sales outside France and that this could not be justified on security grounds, which had been put forward as justification of CFO.

⁴⁷ Case 27/76 *United Brands v Commission* [1978] ECR 207, paras 155-161

⁴⁸ Faull & Nikpay, para 3.314

⁴⁹ Case 226/84 *British Leyland v Commission*

⁵⁰ Faull & Nikpay, para 3.316 and Case C-41/ 90 *Höfner* [1991] ECR I- 1979

⁵¹ Commission Decision 2000/12/EC OJ [2000] L 5/55, para 91

In-efficiency of a company in a dominant position can also be considered as an abuse within the meaning of article 82.⁵² It might not be necessary for a dominant company to make new innovations or to be efficient in other means if it has no competitive pressures on it. This might lead to a limitation of technical development within the meaning of 82(b).⁵³

2.4.3 Discriminatory Practices

One of the core principles of the internal market is the principle of non-discrimination and the case law on article 82(c) shows that matters on discrimination are treated with much concern also in the field of competition law. The case law under article 82(c) has been largely criticised.⁵⁴ Many scholars are of the opinion that certain forms of price differentiation are directly beneficial to consumers and that the approach of the Court and the Commission under article 82(c) does not to a satisfying extent consider the effects of or grounds for such pricing.

The prohibition aims, in the first place, at price discrimination, which occurs when a dominant firm charges different prices for the same services or products.

In the previously mentioned *United Brands*⁵⁵, the dominant company was held to have abused its dominant position by charging different prices in different member states. This type of discrimination can be referred to as geographical. *United Brands* was selling identical products from the ports of Bremerhaven and Rotterdam and held that the pricing policy was objectively justified since there were great differences in what the markets in the different member states could bear due to among other factors, demand. These variations in market conditions were not recognized by the Commission and Court. Special emphasis was instead laid down on the facts that identical products were sold in the same place at widely differing prices and that *United Brands* were not directly selling the bananas to the different markets, but through resellers and therefore not had to bear the risks tied to the different market situations.

It is likely to think that the Commission and Court, although they treated the resale restrictions and discriminatory pricing separately, were particularly concerned with the combination of the price discrimination and the resale clauses discussed above⁵⁶, which they saw as a deliberate attempt to part the Community market.⁵⁷

⁵² Whish, p 196

⁵³ See Case 360/36 *British Telecommunications v Commission* [1983]1 CMLR 457

⁵⁴ See f e Korah, Whish

⁵⁵ Case 27/76 *United Brands v Commission* [1978] ECR 207

⁵⁶ See 3.2.1

⁵⁷ Case 27/76 *United Brands v Commission* [1978] ECR 207, paras 155-161

The judgement in *United Brands* has been sharply criticised for its lack of economic reasoning.⁵⁸ The discriminatory pricing was not proved to reduce efficiency and the harm to consumers was therefore not determined. It has also been argued that, what was to be condemned, were the resale restrictions and the practice of insufficient supply alone. Since *United Brands* was selling the bananas through resellers and not directly to consumers, the market was from alone to be integrated. It is also held to be unreasonable to prohibit geographical discrimination at all for integrated firms since the costs for marketing the products can differ substantively between different national markets. Hindering dominant firms from pricing optimally has been considered too far going and can be seen as resulting in forcing dominant firms to implement public policy.⁵⁹

The granting of rebates by a dominant company has been considered to constitute abusive practices at a number of occasions and the judgements have also been subject to massive criticism.⁶⁰

Rebates can have a number of anti-competitive effects such as discouraging market entry or foreclosing vertically and horizontally. Market entry is hindered when the customers would switch to another supplier if the rebates were not offered or in the case of quantity rebates where short-time sacrifices often have to be made to get the rebate. Horizontal foreclosure is the case when the rebates tie together products of the firm on different markets, by being offered to customers who buys from both the markets concerned. Vertical foreclosure appears when the dominant firm integrate downstream, granting rebates to its retailers encouraging them only to sell its' products. This can have similar effects to contractual single-branding clauses.⁶¹

In *Irish Sugar*,⁶² the dominant company was considered to protect the Irish sugar market from imports through the granting of certain types of rebates offered to customers who bought the sugar on the Irish side of the border area to Northern Ireland. The aim behind the practices was to prevent import of sugar to low costs –inclusive re-imports of Irish sugars' own products, from Northern Ireland. The company also offered rebates on industrial sugar to companies who were exporting the end products to other Member States. This was considered as to distort trade between Member States and fell under article 82(c) since the rebates led to dissimilar conditions applied to equivalent transactions and thereby discriminated against the local processors. *Irish Sugar* held that the Irish processors were not put in disadvantage to the exporters since they were competing in different markets. However, the Commission in *Irish Sugar*⁶³ found that quantity

⁵⁸ See Bishop "Price discrimination under Article 86: political economy in the European Court", [1981]44 CMLR 282

⁵⁹ Faull and Nikpay, para 3.328

⁶⁰ Korah, p 173

⁶¹ EAGCP report, p 35

⁶² Case C 497/99R *Irish Sugar v Commission* [2001]ECR I 5332

⁶³ *Ibid.*, para 153

discounts were allowed in reference to individual orders since they have a cost saving dimension objectively justifiable.

Loyalty rebates –irrespective of whether they are initiated of the purchaser, have been considered to be abusive in among others *Hoffman-La Roche*.⁶⁴ In this case, the abusive character of such rebates was defined in three ways. First, they are intended to deprive the customer of the choice of other sources of supply and are thus hindering other producers from entering the markets (entry barriers). They are not based on a specific economic transaction. Secondly, they are abusive because they are discriminatory. This since their effect is that dissimilar conditions are being used on equivalent transactions. Thirdly, loyalty rebates lead to distorted competition since they are strengthening the dominance of the supplier.⁶⁵

Another type of rebates considered to be abusive is so called target rebates. These are discounts given to purchasers that meet specified sales targets. In *Michelin*,⁶⁶ the Court distinguished the types of rebates from the ones in *Hoffman-LaRoche*, since the target rebates did not put any obligation on the dealers to buy exclusively from Michelin. The abusive element connected to target rebates is instead that the rebates in other ways bind the purchasers to the dominant company through the pressure of reaching the quantities necessary for the discounts and thereby discourage them from buying the products from the competitors of the dominant company. This turns such rebates indirectly into a form of loyalty rebates and reduces the cost-saving element. A similar approach was more recently taken by the Commission in *Virgin/British Airways*⁶⁷, where it held that the reward system, dependant on the achievement on certain sales targets, was based on loyalty rather than efficiency and had as the effect to harm the competitors of British Airways. The discriminatory element in this case was, according to the Commission that two travel agents, selling the same amount of tickets, could get different commission depending on if they had exceeded the sales of the previous year or not. The fact that the competitors of British Airways had been able to gain market share from the dominant company, was not considered to make any difference.

Rebate systems that run over a longer period of time are considered to be particularly dangerous since such systems reduce all incentive for the buyer to switch after some time. In *Coca Cola*⁶⁸, the Commission has accepted a reference period of three months.

These cases cast light on the fact that a dominant company has a special responsibility. Rebates and discounts are considered to be part of normal business practices as long as they are not granted by a company in a

⁶⁴ Case 85/76 *Hoffman La Roche v Commission* [1979] ECR 461, para 89

⁶⁵ Case 85/76 *Hoffman La Roche v Commission* [1979] ECR 461, para 90

⁶⁶ Case 322/81 *Michelin v Commission* [1983] ECR 3461, paras 81-91

⁶⁷ Decision *Virgin/British Airways* OJ [2000] L 30/1, paras 97-109

⁶⁸ Commission Press Release IP(90)7 of 8 January 1990, *Coca Cola Export Cooperation, Filiale Italiana*

dominant position. When offered by dominant market actors, rebates of the kind mentioned are very likely to be considered to constitute barriers to entry, distorting competition on the Common Market. As mentioned above this is a position, sharply criticised, which makes it hard to advise dominant firms of what behaviour is compatible with EC competition law. I will treat this criticism in the following chapter on policy criticism.

2.4.4 Tying and bundling

There are several forms of tying and bundling. Tying is when the purchase of one product is made conditional upon the buy of another one and bundling is when two products are sold together. Tying and bundling can for example include products technically connected to each other or through contractual practice.⁶⁹

The classical examples of the abusive behaviour exemplified in 82(d) are *Hilti*⁷⁰ and *Tetra Pak II*⁷¹. The Commission, in *Hilti*, found as an abuse of a dominant position that the dominant company had made the sales of cartridge strips conditional upon the purchase of specific nails belonging to the product, -a supplementary obligation which the company tried to justify on safety grounds. The grounds for the finding of the Commission were that consumers, through the tying clause, were restricted in their choice of sources of supply and that the tying had the effect as to foreclose the nail-market to competitors. The safety argument was rejected by the Court. It held that if safety was the issue for Hilti, the company should have relied on the British legislation on the sale of dangerous products and not have taken protective measures on its own. In *Tetra Pak II*, Tetra Pak was selling packaging machines for dairy products and fruit juices on the condition that only special Tetra Pak cartons were used. Tetra Pak put forward two grounds trying to justify the tying clause. The first one was that the tying was justified on commercial usage since the products were designed for each other. The Court held that even if there would have been a natural link between the products, the tying could still constitute abuse within the meaning of article 82 since the paragraph is not exhaustive. The second ground from Tetra Pak, trying to justify the clause, was concerns on public health. This ground failed since there were other means, more proportionate, to meet the concerns, according to the Court.

Bundling can be exclusionary on the tied market since the customer buys both products from the dominant firm because it is profitable to do so (=mixed bundling) or because they cannot buy the products separately (=pure bundling). Especially pure bundling makes it harder for competitors active on the tied market to sell their products irrespective of if their

⁶⁹ EAGCP report, p 38

⁷⁰ Case T-30/89 *Hilti v Commission* [1991] ECR II 1439

⁷¹ Case T-83/91 *Tetra Pak International v Commission* [1994] ECR II 755, paras 137-139 and C- 333/94P [1996] ECR I 5951, para 37

products are of better quality or can be produced on a low cost. The effects can be said to be the same as with certain loyalty rebates or predatory pricing. Another exclusionary effect occurs when the dominant company bundles its products to protect market entry on its' primary market, using bundling as an entry barrier.⁷²

⁷² EAGCP report, p 39

2.4.5 Predatory pricing

Although not expressly mentioned in article 82, some practices have been considered falling under the article since they exploit consumers or have exclusionary effects. Of particular interest are predatory pricing, refusals to supply and abuse in linked markets.

Predatory pricing is when a dominant company on short notice drastically lowers its prices to force its competitors out of the market. Often the company raises the prices again when the competition has decreased and the benefits for consumers of the lower prices are therefore only of short-term character. Predatory pricing is often seen as a barrier to entry with market partitioning effects.

*AKZO*⁷³ is the leading case on predatory pricing. In this case, the Court held that it is not abusive for a dominant company to lower its prices to optimize the price and to achieve coverage margins. What is abusive, according to the Court, is to drop prices below average variable costs⁷⁴ since a dominant company has no interest other than to eliminate competitors through such behaviour.⁷⁵ If the prices are above average variable cost but below average total costs⁷⁶ the prices are regarded to form part of an abusive behaviour only if it can be shown that the practice aims at driving competitors from the market.⁷⁷

The reasoning of the Court in *AKZO* has been much criticised. This criticism will be closer described in the chapter on policy criticism.⁷⁸

2.4.6 Refusal to supply

When a dominant company stops to supply a long-standing customer, this can be considered to constitute an abuse. This was the case in *United Brands*⁷⁹. *United Brands* stopped supplying a Danish wholesaler of Chiquita bananas since it had taken part in an advertising campaign for competing banana brands. The Court found the refusal abusive since the long-standing customer relied on continued supply from the dominant firm and ceasing to supply was a too disproportionate measure from *United Brands* to protect its commercial interests.⁸⁰

⁷³ Case C-62/86 *AKZO v Commission* [1991] ECR I 3359

⁷⁴ Variable costs being those that vary according to the units produced and average variable costs being the sum of all variable costs divided by the number of units of output.

⁷⁵ Case C-62/86 *AKZO v Commission* [1991] ECR I 3359, para 71

⁷⁶ Average total costs are those resulting from adding the total fixed costs (the costs that do not vary with the quantities produced) by the number of units of output.

⁷⁷ Case C-62/86 *AKZO v Commission* [1991] ECR I 3359, para 72

⁷⁸ See Chapter 3.4.1

⁷⁹ Case 27/76 *United Brands v Commission* [1978] ECR 207

⁸⁰ *Ibid.*, paras 190-193

If the same practice would hit a casual customer, objective justification from the dominant company would probably be regarded to a greater extent by the Court, as indicated in the *Magill*⁸¹ cases.

In *Magill*, three television companies were found to have abused their dominant position because they had refused to provide Magill with copyright protected information on the programmes they would be showing. Magill wanted to produce a combined guide to all three channels. Such a guide was of course expected to be most attractive to consumers. The Court, who ultimately held that the behaviour aimed at exclude competition from the market of television guides, particularly, put forward three grounds on why the refusal was to be considered abusive. First, it considered that the dominant companies, through the refusal to provide the information for the television guide, were preventing the production of a product for which there was likely to be a consumer demand. The second ground was that there was no objective justification for the refusal. Thirdly, the Court considered that the three companies, who had statutory monopoly in Ireland and UK, were trying to extend their dominance over the secondary market of television guides.⁸²

The criticism on the *Magill* judgement raised questions on however the Court would apply the US doctrine of essential facilities in its coming decisions. According to this doctrine, a dominant company that owns a facility or infrastructure without access to which competitors cannot provide services to their customers, is abusing its position if it refuses access or makes access conditional in discriminatory terms, if there are no objective justification. Such an approach would narrow the duty to supply to such “essential facilities”. Advocate General Jacobs gave a number of reasons for why he considered this narrowed approach necessary in *Oscar Bronner*⁸³. The Advocate General was of the opinion that an obligation to supply reduces the incentives to make original investments in the facility and to duplicate it and therefore suggested that a duty to supply is only necessary when there is no competition downstream or when the company is very dominant.

The judgement in *Magill* has been criticised⁸⁴. The tension between intellectual property rights and provisions related to the free movement of goods is natural, since intellectual property rights include elements of territoriality. This tension is, however, a topic on its own and I will further on only discuss it in general terms relating to the criticism on the intervention in the commercial freedom of the dominant firms.

⁸¹ Cases C-241/91P *ITP, BBC and RTE v Commission* [1995] ECR I 797

⁸² *Ibid.*, paras 54-56

⁸³ Case C-7/97 *Oscar Bronner v Mediaprint* [1998] ECR I 7817, paras 57-58

⁸⁴ See Whish, Korah, *The Interface between Intellectual Property and Antitrust: The European Experience*, 69 *Antitrust L.J.* (2002) 801, p 801-804

2.4.7 Abuse in linked markets

In *Tetra Pak II*,⁸⁵ the Commission found Tetra Pak dominant in the market for aseptic cartons and equipment for filling these, but not in the market for cartons and equipment for pasteurised liquids. Although Tetra Pak was not considered dominant in the non-aseptic market, the Commission found it abusing a dominant position on it under article 82, since there were close links between the two markets. These close links included the fact that the key products packed in the two markets were the same and that, therefore, many of Tetra Paks customers operated in both markets. Another circumstance making the article applicable on the non-aseptic market was that the dominant company, because of its' super dominance, (90%), and technological lead on the aseptic market had the possibilities to carry out the abusive practises also in the non-aseptic.⁸⁶ It was, however, indicated that in the case of associated markets, the application of article 82 can only be justified by special circumstances⁸⁷ and it is therefore doubtful to which extent the concept of abuse in linked markets will be treated by the Court in the future.

⁸⁵ Case T-83/91 *Tetra Pak International v Commission* [1994] ECR II 755 and C- 333/94P [1996] ECR I 5951

⁸⁶ Case T-83/91 *Tetra Pak International v Commission* [1994] ECR II 755, paras 120-121

⁸⁷ C- 333/94P [1996] ECR I 5951, para 27

3 What needs to be reviewed?

3.1 General Criticism

One aspect of the criticism on the policy of article 82 so far is that it has been a lack of rule of reason approach in the application of the article. The Commission has defined such an approach as one “in which the authorities or courts, responsible for competition law, balance the pro-competitive aspects of an agreement against its anti-competitive aspects in deciding whether to prohibit it”⁸⁸. The definition was expressed in relation to the modernisation of article 81, and since then, many scholars have criticised that no measures have been taken to make the application of article 82 subject to similar review.

Another criticism often heard, is that the Court and Commission have not managed to distinguish competition on merits from abusive behaviour, although they have mentioned several times that a dominant company also has to be able to compete on efficiency.⁸⁹

It is a fact that the Court has protected small and medium sized firms on the behalf of dominant companies, without regard to efficiency arguments.⁹⁰

It has been advocated that the Commission shall apply an effects-based, “economic approach” instead of the strictly form-based approach, which is now significant for the method under article 82. Under “economic approach” is to be understood an approach not bound to the forms of specific business behaviour such as “tying” or “exclusive dealing agreements”, but focused on the pure effects of the behaviour of the undertakings concerned. Potential negative effects are then to be weighed against possible efficiency gains in each case and will thus lead to use of “the rule of reason” instead of mere application of per se rules. To avoid a too far-going intervention and “fine-tuning” in each case, such an approach could be based on the examination of the established notion of barriers to entry.

The focus on consumer welfare leads to avoidance of protection of competition being confused with the protection of competitors. Competition is considered a process that forces firms to be responsive to the preferences of consumers in respect of for example quality and price. Such a process will promote effectiveness and is therefore necessary for the creation of a strong and consumer-orientated European market.⁹¹

⁸⁸ See *White Paper on Modernisation of the Rules Implementing Articles 85 (now 81) and 86 (now 82)* OJ [1999] C 132/1, under footnote 46

⁸⁹ See Whish, p 695 and Korah, p 390

⁹⁰ Korah, p 390

⁹¹ EAGCP report, p 3

A large part of the criticism on article 82 policy is of economic character, which is not really surprisingly since competition law and economics are very closely connected and dependent upon each other.

3.2 Criticism on the procedure of defining the relevant market

Defining the relevant market has, due to the formalistic two-step approach mentioned above, been crucial to the application of the law of abuse.

A specific criticism on the approach of the Commission in deciding the relevant market, regards the use of the SSNIP test⁹². It is argued that the SSNIP test may be used in merger cases, where the question is what will happen in the future, after the transaction, but that it is not suitable to use it in cases concerning abuse of a dominant position.

When it comes to defining dominance, it has to be taken into consideration that the undertaking in question might already charge a monopoly price and that a raised price might lead to consumers ceasing to buy from it at all. In such a case, the SSNIP test will show that consumers will be switching from the undertakings' products to a great extent and therefore a high degree of substitutability will be suggested, resulting in an exaggerated breadth of the market.⁹³ Another problem with the use of the SSNIP test is that price-data about substitutability might not always be available. This leads to subjective assessments of the market and urges the need for looking at the actual effects on customers of the application of the SSNIP test, regarding factors such as physical characteristics or intended use of the products in question. A third remark is that when the market strength has to be decided for an undertaking regarding products that are not yet launched, the SSNIP test cannot be used at all, since there are no data available.⁹⁴

The CFI has further on declared that the market must always be defined in each particular case, regarding the circumstances at the time and not by reference to preceding decisions.⁹⁵ This –how necessary it might be, leads to great uncertainty about the legal situation and makes it hard for undertakings to predict their market position.

Another factor of great importance for the effects of article 82 is that the definition of the relevant market, due to the information problems naturally inherent, more or less has been arbitrary. Therefore, it has been suggested that the definition of the market shall not, necessarily, determine whether a

⁹² See explanation on the test in chapter 2.3.1

⁹³ Whish, p 31-32

⁹⁴ Ibid., p 36

⁹⁵ See for example Case 125/97 *Coca-cola v Commission* [2000] ECR II 1733

firm has market power, but serve as an indicator on the factors relevant.⁹⁶ Such a new method –leaving the two-step approach, is suggested in the EAGCP Report, which I will discuss in more detail in chapter 4.

Conclusively, it can be said that the uncertainty inherent in the approach of the Commission and Court when defining the relevant market has raised the question whether it is really necessary, formally, to define the market separately or if a case to case analysis of the overall effects on competition might serve the objectives of competition law to a greater extent.⁹⁷ It has been argued that the exact definition is not of such great importance, if the competitive pressures on the firm, both from within the thought relevant market and from outside, are given considerable weight in the analysis.⁹⁸ An analysis based on the inquiry into the barriers to entry might be a method to attain a more effects-focused application of the law of abuse.

3.3 Criticism on the findings of dominance

There are obvious shortcomings inherent in the market share approach. As described above, market shares are not indicative on the definition of the relevant market when there is high substitutability in consumption – the producing undertakings can enjoy market power although there are product substitutes.⁹⁹ In the case of collusion, small market shares can be consistent with market power, when many small actors control the market.¹⁰⁰ Furthermore, large market shares do not necessarily equal market power. An example on this is a situation where there are few barriers to entry and potential entry would significantly reduce the market share of the incumbent undertaking.¹⁰¹

Economists with the primary interest of protecting consumers, say that even very high market shares do not indicate a dominant position in the absence of entry barriers. The efficient production in such cases only leads to exclusion of less efficient firms.¹⁰²

The imperfectness of market shares as tool for the assessment of dominance is particularly clear on bidding markets with strong buyers. Additional factors such as the strength of the buyers and barriers to entry should thus be properly analysed.¹⁰³

⁹⁶ Korah, p 95

⁹⁷ Ibid., p 95

⁹⁸ Ibid., p 117

⁹⁹ Whish, p 31-32

¹⁰⁰ Bilal & Ollarega, p 7

¹⁰¹ Ibid., p 7

¹⁰² Korah, p 109

¹⁰³ Geradin, Hofer (...), GCLC, p 16

Another remark on the definition of dominance as expressed in *United Brands*¹⁰⁴ is that an undertaking cannot, regardless if it is dominant or not, behave very independently since every firm is restricted by its demand curve. All firms will increase prices, until the point where further price increase is unprofitable is reached. In one sense, however, a dominant undertaking can act independently of its competitors; it can for some time raise prices above the competitive level. If there were not inherent problems in calculating the competitive price, it would be enough, for the objectives of competition law, to require from all market participants to price over the competitive level and a finding of dominance would be unnecessary.¹⁰⁵

3.4 Criticism on the findings of abuse

The notion of abusive behaviour, as defined in the case law, contains a number of weak elements, which have given rise to legal uncertainty.¹⁰⁶ In *Hoffman La-Roche*¹⁰⁷, the Court used the term “normal competition”, but did not explain the notion any further. Efficiency enhancing conduct by a dominant firm, which is also, and without objection, carried out by a non-dominant firm might not be considered as “normal”. A policy, which is common within an industry, does not necessarily constitute “normal competition”.¹⁰⁸

“Competition on the merits”, has also been used as expression for a benchmark¹⁰⁹ and has been defined as “*competition on the basis of price, quality and functionality of the product*”¹¹⁰. However, predatory pricing, loyalty rebates and tying are examples on such competition –but they are not always allowed.

Another vague term, often referred to, is “special responsibility”¹¹¹. This notion has not been explained any further and it is unclear what types of conduct will be looked upon as abusive when carried out of a dominant firm.

¹⁰⁴ See Note 21

¹⁰⁵ Geradin, Hofer (...), GCLC, p 7-8

¹⁰⁶ Temple Lang & O’Donoghue, GCLC, p 41-42

¹⁰⁷ Case 85/76 *Hoffman La Roche v Commission* [1979] ECR 461, para 91

¹⁰⁸ Commission Decision of March 21, 2004 *Microsoft*, footnote 877 and Case 322/81 *Michelin v Commission* [1983] ECR 3461, para 57

¹⁰⁹ Case T-203/01 *Michelin II* [2002] 5 CMLR 388, para 107

¹¹⁰ See Comments by Mario Monti to the speech given by Hew Pate, Assistant Attorney General at the US Department of Justice, at the conference “Antitrust in a transatlantic context”, in Brussels June 7th, 2004,

http://europa.eu.int/comm/competition/speeches/text/sp2004_005_en.pdf

¹¹¹ Case T-191/98 *Atlantic Container Lines* [2003], para 1460

Further difficulties arise when the practice is considered to be abusive in some cases but not in others, which have been the case in the case law so far.¹¹²

¹¹² Temple Lang & O'Donoghue, GCLC, p 42

3.4.1 Predatory prices

The difficulties with condemning predatory prices are also more or less obvious. Lower prices are a clear benefit to consumers –and consumers are the ones who shall be protected by competition law. As mentioned above there is of course a risk that the dominant company, after it has lowered its prices and forced competitors off the market, will raise its prices to a non-competitive level –which then no longer is an acceptable outcome for customers.

If low prices, however, inherit the risks of being treated as abusive there would be serious disincentives for dominant firms to engage in price competition.¹¹³ Such an outcome cannot possibly be the intention of the competition authorities.

Although the intent of the undertaking concerned is of no importance when defining abuse (as described above it is enough that the dominant firms' conduct may result in distorting competition on the Common Market)¹¹⁴, the Court has stated that pricing under average variable cost is to be seen as abuse since the dominant firm cannot have any other objectives with such conduct than to force competitors off the market.¹¹⁵ There are a number of non-predatory reasons for a company to, at times, charge below average variable cost. Introductory offers, technical products that are out of date and are to be replaced by newer, targeting new customer segments or pricing in the downturn of the business cycle in cyclical industries are some imaginable reasons.¹¹⁶

If the dominant firm had as its objectives to eliminate competition it would be necessary for it to prevent re-entry of the firms hurt by the predatory pricing. Otherwise, these firms, or new market entrants, would try to “fill the gap” and enter the market once the dominant firms have raised its prices and the dominant firm would not be able to recoup the losses made during the price-cutting phase. The dominant firm is therefore dependent on a certain level of entry barriers if it has the intent to eliminate competition.¹¹⁷

It can be harmful to consumers to merely scrutinize whether or not the prices set by a firm with a large market share are below average variable cost or not, since the objective of driving out competitors is a natural part of competition. The question is however this is done by “fair” means and as a result of efficiency or if the dominant company uses its' dominant position to for example create entry barriers making it impossible for other firms to compete.

¹¹³ Korah, p 158

¹¹⁴ See chapter 2.2 and the wording of article 82 ECT

¹¹⁵ Case C-62/86 *AKZO v Commission* [1991] ECR I 3359, para 71

¹¹⁶ Turnbull, p 99

¹¹⁷ *Ibid.*, p 98

3.4.2 Rebates

A special aspect to the criticism is that there has been a tendency to protect certain competitors instead of consumers by not distinguishing what conduct amounts to exclusive behaviour and what is merely competition on merits.¹¹⁸

In *Michelin* and *Hoffman-La Roche*,¹¹⁹ the Court stated that distinction shall be made between traders' performance and abusive conduct. In other words, competition on merits shall not be prohibited under article 82. Dominant firms must be able to compete and to protect their commercial interests, but this must be done in an economically efficient way that is consistent with the interests of consumers, according to the CFI.¹²⁰ In the same case¹²¹, however, the Court has been understood as to suggest a *per se* standard for the scrutiny of rebates – which has been considered particularly unsuitable since rebates and similar pricing practices are normal part of business life and in fact can contribute to competition.¹²²

If rebates are not based on quantity and justified by cost-savings (such as less transport costs), they are likely to be considered as abusive if given by a dominant company.¹²³

What makes rebates granted by a dominant firm dangerous for competition is, as described above under 2.2.3, is that they raise switching costs for the customer and inherit the risk of foreclosure vertically and horizontally. Particularly loyalty rebates have been looked upon with great care, since such rebates have been considered to have the same effects as exclusive purchasing agreements, namely to tie the customer to the firm.¹²⁴

It has been held that in an oligopolistic market structure, secret rebates are the only means of price competition.¹²⁵ Besides that, there are a number of reasons for a company to grant rebates. The most obvious one is to gain customers from competitors, which ought to be considered as normal competitive behaviour. A close connected reason is then to keep the customers. Granting selective rebates to gain or keep customers has clear benefits for those customers and constitutes a form of price competition, which is likely to be of favour also to the consumers.¹²⁶

¹¹⁸ Korah, para 14.1.5

¹¹⁹ Case 322/81 *Michelin v Commission* [1983] ECR 3461 para 70 and Case 85/76 *Hoffman La Roche v Commission* [1979] ECR 461 para 91

¹²⁰ Case C 497/99R *Irish Sugar v Commission* [2001] ECR I 5332 paras 189 and 112

¹²¹ Case 85/76 *Hoffman La Roche v Commission* [1979] ECR 461, para 89

¹²² Whish, p 695

¹²³ See Cases 85/76 *Hoffman La Roche v Commission* [1979] ECR 461, Case 322/81 *Michelin v Commission* [1983] ECR 3461

¹²⁴ Case 85/76 *Hoffman La Roche v Commission* [1979] ECR 461 para 89

¹²⁵ Turnbull, p 99

¹²⁶ EAGCP report, p 36

Some forms of rebates, such as target rebates for retailers can have the function as to encourage the distributors to improve their performance or promote the product and in that sense improve competition rather than to hinder it.¹²⁷

Another reason for any firm to grant rebates is, however, to be able to plan its orders and thus reach increased efficiency.¹²⁸

Unfortunately, it is hard for a firm to demonstrate that efficiency considerations motivate the rebate system. So far, the Commission and Court have, in some cases, accepted rebates based on quantity but no fidelity rebates. It seems as quantity rebates thus are easier to motivate on efficiency grounds.¹²⁹

It has been argued that a dominant firm must have some possibilities to develop and apply its pricing practices, just as any other firm.¹³⁰ If the approach from the Commission and Court makes it hard for firms with large market shares to compete on merits, this will lead to in-efficiency, which in terms will lead to bad resource allocation and higher costs.¹³¹

The inconsistent case law so far is unfortunately making it very hard for a firm with large market share to predict the consequences of its pricing practices.

3.4.3 Tying and bundling

There are reasons for tying or bundling products other than excluding competitors from second markets. Efficiency is once again one of the main arguments. Quality and safety has been put forward as grounds, but with limited success so far¹³², avoidance of price regulation and secret discounting are other possible reasons. As mentioned above, secret discounting can be the only possibility for a company in an oligopolistic market structure to compete.

From the consumers' point of view, bundling can bring clear benefits such as lower costs -if the products otherwise were to be bought separately and better compatibility -in the case of technically integrated products. Bundling products can also reduce information problems, for example when the quality of each one of the products, looked upon separately, is uncertain.¹³³

¹²⁷ Turnbull, p 100

¹²⁸ Ibid., p 100

¹²⁹ EAGCP report, p 36-37

¹³⁰ Whish, p 695

¹³¹ Turnbull, p 100

¹³² Case T-30/89 *Hilti v Commission* [1991] ECR II 1439

¹³³ EAGCP report, p 40

Through so-called meter usage, the firm has the possibility to assure that it is paid the right royalty for a machine, which it licenses.¹³⁴ This can for example be done by selling photocopiers together with the paper or with the service on the machines. The consumer of the latter then shows the demand for the former, which enables the company to adjust to the demand more flexibly.¹³⁵

Tying leads to a system-based competition, which is likely to be more intense than a component-based. Depending on the market structure, the cost savings that are connected with the bundling and the possible strategic reasons tying can have both pro- and anti-competitive effects and the cases on tying are therefore particularly suitable to effects-based scrutiny.¹³⁶

¹³⁴ Turnbull, p 99

¹³⁵ EAGCP report, p 40

¹³⁶ Ibid., p 41

4 A new approach

4.1 Barriers to entry and their relevance to article 82 EC Treaty

Since some time it has been advocated that the Commission and Court shall leave the strict form-based approach of defining the dominant position and abusive behaviour separately and focus more on the actual effects of the conduct of stronger firms on the market. An alternative view on the market structure is offered through the focus on barriers to entry and barriers to expansion.

If there were no entry barriers, a monopolist earning monopoly profits would attract new entrants to the market and thereby, through the exploitative behaviour, increase competition.¹³⁷

Even if a firm has a high market share, the possible dominance on the relevant market is dependent on how easy it is for other firms to enter that market. The assessment of dominant position must therefore include –if not be based on, an analysis on the barriers to entry onto the market in question.

There are two views on the idea of barriers to entry. The idea can either be considered broadly, embracing more or less everything that can prevent a firm to enter the market. This view tends to increase the risk for a firm to be considered dominant. The other idea of barriers to entry is more focused upon separating competition on merits from artificial barriers, constructed to prevent market entry and thus making a difference between entry-barriers that are indicative to the efficiency of the firm and those constituting abuse.¹³⁸ This idea is the one advocated in the EAGCP Report.

One model to define entry barriers is to categorize them into four different forms.¹³⁹

Legal or administrative barriers constitute one of these forms. Included are for example exclusive rights by law to operate within a certain market, for example national monopolies. Another very important legal barrier to entry is the possession of intellectual property rights, since such possession completely excludes, for a period of time, the competitors from activity covered by the exclusive right.

Next category of barriers to entry are the costs a new market entrant has to bear to enter the market and which cannot be recovered if entry fails. This barrier is referred to as sunk cost of entry. Very large costs to enter the

¹³⁷ Whish, p 194

¹³⁸ Craig & de Burca, p 1003

¹³⁹ Faull & Nikpay, paras 3.50-3.72

market are for example the setting up of commercial networks, advertising campaigns and investments in production facilities such as plants. Sunk costs of entry are barriers to entry, not only because they in themselves are financial risks to the market entrant, but also because the fixed ones lead to so called “economies of scale”. For example, great investments in research and development have to be made in markets where innovation plays an important role. Such costs are sunk since it is impossible to know if the market entrance is going to be successful or not. In determining dominance, the Court has referred to technological lead as constituting a barrier and thus indicating dominance. This since competitors could not develop research at a comparable level and therefore were in disadvantage.¹⁴⁰ Sales and service networks, so-called vertical integration and the sunk costs arising from it have also been considered factors contributing to dominance, as mentioned above.¹⁴¹ To be referred to sunk costs are also barriers constituted by a strong trademark. Several decisions on mergers have referred to this factor.¹⁴²

Economic barriers to entry are also the switching costs for consumers. A new market entrant would have to support such costs in order to break in to the market, while already established will not have to do so. An example on such costs is when the customer will have to train staff in order to use the products provided from the new entrant or change logistics to be able to be supplied.¹⁴³

The last of these four forms is the strategic behaviour. This type of entry barriers are created or strengthened by an undertaking in order to make it more difficult for new firms to enter the market. Examples on such behaviour are threats on price war, to expand output, loyalty bonuses or to make excessive investments. The ability to, on short notice, expand output as response to raised output from competitors can, on the other hand, be seen as a counterweight to a large market share when determining dominance. This since the ability to compete is then increased.¹⁴⁴

This method of defining entry barriers is, of course, to refer to the broad interpretation of the concept since it covers all possible barriers to market entry and not only the barriers deliberately constructed to prevent it. My point of view is that a separation of these views is of high importance to, in the first place, understand the concept of barriers to entry and secondly to be able to use this concept in accordance with the objectives of article 82 when assessing market power.

¹⁴⁰ Case 27/76 *United Brands v Commission* [1978] ECR 207

¹⁴¹ See Case 27/76 *United Brands v Commission* [1978] ECR 207, paras 70-81

¹⁴² Faull & Nikpay, para 3.63

¹⁴³ Decision 88/501 of the Commission *Tetra Pak I* [1988] OJ L 272, para 37

¹⁴⁴ Faull & Nikpay, para 3.67

If the same concept were to be defined in accordance with the somewhat narrower view, barriers of entry should be placed in two different categories, natural and artificial barriers.¹⁴⁵

The first category refers to those barriers that naturally exist when a firm is established on the market. Skill, knowledge, equipment and reputation are factors that, of course, will make market entry for other firms harder. However, there should, according to this view, be no objections to such barriers when they are the result of efficiency. Only when they are not, when they are so called artificial barriers, law has a role to play to keep the possibilities for market entry open. Artificial barriers are, consequently, those that are not results of efficiency but have been created by the incumbent to prevent entry or growth of smaller firms. Such barriers are therefore always a form of exclusionary practice and are the ones to be prevented by competition law.

It is of great importance to distinguish between barriers that are results of pure efficiency and artificial barriers, or “the law will find itself – indeed, it has found itself –attacking efficiency in the name of market freedom”, as Richard Bork has expressed it.¹⁴⁶

There seems to be much confusion on how to use entry barriers analysis within the frames of article 82. If all entry barriers that could, potentially, harm firms competing with the dominant firm were to be taken into consideration, the analysis that had to be made would be very extensive and complicated. As highlighted above some entry barriers can also serve as pro-competitive factors.¹⁴⁷

If the objective with article 82 can be said to be the protection from exploitation or exclusion of firms dealing with the dominant firm, then it will only be necessary to protect those undertakings that are equally efficient. To do this, focus must stay on those entry barriers that prevent market entry or otherwise harm firms equally efficient to the dominant firm.¹⁴⁸

In the process of establishing market dominance, it has been suggested that the ability to reduce output substantially in the market, is a more useful indicator than, for instance, assessment of power over price. The reason for this is that if an undertaking alone has the power to, significantly, restrict the entire output of the market, this indicates that other firms are unable to fill the gap, which points at barriers to both expansion and entry.¹⁴⁹ Expressed the other way around; analysis of barriers to entry and expansion would be a very useful, if not necessary, tool for the assessment of dominance.

¹⁴⁵ Bork, p 310-311

¹⁴⁶ Ibid., p 311

¹⁴⁷ See definition on entry barriers

¹⁴⁸ Korah, para 4.2

¹⁴⁹ Geradine, Hofer, (...), GCLC, p 10

4.2 The EAGCP Report and the Commission Discussion Paper

The Economic Advisory Group for Competition Policy (EAGCP) is a group of economists with the main purpose of supporting the DG Competition in the economic reasoning on competition policy analysis. The members of the group are nominated by the Commissioner for competition, on proposal by the Chief Economist and it is divided into three sub-groups to work on issues on antitrust, mergers and State-aid. The Report on “An economic approach to article 82” has been commissioned by the Chief Economist of the DG Competition and was published in July 2005. It contains a detailed analysis on the pros and contras of the approach of the Commission so far, as well as practical examples on a new approach to the application of article 82.¹⁵⁰

The “DG Competition Discussion Paper on the application of article 82 of the Treaty to exclusionary abuses”, was published on December 19th 2005, and is supposed to lead to reflection on the precise form of the guidance, provided through potential future Guidelines.¹⁵¹ The document will be open to public consultation until March 31st 2006.

In this chapter, I will highlight the main ideas of the Report and the Discussion Paper and analyse the examples on new approach given to some specific forms of conduct.

4.2.1 The Relevant Market

In its Discussion Paper, the Commission defends and explains its position regarding the definition of the relevant market. The objective of defining the geographical- and the product market, is the necessity of structurally identifying actual competitors that are capable of constituting competitive constraints on the undertaking concerned. The Commission Notice on the definition of the relevant market for the purposes of Community Competition law¹⁵² will serve as basis for the market definition.¹⁵³

Regarding the SSNIP test, the Commission recognises that there is a risk for the market to be too widely defined and that it is necessary to rely on more than a single method for defining the relevant market. Such an additional

¹⁵⁰ Note on the EAGCP report, available at http://europa.eu.int/comm/competition/publications/studies/note_eagcp_july_05.pdf (last visited 2006-02-03)

¹⁵¹ See Neelie Kroes comment at <http://www.eu.int/rapid/pressReleasesAction.do?reference=MEMO/05/486&format=HTML&aged=0&language=EN&guiLanguage=en> (last visited 2006-01-05)

¹⁵² OJ C 372 09.12.1997, p 5

¹⁵³ Discussion Paper, para 12

method might be to examine the product characteristics and intended use and to assess whether they can satisfy an inelastic consumer need. If the products are only to a small extent interchangeable, they will not be subject to constraints in the form of competitive prices. It is decisive if a sufficiently large number of consumers find the products substitutable for them to form part of the same market. If a single supplier would be able to sell the product to a higher price to consumers with less elastic demand and preventing consumers with more elastic demand from reselling to these consumers, the consumers with less elastic demand might form a market of their own. Another method of relevance to the Commission when defining the relevant geographical- as well as product market is to compare prices charged in different regions. If an undertaking charges higher prices in regions where it has a higher share of sales, this could be a sign on that the main competitive constraints come from other suppliers of that particular type of product and not from other types of the product.¹⁵⁴

4.2.2 Dominance

The Discussion Paper defines a dominant position as consisting of three elements:¹⁵⁵

- there must be a position of economic strength on a market
- this strong position enables the undertaking to prevent effective competition being maintained
- the undertaking has the power to behave independently to an appreciable extent

Thereby, the Commission emphasizes that a dominant position can only exist in relation to a market, and not in the abstract. The two other elements, both concern the relation between market strength and the competitive process. An undertaking in a dominant position is, according to the Commission, not subject to effective competitive constraints for a significant period of time.¹⁵⁶ Higher than normal profits and the way the undertaking acts on the market can serve as indicators on lack of competitive constraints.¹⁵⁷

When defining dominance, the first step to take is that of defining the relevant market. Thereafter the ability to behave independently must be assessed. Factors of relevance in this assessment are the market position of the undertaking concerned and that of its competitors, barriers to expansion and entry and the market position of buyers.¹⁵⁸

¹⁵⁴ Discussion Paper, paras 18-19

¹⁵⁵ Ibid., para 21

¹⁵⁶ Ibid., paras 21-22

¹⁵⁷ Ibid., para 26

¹⁵⁸ Ibid., para 28

The analysis of the market position of the undertaking and of its competitors, as before takes its' begin in the calculation of market shares.¹⁵⁹

Next step in the assessment of dominance, as proposed in the Discussion Paper, is an analysis of the barriers to entry. The Commission has clearly acknowledged the criticism and presents an approach that to great extent considers barriers to entry and expansion. The Commission will also consider potential entry when assessing the independence of the allegedly dominant firm. Such entry must be sufficient immediate and persistent to prevent the exercise of substantial market power and the time period needed for undertakings already established on the market to adjust their capacity, can serve as a yardstick. The history of entry and expansion of the industry and the question in how far suppliers in other markets already possess production facilities necessary to enter the market in question, as well as the likely evolution of the market are also factors that will be taken into consideration by the Commission.¹⁶⁰

The market power of buyers is an indicator on in how far they can put constrains on the allegedly dominant undertaking and must therefore also be taken into account. In cases where several strong buyers might be able to get better conditions than others when dealing with the strong undertaking, these buyers may form a market of their own.¹⁶¹

In the EAGCP Report, the authors advocate that a separate assessment of dominance is not necessary. The focus shall stay on the competitive harm since such an effect in itself is considered to be sufficient proof of dominance. Such an approach would have effects also on the burden of proof. It is suggested that the Competition Authorities then solely will have to present proof on significant competitive harm and the undertaking in question will have to provide credible efficiency arguments.¹⁶²

4.2.3 Abusive behaviour

The EAGCP Report presents a detailed analysis of the approach on abusive behaviour, which is not to find in the Discussion Paper. I have therefore chosen, in this part, to use the EAGCP analysis as a base.

Of particular importance for the effects-based approach advocated in the Report, is the existence of open competition. The role of the competition authorities shall not be to replace competition by intervention, but to prevent certain development and to prohibit some kinds of conduct without actively telling the market participants where they shall be going.¹⁶³ Natural focus

¹⁵⁹ See above, chapter 2.3.2 and criticism in chapter 3.3

¹⁶⁰ Discussion Paper, paras 35-39

¹⁶¹ Ibid., paras 41-42

¹⁶² EAGCP Report, p 4

¹⁶³ Ibid., p 10

therefore lies on exclusionary behaviour and on the impact of competition law on barriers to entry.

The EAGCP Report distinguishes between three forms of exclusionary behaviour: exclusion within the same market, where the incumbent tries to prevent entry or to force the competitor to exit the market, exclusion in an adjacent market, where the firm is excluding competitors on a secondary market horizontally related to the main market and exclusion in a vertically related market, on different production stages. Given that the same type of exclusion can be implemented through different practices, this classification is intended to help keeping a consistent approach.¹⁶⁴

Identifying the nature and scene of the competitive harm in accordance with the classification in the Report is meant to make the investigation process in antitrust cases faster and to increase the legal predictability through the more consistent treatment of the different practices with similar anti-competitive effects.¹⁶⁵

With exclusion is meant a conduct that seeks to force the competitor to exit the market, to hinder the competitor to entry the market or to force the competitor to act in such a passive way that it does not compete.¹⁶⁶

The first form of exclusion, within the same market, inherits an initial, aggressive period where the incumbent tries to reduce profitability of the competitor through for example predatory pricing, tying, targeted rebates or any of the other kinds of behaviour described above in chapters 2.2 and 4.1. The initial phase thus often leads to losses for the incumbent and benefits for the consumers. In the long term, however, the exclusion brings worse conditions for the consumers since competition has been reduced, as explained in the above chapters.

Whether the exclusionary strategy is profitable or not is dependent on if the incumbent succeeds in forcing competitors out of the market and preventing new entry during the catch-up phase following the initial period of actual exclusion. The Report therefore recognises that the scene on the market and the evidence on the exclusionary behaviour can look very differently depending on when the antitrust case is opened.¹⁶⁷

The fact that many of the types of behaviour with the potential to have exclusionary effects are merely normal competitive reactions is also highlighted in the Report. Thus, every case must be individually investigated in accordance with the rule of reason, comparing possible pro-competitive effects and alternative explanations to the alleged abusive behaviour.

¹⁶⁴ EAGCP report, p 17

¹⁶⁵ Ibid., p 29

¹⁶⁶ Ibid., p 18

¹⁶⁷ Ibid., p 18-20

The concrete approach suggested in the Report pre-supposes a set of example questions to be answered.

Does the competitor rely on external funding and do the financial conditions depend on the performance of the borrower? Does the aggressive conduct of the incumbent reduce the possibilities for the competitor to obtain external finance? Does the incumbent have alternative sources of internal financing, for example from other lines of business and is the impact of the reduced cash flow during the initial phase thus limited? Is the incumbent able to recoup the losses once exclusion is realized or would future entry constitute a too big threat?¹⁶⁸

Exclusion in adjacent markets can be achieved through for example tying, bundling, rebates, refusal of access to interfaces or technical integration. Also in these cases, the policy of the incumbent can be beneficial to the consumers at the same time as it has exclusionary effects. Exclusionary conduct would be the case when the incumbent is making entry to its' primary market harder through its actions in the secondary or when the incumbent uses its' market power from the primary market to exclude competitors from the secondary one.

To distinguish exclusionary behaviour from sound profit-maximising strategy, it is necessary to look at factors as the relationship between the products being bundled, the costs of entry and the irreversibility of the bundling.¹⁶⁹

Vertically related markets are markets to which the dominant firm controls the input production or service. Exclusion takes place when the activity of firms up- or downstream is hindered by the dominant company through for example refusals to deal or limiting access to its' resources, partly or completely. Other possibilities for the dominant firm to foreclose is through making its' products incompatible with the products of the competitors, engage in bundling or to favour some customers/competitors through loyalty rebates or substantial quantity discounts to allow the survival of only a few competitors.¹⁷⁰

According to the Chicago-criticism, the dominant firm might, however, lack incentive to foreclose the vertical markets. This since disturbance of competition in these markets might reduce the profitability of the own product or service. The firm would rather let other firms be active on the vertical markets to take advantage of increased demand on its' primary products. A possible incentive to deter competition in a vertically related market does, on the other hand, exist when the dominant firm wants to protect its' primary market, as is the case with exclusion in adjacent markets.¹⁷¹

¹⁶⁸ EAGCP report, p 22-23

¹⁶⁹ Ibid., p 23-26

¹⁷⁰ Ibid., p 26

¹⁷¹ Ibid., p 27-28

The intervention of competition authorities in cases of vertical exclusion will increase competition in the related markets and benefit consumers both in the short- and long-time run. In the short run, prices will be lower through the increase of competition and in the end, the diversity of inventions will be increased since more actors will be able to act on the markets. Another possible long run effect is, however, that the dominant firm loses its' incentive to innovate. A prospective licensee would not be prepared to pay much for the use of a new technology if he knows that the licensor will equip the market with a number of similar licensees. Such a situation would have as potential effect as to impede development in key infrastructures.¹⁷²

4.3 Examples on a new approach

The EAGCP Report contains practical examples on the use of the new approach through applications on some of the conduct currently being treated as abusive behaviour. The examples concern price discrimination, rebates, tying and bundling, refusal to deal, exclusive dealing and predatory pricing.

In the Discussion Paper, a more general policy discussion is held in combination with very practical examples on application. Where the EAGCP Report considers the whole market situation, the Discussion Paper builds, to a great extent, on the procedure and method that has been used so far and how this might have to be modified to be in conformity with the reformed policy o the application of article 82.

Below, I will briefly compare the solutions suggested in the Report with the ones suggested in the Discussion Paper.

4.3.1 Predatory prices

4.3.1.1 EAGCP Report

There are difficulties with the approach on predatory pricing. The challenged behaviour of the dominant firm is that of the predatory price-cutting phase, when a strong incumbent is dramatically lowering its' prices to weaken or eliminate competition. At the same time, however, the overall objective of the antitrust regulations is to promote lower prices. The problematic thus lies in the ability of the competition authorities to separate prices that are low for predatory reasons and those forming normal price competition.

¹⁷² EAGCP report, p 28

The Report considers the case of signal jamming as an example for the new approach. A firm considers entering a market where there is high uncertainty on profitability. To avoid a high-risk entry, the firm decides to enter a test market limited in for example geographical means, to gain information on the profitability. The incumbent prevents the entering firm to learn about the demand under normal competitive conditions on the market through lowering its' prices on the test market. The prices charged by the incumbent on the test market differ from the prices on the markets where the incumbent does not face new competition.¹⁷³

The harm on competition is that the potential entrant will delay entry or completely refrain from entry due to the inability to estimate demand.

To prove test market predation, the competition authorities must consider the following aspects in each case:

- The catch-up ability of the predator must be carefully assessed
- Are there alternative channels for market information that are not significantly more expensive or less accurate? If there are not, the conduct of the incumbent can constitute a strategic entry barrier that is harmful to competition since it prevents entry or forces exit. Otherwise, the incumbent would not be able to recoup and the competitive harm would not be consistent.
- The competition authorities should be able to prove a well-defined predation strategy of the incumbent. The nature of the concern must thus be identified. The present cost-price calculation of the incumbent is an uncertain indicator of predation. Key factors are instead the need of the entrant to attain market information and to attract outside investors.¹⁷⁴

4.3.1.2 Discussion Paper

In the Discussion Paper, it is recognised that the pricing is not predatory solely because the lower prices incur losses in the short run.¹⁷⁵ Predatory pricing, in its terms, is exclusionary when it serves as a tool for strengthening the dominant market position of the predator and thereby allows the predator to obtain higher prices after the price-cutting phase.¹⁷⁶ A dominant company is considered, under normal market conditions, not to be forced to lower its prices below average total costs. The large market share already held in combination with entry barriers are factors that should enable the undertaking to apply a pricing that will not lead to losses being made. If thus the reaction to new entry or increased competition is to drop

¹⁷³ EAGCP report, p 51-52

¹⁷⁴ Ibid., p 52-53

¹⁷⁵ Discussion Paper, para 95

¹⁷⁶ Ibid., para 97

prices and make losses, the Commission finds itself to have good reasons for intervention.¹⁷⁷

The Discussion Paper builds in its practical exemplification –in contrary to the EAGCP Report, still on cost-price calculations.

The Commission might continue using information on the cost structure of the dominant company. When such information is not available, a use of information on the costs of apparently efficient competitors can come into question. In the latter case, the dominant firm will have the opportunity to show that it is in fact not charging under its own costs. Regard must be taken to the period of time in which the dominant firm charges below cost.¹⁷⁸

An example is when a dominant company charges below average avoidable cost, which is the case when it charges prices on its output, not covering the costs and if these costs could have been avoided by not producing the output. In the short run, the company is then not minimizing its losses. This would be sufficient for the Commission to *presume* that the target of the sacrifice then made by the undertaking is to exclude competitors and no further justification through facts – such as those mentioned in the EAGCP Report¹⁷⁹, will have to be made.¹⁸⁰ The possibility remains, as before¹⁸¹, for the dominant company to justify the pricing.

In cases where the dominant undertaking charges prices above average avoidable cost but under average total cost¹⁸², other factors must, however, be taken into consideration as proof on predatory intent. Direct evidence on such intent is for instant documents from the dominant company showing a detailed plan on how predatory prices shall be used to exclude competitors or prevent entry. Of relevance as indirect evidence on predation is however the pricing policy make commercial sense in other ways as part of a predation strategy, or not. Other factors to look at are the scale, the duration and continuity of the low pricing, are certain customers selectively targeted, does the undertaking have the possibility to recoup losses in the foreseeable future, in how far there are effects in linked markets, if the prey is dependent on external financing and if it has counter strategies. It must be shown that foreclosure is, at the very least, likely to occur.¹⁸³

The case of “signal jamming” as I have described above in relation to the example of the EAGCP Report, is also recognised in the Discussion Paper. Of relevance is here whether the pricing strategy is limited to one market or to a period of time. It can make sense to a predating company to “invest” in a reputation as a rough competitor. Such a pursuance of reputation would

¹⁷⁷ Discussion Paper para 102

¹⁷⁸ Ibid., paras 103-105

¹⁷⁹ See above under note 139

¹⁸⁰ Discussion Paper, paras 108-110

¹⁸¹ See Case C-62/86 *AKZO v Commission* [1991] ECR I 3359, para

¹⁸² See notes 62 and 64 for definition of average total cost

¹⁸³ Discussion Paper, paras 115-117

serve as indirect evidence on a predation strategy in the case of multiple markets or periods hit by the strategy.¹⁸⁴

As regards the possibility for the undertaking to recoup the losses made during the price-cutting phase, the Commission does not find it necessary to provide other separate proof than that of the existence of entry barriers. The Commission argues in the Discussion Paper that a predating company will not have to increase its prices to a level higher than before the price-cutting phase in order to recoup its losses –it is enough that the predation prevents or delays the lower prices, which would be the result of undistorted competition. Further, the facts that the company is dominant and the existence of entry barriers are considered sufficient proof of the likeliness of the ability to recoup the losses.¹⁸⁵

If the pricing is above average total cost, it is in most cases only excluding less efficient competitors and shall thus only in exceptional cases be looked upon as predatory.¹⁸⁶

4.3.1.3 Comment

Pricing below cost of a dominant company can form part of an abusive behaviour and result in exclusion of competitors since a dominant company might, due to its economic strength on the market, possess a greater ability to recoup the losses being made during the price-cutting phase. The Commission in its' Discussion Paper considers the possession of a dominant position and the existence of entry barriers as proof enough of the ability to recoup the losses incurred during the price-cutting phase. Since the dominant position as such in this case also constitutes an entry-barrier, it seems to be much more the fact that the company is dominant –and has the possibility to extend this dominance, that is problematic. From my point of view, this is one of the clearest examples on that the dominance as such is punished.

Price competition is in practically all other situations desirable since it is of direct advantage to the customers. What makes extremely low prices dangerous in this case is that when applied over time, only the one who is able to recoup the losses will survive and the “battlefield” is, in the worst case, left with one sovereign, which is able to act to great extent independently and without competition. Therefore it is presumed, that when a dominant firm prices below average avoidable cost, it does this since it is convinced that it will survive and that other competitors will not. The actual possibility of recouping the losses is left without further scrutiny.

In my point of view and as suggested in the EAGCP Report, the focus should lie completely on barriers to entry and on the predatory intent and

¹⁸⁴ Discussion Paper, para 119

¹⁸⁵ Ibid., para 122

¹⁸⁶ Ibid., para 127

not on the pricing below different cost levels. One reason is the difficulty to obtain relevant information on the costs, another is that a pricing that over time is below costs and is then raised, will attract new entry, or re-entry of former actors on the market if not combined with other entry barriers, a third reason is that price competition is in fact desirable.

In the case of predatory pricing, an effects-based approach seems to be particularly suitable.

4.3.2 Rebates

4.3.2.1 EAGCP Report

The analytical framework of the new approach presented in the EAGCP Report differs strongly from the per se prohibition. The competition authority shall first analyse the kind of exclusionary strategy – is the conduct exclusionary within the primary market of the incumbent or on a secondary, horizontal or vertical? Thereafter, possible pro-competitive effects shall be balanced against the anti-competitive.¹⁸⁷

In the Report, the new approach is illustrated through the plain example where an incumbent uses rebates as a kind of penalty on new entrants. For the customers to want to switch to a new supplier, the latter has to offer a price lower than the one offered by the incumbent, minus the rebate. The rebate can be seen as an “entry fee”, aiming at reduce the efficiency gains of the new entrant and thus creating a barrier to entry. An entrant would enter the market only if costs are so low that the entry would be profitable despite the “entry fee”. The reduced profitability of entry and loss of potential price competition is harmful to consumers.¹⁸⁸

The following questions are considered relevant in the approach to the situation described above:

- What exactly are the negative external effects on a third party, inducing that the buyer would be prepared to enter an anti-competitive exclusive dealing agreement with the incumbent? – If no such effects can be found the case shall be dismissed.
- What is the magnitude of the penalty imposed on the entrant? Here an approximation on the reduction in price that the entrant would have to offer at various quantity levels can be made.
- Has the rebate in fact the effect of keeping equally efficient competitors out of the market?
- What ability do the downstream firms have to pass on a reduction in their own input prices to the consumers? Is there an incentive for the downstream firms to increase efficiency? – Such considerations have

¹⁸⁷ EAGCP report, p 37

¹⁸⁸ Ibid., p 37

to be made when considering possible efficiency gains based upon the granting of the rebate.

4.3.2.2 Discussion Paper

The Discussion Paper also suggests a move away from a per se prohibition. The "loyalty increasing" effect of the rebate will be evaluated by reference to the effective price of the products and how great the share of demand represented by the relevant products, in comparison to the average avoidable costs of the dominant undertaking. The lower the calculated effective price is compared to the average price of the dominant supplier, the stronger the loyalty enhancing effect.¹⁸⁹ If the effective price is lower than average total cost of the dominant company, it will be very difficult for equally efficient competitors to compete for this part of demand. This method will enable the Commission to assess whether an equally efficient competitor would be able to compete.

A distinction between unconditional and conditional rebates is made in the Discussion Paper.

Unconditional rebates, are rebates granted only to certain customers - independently of their purchase behaviour, and has as the effect as to differentiate the purchase price between customer groups. Such rebates can have exclusionary effect when, for instance, offered to customers that might more easily switch to foreign suppliers because they are situated in a border region. To assess possible exclusionary effects, the Commission will apply the guidance as described for predatory pricing.

Conditional rebates, on the other hand, are granted to customers to achieve certain purchase behaviour. Such rebates can lead to differentiation in price between different buyers.¹⁹⁰ Conditional rebates are considered to have particularly strong foreclosure effect when given on *all* purchases when a certain threshold has been exceeded within a given reference period and when this threshold is set above the amount that would anyhow be purchased of the buyer. Such rebates would result in inducing the buyer to buy more than it would otherwise have done from the dominant undertaking. The strength of the inducement is dependent on the level of threshold and the rebate percentage.¹⁹¹ A rebate system with standardised volume thresholds is less likely to be found abusive, since the rebates sets in to all buyers at the same level. The buyers that cannot purchase the required amounts will not be caught by the loyalty enhancing effect and the buyers who buy amounts far greater than the threshold will not gain any further privileges. It is thus not likely that a foreclosure will be the effect of such a system, there can however be cases where the buyers buy similar amounts and where the rebate system is targeted to hinder these customers to switch.

¹⁸⁹ Discussion Paper, para 154

¹⁹⁰ Ibid., para 137

¹⁹¹ Ibid., paras 152-153

Individual analysis is therefore essential in each case concerning rebates. The main possible anticompetitive effects of rebate systems are considered those of market foreclosure and price-discrimination.¹⁹² The dominant position of the company, results in that there is no proper substitutes to the dominant company's products for a great deal of the market. The reason for this might be that many end customers due to reputation prefer the dominant brand or that the demand cannot be sufficient provided for by other producers.

As mentioned above, it is also of importance for the assessment of the foreclosing effects, in how far the rebate system affects a substantial part of market demand i.e. that the dominant company applies it to a great part of its buyers. If the dominant company does only apply the rebates to certain customers, the Commission will investigate in how far these customers are of particular importance to the entry or expansion of competitors.¹⁹³

The Commission will assess the likely and actual foreclosure effects of the obligation or system in the market where the company is dominant and with regard to the possibility of existing and future competitors to counter and constrain such conduct by the dominant firm.¹⁹⁴

In cases where there is a lack of reliable information on the dominant company's costs, the Commission will, as in the case of predatory pricing, use the cost data of apparently efficient competitors. If this is not possible, there will be a general assessment on in how far the rebate system hinders entry or expansion. This can be done through comparing the performance of the dominant company and its competitors before and after the introduction of the rebate system.¹⁹⁵

4.3.2.3 Comment

Concerning rebates, the Commission seems to move more in the direction of the EAGCP. The "loyalty increasing" effect of the rebate will be evaluated by reference to the effective price of the products and how great the share of demand represented by the relevant products in comparison to the average avoidable costs of the dominant undertaking. This will enable the Commission to assess whether an equally efficient competitor would be able to compete. In this case, cost calculations will also have to be made. In the case of rebates, however, the possibility of directly comparing the rebate prices with other effective prices remains.

¹⁹² Discussion Paper, paras 139-140

¹⁹³ Ibid., para 162

¹⁹⁴ Ibid., 143-144

¹⁹⁵ Ibid., para 164

4.3.3 Tying and bundling

4.3.3.1 EAGCP Report

Tying or bundling is listed as a possible abuse within the meaning of article 82 in 82(d).

The classical example of pure bundling is when a firm with dominance on market A, prevents entry of a firm active on market B, on which the former is also acting. By bundling the products from market A and B, the dominant firm prevents customers from buying the other company's products. There are, as described above¹⁹⁶, few incentives for a firm to reduce competition on a market on which there is a demand for its own products. If the company from market A is active also on market B, it is more likely that it would try to prevent entry or successful expansion of other companies on market B in the first place and thereby also protect its' primary market from entry. Such effects can be reached by bundling the products of market A and B. If entry on market B takes place despite the bundling, the dominant firm would once again be interested in selling the products separately.¹⁹⁷

The different and complex situation of bundling and the pro- and anti-competitive effects possible for consumers, calls specific for an economic approach according to the authors of the Report. A full picture of the scenario must be analysed and the following questions are, according to the EAGCP- Report, of certain relevance:

- Is there sequential entry?
- Does the existence of a competitor on the secondary market make entry into the primary market more likely?
- Is the quality of the products on market B of the competing company higher than of those offered by the dominant company?
- Does the bundling make sense? Does it have commercial or technological reasons?
- Are efficiencies the major determining factor for the dominant firm to bundle? – Caution must be taken when considering efficiency arguments, especially in cases of compatibility problems.¹⁹⁸

4.3.3.2 Discussion Paper

In the Discussion Paper, it is also recognised that tying and bundling can have anti-competitive effects as well as being beneficial to customers. As

¹⁹⁶ See note 135, p 32

¹⁹⁷ EAGCP report, p 41-42

¹⁹⁸ Ibid., p 42

anti-competitive effects, higher prices, foreclosure and price discrimination are mentioned.¹⁹⁹

The assessment of the abusive character of the tying or bundling builds upon the following elements:

- The company concerned is dominant in the tying market. Dominance also on the tied market makes abuse more likely, but is not necessary.
- The tying and tied goods are distinct products. This is the case if, from the customers' point of view, the products would be purchased separately. It is, however, not necessary that the products belong to separate product markets.
- A market distorting foreclosure effect is likely
- There is neither objective nor efficiency justification for the practice

In the assessment of the foreclosure effect on the tied market, the Commission suggests a two-step procedure in combination with an overall analysis of the practice, its application and the strength of the dominant position. First, the Commission aims at establishing which customers are tied and second, at assessing whether these customers constitute a sufficient part of the market being tied. The larger part of the market being tied, the more likely the conclusion that the practice has foreclosing effects.²⁰⁰

Moreover, in the case of bundling, competitors are foreclosed if the bundled price is so low that efficient competitors offering some, but not all, of the products cannot compete against the bundle. For an equally efficient competitor to be able to compete, the individual price that the customers pay for each component in the bundle should cover the long run incremental cost of the product. The incremental costs are chosen as benchmark since these also covers the costs that the dominant company might have for the products in the market where it is not dominant. If no information on the incremental costs of the dominant company can be found, data from rivals can be used, provided there is no reason to believe that the rival is less efficient. Where there are no cost data at all available, it might still be possible to show that the rival was in fact excluded or marginalised from the market.²⁰¹

The analysis of the market foreclosure also needs to contain an assessment on in how far multi-product rebates tie customers that are particularly important for the entry or expansion of rivals or if the rebates are targeting the customers of specific competitors.²⁰²

¹⁹⁹ Discussion Paper, para 179

²⁰⁰ Ibid., para 188

²⁰¹ Ibid., paras 190-191

²⁰² Ibid., para 194

To some extent there are considered to be possibilities for the undertaking to justify its tying practice on grounds as quality, health or safety or for efficiency reasons.²⁰³

4.3.3.3 Comment

In the case of tying and bundling the Commission, again, has chosen cost-price calculations as a base for the assessment of abusive behaviour. These data shall be compared to data from apparently equally efficient competitors. The question on which competitors are equally efficient, however, remains.

4.3.4 Microsoft

In the recent case of *Microsoft*,²⁰⁴ the Commission shows signs on a new approach. Two abuses were considered, which I will just briefly analyse below.

By refusing to supply interoperability information, Microsoft had extended its dominance to an adjacent market. This foreclosed other firms to design work group servers compatible with windows. The Commission compared the circumstances with cases like *Magill*²⁰⁵ and found that the special circumstances mentioned in the case were not exhaustive.²⁰⁶ The Microsoft case was found to be special. Microsoft had stopped providing interface information as it had started to compete on the work group servers itself, which was considered to eliminating competition, reducing incentives to innovate and harming consumers since Microsoft would also lack incentives to innovate if it was not faced with competition.²⁰⁷ Microsoft tried to justify its refusal to supply with the argument that the information was the result of research and that it, to a great extent, was protected by intellectual property rights. This was rejected by the Commission since it considered the primary function of intellectual property rights to be the stimulation of creativity for the public good. A refusal to supply would in this case have harmful effects on innovation and thereby on consumers.²⁰⁸ The Commission did not consider Microsoft's own incentives to innovate to be reduced as a result of the granting of access since this granting did not include access to the source code.²⁰⁹

²⁰³ Discussion Paper, para 204-206

²⁰⁴ Case COMP/C-3/37.792, *Microsoft* [2004] Commission Decision of March 24

²⁰⁵ Cases C-241/91P *ITP, BBC and RTE v Commission* [1995] ECR I 797

²⁰⁶ Case COMP/C-3/37.792, *Microsoft* [2004] Commission Decision of March 24, para 555

²⁰⁷ *Ibid.*, paras 725-734

²⁰⁸ *Ibid.*, para 711

²⁰⁹ *Ibid.*, paras 713-729

The other abuse concerned bundling of a streaming media player to the Windows operating system. The Commission found that Microsoft since 1999 had provided the Windows Media Player without extra charge in combination with purchase of Windows. Although Media Player was integrated into Windows, the Commission found the products to be separate since independent companies provided them separately and this was found to indicate a separate demand.²¹⁰ The Commission held that Microsoft did not give customers a choice other than pre-installing the media player when licensing Windows²¹¹ and went on to analyse the possibility of selling other media players, which could then be additionally installed, over the internet.²¹² The Commission found that such possibilities were less satisfactory than pre-installation and that Microsoft's share of the media player market had increased significantly through the tying.²¹³ The increased share of the media player market was not accepted as a result of competition on merits by the Commission, since commercial reviews often found other media players better.²¹⁴ Microsoft was considered to have used Windows to distribute its media player. Such tying raises the barriers to entry and expansion and has particular impact on a market with network effects, such as the software market. The strength of Microsoft in the media player market is thereby protected and this reduces incentives to innovate in similar software.

The Commission has to a high degree focused on entry barriers in its decision, which is a step towards an effects based approach. This is of course difficult not to do in a case where the allegedly abusing undertaking has a market share of over 90% on the market for operating systems.

Refusal to supply interoperability information was considered to eliminate the incentives of other companies to innovate. The lack of further innovations will leave Microsoft without competition –which will then reduce Microsofts own incentive to innovate and such a development would be harmful to the general public good. The Commission thereby considers, as also done in *Magill*²¹⁵, that intellectual property rights in exceptional circumstances will not prevail. The question is in which extension this will be the case.

The Commission chose to focus on tying instead of predation. The free giving away of media player at purchase of windows after investing huge amounts in developing it, could also have been seen as predation. However, in this case, it was considered that the sale above long run incremental cost was not predatory. The reasoning of the Commission concerning the tying is to a great extent effects based. Software is a market with very rapid

²¹⁰ Case COMP/C-3/37.792, *Microsoft* [2004] Commission Decision of March 24, paras 800-825

²¹¹ *Ibid.*, paras 826-834

²¹² *Ibid.*, paras 844-846

²¹³ *Ibid.*, paras 871-879

²¹⁴ *Ibid.*, paras 891-897

²¹⁵ Cases C-241/91P *ITP, BBC and RTE v Commission* [1995] ECR I 797

development. In the case, the Commission did not closely address the fact that the tying of media player could lead to an elimination of future competition in the field of information technology.

5 Conclusion and Outlook

The Commissions approach to the assessment of abuse under article 82 appears to move slightly in an economic direction. However, the working method seems to remain to the greater extent the same.

The Commission apparently considers it a fact that, regardless of whether one advocates a form-based or an effects-based approach, article 82 is only applicable on dominant undertakings. Thus the question of however the company is dominant or not has first to be solved. The relevant market is considered necessary to define for a couple of reasons. First, to be able to identify actual competitors who are able to put competitive constraints on the undertaking in question. Secondly, since a dominant position, according to the view of the Commission, only can exist in relation to a market and not in the abstract, the relevant geographical- and product market has to be carefully defined. In order to avoid the previous difficulties concerning market definition and the assessment of dominance, the Commission has considered some of the criticism. For instance, the SSNIP test will only be used in combination with scrutiny of among others product characteristics and substitutability, buyer power, history of expansion and barriers to entry etc will be taken into consideration in the assessment of the ability of the undertaking to behave independently.

Regarding the definition of the relevant market and of a dominant position, there seem to be few actual reforms. When assessing a dominant position, the Commission will still focus on market shares as a first step -even though market shares are in fact in very few cases indicative on market power. This means that undertakings with large market shares will have to be extra careful in setting prices, granting rebates and offering product combinations, since they more easily attract the attention of competition authorities.

Firms that are in possession of very large market shares and thereto for instance intellectual property rights -or which are protected by other entry barriers, can raise prices above the competitive level, which would then be harmful to consumers. Such dominance does, however, only exist in combination with barriers to entry or expansion.

It is not surprising that the Commission hesitates to adopt a completely new approach to the application of article 82. If the form-based method was to be left entirely and a case-to-case analysis of all relevant circumstances such as entry barriers and the effects of specific behaviour would be applied, this would, initially, probably lead to legal uncertainty and unpredictability. Nevertheless, if the view on the functions of article 82 shall be modernised, the review calls for a change of method in its application.

There were several reasons for reviewing article 82. The massive criticism, as described above, from economic and legal scholars regarding the

uncertainty of the application and the confusing of objectives as well as the lack of economic sense, the Commissions' own interest to create a uniform approach to competition issues and to follow the objectives of the Lisbon agenda and, most certainly, pressure from trade and industry.

So, which function is article 82 supposed to have in the context of the objectives of competition law?

A great deal of the problems of keeping a market competitive is already regulated through article 81. The specific features of article 82 lies in the difficulties connected to market strength. In theory, the goals of the articles, however, coincide: to create/maintain an open, competitive market where efficiency benefits the consumers in terms of price, quality and progress. What makes market strength dangerous is that it enables the undertaking to reduce competition through unilateral actions.

-Does this mean that market strength is not desired? The driving force of the competitive process is the will of the actors to increase market share and not the adjustment to their competitors' behaviour. The desired effect of competition law is that the key to success lies in the efficiency of the undertaking, from the consumers' point of view.

It must, therefore, be possible for a dominant undertaking to justify its' behaviour on efficiency grounds. If this is not possible, the dominant company would lack means to compete and would only be able to participate in the competitive process to a certain limit, namely that of its' dominance. Thereafter it would have to adopt a more or less passive behaviour. In its Discussion Paper, the Commission has recognised the need for allowing objective justification or justification based on efficiency arguments. The justification is suggested as to underlie the same criteria as those of article 81

It has repeatedly been said that dominance as such shall not be punished. Dominant undertakings are, however, underlying a special responsibility. This special responsibility can, according to my view, only be understood by- and be clear to the undertakings, if the anti-competitive effects of certain behaviour are defined. If there are significant anti-competitive effects of behaviour such as price dumping or tying, then dominance can also be concluded. It is not the dominant position that hurts the competitive situation.

Does the method of assessment of the Commission have to be based on a starchy multiple step method? Article 82 is only applicable on undertakings in a dominant position. The Commission has preferred to continue to assess dominance as a second separate step after the definition of the relevant market. As expressed in the EAGCP Report, a significant competitive harm should constitute sufficient proof of dominance.

If there is a need for a more effects based approach and if consumer welfare is the primary interest of the Commission, the focus should lie on however

equally efficient competitors are excluded or if the competition is in fact fair and justifiable. To put undertakings with high market shares in a corner so that they automatically underlie a special responsibility, is to punish market strength. Dominance has to be determined under the circumstances of the questioned behaviour.

It is often said that the new approach to article 82 is an economic approach. Many of the elements in the method suggested by the Commission in its' Discussion Paper are of economic character and require analysis made by economists, for instance the market share analysis, the SSNIP test and the cost / effective price calculations. This leads unavoidable to a certain degree of expert rule. It seems to be likely that the concerns of the Commission on the effects based approach suggested in the EAGCP Report regard legal predictability. The question is if not the effects based approach provides for greater understanding and legal certainty than the form based.

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