



FACULTY OF LAW
University of Lund

Anders Tjernlund-Jemail

The Dilemma of Article 81(1) EC
-the notion of 'restriction of competition'

Master thesis
20 points

Mark Furse

EC Competition Law

Spring 2001

Contents

<u>SUMMARY</u>	1
<u>ABBREVIATIONS</u>	4
<u>1 INTRODUCTION</u>	5
<u>2 THE DILEMMA OF ARTICLE 81(1) EC</u>	6
<u>3 THE UNITED STATES APPROACH</u>	9
<u>4 EC COMPETITION POLICY</u>	11
<u>5 ECONOMICS IN COMPETITION LAW</u>	13
5.1 <u>EFFECTIVE COMPETITION</u>	13
5.2 <u>ECONOMIC MODELS OF COMPETITION</u>	14
5.3 <u>MARKET POWER</u>	15
5.4 <u>ECONOMICS OF ARTICLE 81 EC</u>	16
5.5 <u>VERTICAL AGREEMENTS</u>	17
5.6 <u>HORIZONTAL AGREEMENTS</u>	19
<u>6 THE NOTION OF RESTRICTION OF COMPETITION</u>	20
6.1 <u>INTRODUCTION</u>	20
6.2 <u>THE ACADEMIC DEBATE ON THE NOTION OF RESTRICTION ON COMPETITION</u>	21
6.2.1 <u>Introduction</u>	22
6.2.2 <u>Arguments in favour of a rule of reason approach</u>	22
6.2.3 <u>Arguments against a rule of reason approach</u>	26
6.2.4 <u>Advocate General Lenz in the Bosman case</u>	29
6.3 <u>OBJECT OR EFFECT AND APPRECIABILITY</u>	30
6.4 <u>THE ANCILLARY RESTRAINT DOCTRINE</u>	31
6.5 <u>RESTRICTION OF COMPETITION – A CASE STUDY</u>	32
6.5.1 <u>Exclusive distribution agreements</u>	32
6.5.1.1 <u>Consten and Grundig</u>	33
6.5.1.2 <u>Société Technique Minière</u>	35
6.5.1.3 <u>Concluding remarks</u>	36
6.5.2 <u>Selective distribution agreements</u>	37
6.5.2.1 <u>Metro I</u>	38
6.5.2.2 <u>Metro II</u>	39
6.5.2.3 <u>Concluding remarks</u>	39
6.5.3 <u>Exclusive purchasing agreements</u>	40
6.5.3.1 <u>Delimitis</u>	41
6.5.3.2 <u>Langnese-Iglo</u>	42
6.5.3.3 <u>Concluding remarks</u>	43

6.5.4	<i>Licensing of intellectual property rights</i>	44
6.5.4.1	<i>Nungesser</i>	44
6.5.4.2	<i>Coditel II</i>	45
6.5.4.3	<i>Concluding remarks</i>	46
6.5.5	<i>Franchising</i>	47
6.5.5.1	<i>Pronuptia</i>	47
6.5.5.2	<i>Concluding remarks</i>	48
6.5.6	<i>Sale of businesses</i>	49
6.5.6.1	<i>Remia</i>	49
6.5.6.2	<i>Concluding remarks</i>	51
6.5.7	<i>Co-operation agreements</i>	51
6.5.7.1	<i>The Odin decision</i>	51
6.5.7.2	<i>Gottrup-Klim</i>	54
6.5.7.3	<i>European Night Services</i>	55
6.5.7.4	<i>Concluding remarks</i>	58
7	<u>THE NEW POLICY ON VERTICAL AND HORIZONTAL RESTRAINTS</u>	60
7.1	<u>THE COMMISSION'S NEW POLICY ON VERTICAL RESTRAINTS</u>	60
7.2	<u>THE COMMISSION'S NEW POLICY ON HORIZONTAL RESTRAINTS</u>	61
7.3	<u>THE MODERNISATION WHITE PAPER</u>	63
8	<u>CONCLUSIONS</u>	64
	<u>BIBLIOGRAPHY</u>	68
	<u>TABLE OF CASES</u>	71

Summary

The dilemma of Article 81(1) EC can be described as a fight between control and freedom. Control in the sense that the Commission has taken a formalistic approach on the interpretation of Article 81(1) EC with the result that many agreements are caught by the prohibition. The only way to avoid the automatic nullity of Article 81(2) EC is then through the exemption paragraph, Article 81(3) EC, which is exclusively controlled by the Commission. Freedom in the sense that all agreements that, after balancing pro- and anti-competitive effects, produces a positive net effect and enhances consumer welfare cannot be subject of the prohibition or control.

Article 81(1) EC prohibits all agreements 'which have as their object or effect the prevention, restriction or distortion of competition'. Similarly, Section 1 of the Sherman Act 1890 in the United States declares every contract in restraint of trade or commerce to be illegal. In order to distinguish agreements that are in restraint of trade from those who are not, the American courts have developed a rule of reason. The pro- and anti-competitive effects of the agreement are weighed against each other, in its economic context, in order to determine whether the agreement in question enhances or reduces competition. In order to do that, an extensive analysis of the market has to be undertaken. The American rule of reason is solely based on economic theory, while Article 81(1) EC also adheres to the goal of creation of a single market.

Businessmen, economists and several commentators have been arguing in favour of a rule of reason under Article 81(1) EC. However, the Commission has only abandoned its formalistic interpretation on a few occasions. The ECJ, on the other hand, has through several judgements narrowed the scope of Article 81(1) EC and opened the door for economic assessments under the paragraph. Because of this, there is a parallel academic debate going on. One concerning whether the ECJ has adopted some form of rule of reason and one concerning whether there should be a rule of reason.

There are several arguments put forward in favour of a rule of reason under Article 81(1) EC. Besides strictly economical arguments the system failure with the current system is stressed. Because many agreements falls into the scope of Article 81(1) EC on more or less loose grounds, everyone tends to notify its agreement to the Commission in order to be on the safe side and to get immunity from fines. The Commission lacks the resources to effectively deal with these notifications, which has created a huge backlog. In order to resolve the problem

the Commission introduced formalistic block exemptions and informal comfort letters instead of individual formal decisions as was intended by Regulation 17. All this has caused a state of uncertainty if not the agreements were drafted in line with a block exemption. In addition there are also problems caused with private enforcement in national courts. Furthermore, the illogical application of Article 81 is also put forward. Economic analyses are frequently made to determine if Article 81(3) EC is applicable. The issue here is whether or not, or to what extent, a competitive analysis should be made under Article 81(1) EC. The Commission has granted exemptions under Article 81(3) EC, usually justified by the agreements pro-competitive effects. This leads to the fact that the Commission states that the agreement in question both restrict and promote competition, which from an economic perspective is unacceptable.

The arguments put forward against a rule of reason does foremost relate to the structural differences between the American system and the system of Article 81 EC. Section 1 of the Sherman Act does not have any possibilities for exemptions as Article 81 EC has. Therefore, Section 1 has to consist of both the jurisdictional and the assessment approach, whereas Article 81(1) EC is jurisdictional and Article 81(3) EC contains the assessment aspect. Thus, it is argued that Article 81(1) EC is designed to confer jurisdiction to the Commission in order to be able to assess the agreement under Article 81(3) EC, which according to the Commission contains all the aspects of a rule of reason. It is argued that any import of the terminology, 'per se' and rule of reason, from the American system therefore only would cause confusion in the EC system. However, the scope of economic assessment under Article 81(1) EC, introduced by the ECJ, has carefully been examined and the conclusion is made that the ECJ has created its own notion of restriction of competition, similar to the ancillary restraints doctrine. The restriction has to be objectively necessary for the attainment of a legitimate business practice and the agreement must be assessed in its legal and economic context in order to acknowledge the effects. Legitimate business practices identified by the Community Courts are exclusive distribution, selective distribution, exclusive purchasing, licensing of intellectual property rights, franchising and in special circumstances joint ventures on the horizontal level. Regard is being taken to the integration goal of the Community.

The Commission has, however, changed its approach in their new block exemptions. The new block exemption on vertical restraints has already entered into force and the block exemption on horizontal restraints is on the way. The Commission has now surrendered to economic thinking and created broad flexible block exemptions based on economic theory. However, the 'hard core'

clauses are still present representing the integration goal. Furthermore, by the issuance of the Modernisation White Paper the Commission intends to give up its monopoly on Article 81(3) EC.

These changes have taken the force out of many of the arguments put forward in favour of a rule of reason under Article 81(1) EC. Thus, the claimed system failure seems to be on the way to be mended. Economic thinking in flexible block exemptions clears the majority of the concerned agreements without having to draft the agreements after the structure of a block exemption. Still, there is the argument of illogical application of first prohibiting and then exempting. The Commission has still the formal control; even in practice life is easier for the businessmen and lawyers.

The notion of restriction of competition, however, remains the same. The Commission uses, in general, Article 81(1) EC as a jurisdictional paragraph although the ECJ's notion of restriction of competition should prevail. With the new block exemptions it may be hard to know if an agreement is benefiting from a block exemption or falls out of Article 81(1) EC when the two mechanisms partly coincide. This does not cause, for the majority of the agreements, any practical problems, but remains to be a question with fundamental concern.

Abbreviations

A. 81 EC	Meaning Article 81 of the Treaty of the European Community
CFI	Court of First Instance
EC	European Community
ECJ	European Court of Justice
EU	European Union

1 Introduction

Article 81(1) EC prohibits all agreements which have as their ‘object or effect the prevention, restriction or distortion of competition’. The interpretation thereof can result in different approaches towards what constitutes a restriction of competition. The Commission interprets the paragraph mostly as a jurisdictional provision, that is very widely, in order to exercise control under the exemption paragraph in Article 81(3) EC. On the other hand, the commercial world, economists and several commentators argues for a rule of reason approach based on economic theory, that is a very narrow interpretation. The ECJ has opened the door for economic assessments under Article 81(1) EC in its jurisprudence, but it is considered to be rather unclear to what extent economic assessments under Article 81(1) EC applies.

The purpose of the thesis is, therefore, to examine what the notion of restriction of competition means under Article 81(1) EC. In order to do that an examination of the Community Courts’, not that extensive, case law on the subject is needed. Because of the different opinions on the subject it is in order to examine the differing views on what is or should constitute a restriction of competition within the meaning of Article 81(1) EC. Furthermore, a recent change in policy on vertical and horizontal restraints by the Commission has caused it to introduce new block exemptions quite different from the old ones. A question worth examining is, therefore, if this change in policy towards more economic thinking has change anything in relation to the notion of restriction of competition under Article 81(1) EC.

The debate has generally concerned the treatment of vertical agreements and not so much horizontal agreements whereas Article 81 EC makes no distinction between them. This is because vertical agreements are the category which would, to a greater extent, be affected by an introduction of a rule of reason.

The thesis is structured in the way that first the author will explain the dilemma of Article 81(1) EC and compare it with the American system. Then policy and economics behind competition law will be explained. The head chapter of the thesis is the examination of the notion of restriction of competition, including the Community Courts’ case law. Then the new policy approach by the Commission will be examined and finally the author’s conclusions will be revealed.

2 The Dilemma of Article 81(1) EC

For the purpose of this thesis it is in place to first provide a full reading of Article 81 EC. The most relevant wordings are marked in italics. Article 81 EC states:

1. The following shall be *prohibited* as incompatible with the common market: all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their *object or effect the prevention, restriction or distortion of competition* within the common market, and in particular those which:
 - (a) directly or indirectly fix purchase or selling prices or any other trading conditions;
 - (b) limit or control production, markets, technical development, or investment;
 - (c) share markets or sources of supply;
 - (d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;
 - (e) make 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.
2. Any agreements or decisions prohibited pursuant to this Article shall be *automatically void*.
3. The provisions of paragraph 1 may, however, be *declared inapplicable* in the case of:
 - any agreement or category of agreements between undertakings;
 - any decision or category of decisions by associations of undertakings;
 - any concerted practice or category of concerted practices,which contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not:
 - (a) impose on the undertakings concerted restrictions which are not *indispensable* to the attainment of these objectives;
 - (b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.

How to interpret Article 81(1) EC in the sense of what constitutes a ‘restriction of competition’ has proven to be a dilemma in EC Competition law. Two major problems can be identified. First, the ‘essence’ of an agreement is to restrain the parties in some manner.¹ The author assumes that it is fully accepted that all agreements cannot fall under the prohibition of Article 81(1) EC. The problem is,

¹ Chicago Board of Trade v. US, 246 US 231 (1918).

therefore, to find a way to distinguish the agreements that are caught by the prohibition from the ones that are not. Secondly, an agreement may both have pro- and anti-competitive features, where the restriction is more or less necessary in order for the implementation of the agreement, which has overall positive effects on competition. Often these two problems are related. The application of Article 81(1) EC has been inconsistent in dealing with these problems and voices have been raised to follow the United States in their solution to the problem. However, to copy the US solution may not be possible due to the structural differences in the respective statutes. The EC competition law contains a mechanism for exemptions, while the US antitrust law does not.² This perspective also reveals a more fundamental aspect to the dilemma, namely the substantive and the procedural aspect of competition law. In other words, these two aspects determine what respective paragraph, provision or article should contain and maybe more important the issue of who will control the applicability thereof.³

Control is generally not a popular feature in western countries, but may serve its purpose in the field of competition law. The problem is, that the level of control must be set at a level where it does not disturb the trade which is the essence of what competition law is bound to protect. This issue becomes apparent in the Commission's view that too many agreements have to travel through 81(3) EC and this is probably one point Korah rightly raises in her article⁴ when she explains the difficulties for companies to be subject to 81(3) EC when it is not necessary.

The nullity conferred by Article 81(2) EC is automatically, but does not necessarily apply to every provision in the agreement. Only the provisions subject to the prohibition become void provided that those provisions can be separated from the agreement without depriving the purpose of it. This is to be determined objectively.⁵ The nullity has opened the door for the 'Euro-defence' in private litigation, where one contracting party is trying to escape the obligation of a contract claiming that it is in breach of Article 81(1) EC.⁶

An exemption is an exemption from the application of Article 81(1) EC and does not remove the agreement from the scope of Article 81(1) EC. Analyses made under Article 81(3) EC are similar to the analyses under the notion of 'rule

² Craig, de Búrca, *EU law: text, cases, and materials*, 2 ed., Oxford 1998, p. 903.

³ Forrester and Norall, 'The Laicization of Community law: Self-help and the Rule of Reason: How Competition law is and Could be Applied' in *CMLRev* (1984) 21, p. 13.

⁴ Korah, Valentine, 'The Rise and Fall of Provisional Validity – The Need for a Rule of Reason in EEC Antitrust' (1981) 3 *NW J Int. L and Bus.*, p. 355.

⁵ See cases 56 and 58/64 *Etablissements Consten SARL and Grundig-Verkaufs-GmbH v. Commission* [1966] ECR 299; and Case 56/65 *Société Technique Minière v. Maschinenbau Ulm GmbH* [1966] ECR 235.

⁶ Furse, Mark, *Competition Law of the UK & EC*, Second edition, London 2000, p. 136-137.

of reason' in the US. The difference is that the rule of reason takes the agreement in question out of Section 1 of the Sherman Act. The Commission's monopoly on applying Article 81(3) EC and to give individual exemption is often seen as an obstacle to trade. The Commission is swamped with notifications and deals with the vast majority in an informal way. Furthermore, the Commission can in an exemption confer conditions to the agreement, which might alter the initial bargain power of the parties to the agreement.⁷

⁷ Ibid, p. 139-140.

3 The United States approach

By reason of constant referrals to United States antitrust law and their rule of reason there is a need to briefly explain its content and structure. Section 1 of the Sherman Act 1890 states:

“Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal. Every person who shall make any contract or engage in any combination or conspiracy hereby declared to be illegal shall be deemed guilty of a felony...”

The statutory language in Section 1 of the Sherman Act is simple. It outlaws any sort of agreement of restraint of trade. The Sherman Act has been in force for over 110 years and has significantly been shaped by case law over time. Classic anti-competitive categories has been identified and are seen as ‘per se’ violations, which means that if the conduct is proved there will be no further analysis of the restraints reasonableness.⁸ The US Courts has developed a rule of reason approach, based on the old common law doctrine of ancillary restraints. This way of thinking was first acknowledge in 1911 in the case *Standard Oil Co. of New Jersey v. United States*,⁹ where it was held that only undue or unreasonable restraints should be illegal. The pro- and anti-competitive effects of the agreement are weighed against each other, in its economic context, in order to determine whether the agreement in question enhances or reduces competition. In order to do that, an extensive analysis of the market has to be undertaken.¹⁰

United States antitrust law does not have an exemption process, but there is a business review processes available to some extent. The firm sends in a detailed description of what they intend to do and the enforcer answers with a business review letter, which states if they intend to enforce the agreement or not. These letters are also published and serve as a helpful indication on what is doable or not. However, such a letter does not protect against private litigation. Furthermore, there are no ‘de minimis’ requirements to enforce the Sherman Act. Private enforcement is important in the United States and Section 4 of the Clayton

⁸ Interview with Ray V. Hartwell, III, Hunton & Williams, Washington D.C April 2000 by Mark Furse.

⁹ *Standard Oil Co. of New Jersey v. United States* (1911) 221 US 1.

¹⁰ Craig, de Búrca, *supra* note 2, p. 903-904; and Furse, Mark, *supra* note 6, p. 147-148.

Act gives private parties the power to enforce and the right to enjoy treble damages.¹¹

The rule of reason was developed by the US courts in order to make the Sherman Act judicial efficient. However, the classification of an agreement in a specific case is a problem and that is the struggle lawyers are faced with in the United States. What categories belong under ‘per se’ or ‘rule of reason’ has also shifted over time, generally from ‘per se’ towards the rule of reason.¹²

In United States vertical agreements are subject to Section 1 of the Sherman Act, which makes no distinction. The question is really what is a ‘restraint of trade’. Vertical agreements are generally treated under the rule of reason. As long as the inter-brand competition, or inter-company competition, is good vertical agreements are not a problem despite territorial protection. It is only when inter-brand competition is low that vertical agreement could be in trouble. Accordingly, the moment substantial market power is present there is a risk that the agreement will be illegal, but even then there are justifications such as the free riding dilemma.¹³

To the question if horizontal agreements are likely to be anti-competitive in the US the answer is both yes and no. There is a group of agreements where the restraint is considered to be ‘ancillary’ to an otherwise pro-competitive agreement. The presumption of violation, or ‘per se’ violation, refers only to the ‘naked’ restraints on trade as price fixing. The presumption is a legal assumption and it, generally, does not help to argue otherwise. It is the agreement that is illegal and it does not matter if it has been carried out or followed.¹⁴

¹¹ Interview with Ray V. Hartwell, *supra* note 8.

¹² Interview with Michael G. Cowie, Howrey Simon Arnold & White, LLP, Washington D.C April 2000 by Mark Furse.

¹³ Interview with Roxanne E. Henry, Howrey Simon Arnold & White, LLP, Washington D.C April 2000 by Mark Furse.

¹⁴ *Ibid.*

4 EC Competition policy

As we have seen, United States antitrust policy is governed only by economic considerations. Does EC competition policy differ? Competition policy determines the road to take when deciding on the use of economics in the decision-making and the choice between different values. Two main goals exist in EC competition policy: the promotion of integration within EU and the promotion of effective and undistorted competition. The integration goal is laid down in Article 2 EC and explains why the Commission strikes down agreements or practices, which might conflict with this goal.¹⁵ The rationale behind this goal is the notion of the single market. The rules regulating the four freedoms has effectively removed the barriers between the Member States allowing goods, services, persons and capital to flow freely across the borders. EC competition law must support this objective in the sense that private undertakings cannot be allowed to restore those barriers between the Member States. This is why the Commission and the Courts strictly upholds the integration goal.¹⁶

Article 3 g EC sets out the economic goal, which is further acknowledge in the main competition rules: Article 81, 82 EC and the Merger regulation.¹⁷ For the purpose of this thesis Article 81(1) EC states that agreements ‘which have as their object or effect the prevention, restriction or distortion of competition’ are incompatible with the common market and void if not exempted. In other words, effective competition must also be preserved within EU.¹⁸

The two different goals of EC competition policy can sometimes conflict with each other. For example, territorial protection for retailers may sometimes be pro-competitive, supported by economic theory, but at the same time conflict with the integration goal. The Commission has often given priority to the integration goal over the economic goal. It is argued that, the result of this practice has sometimes proven to be a total failure. For example, in the Commission’s *United Distillers* decision¹⁹ the Commission gave priority to the integration goal, but by ignoring what the economic theory of the case showed, the ‘post-decision’

¹⁵ Bishop and Walker, *Economics of E.C. Competition Law: Concepts, Application and Measurement*, London 1999, p. 3-4.

¹⁶ Craig, de Búrca, *supra* note 2, p. 892.

¹⁷ Commission Regulation 4064/89 of 21 December 1989 on the control of concentrations between undertakings, as amended by Regulation 1310/97.

¹⁸ Bishop and Walker, *supra* note 15, p. 4-5; also Craig, de Búrca, *supra* note 2, p. 891.

¹⁹ Commission Decision, *Distillers Company plc (Red Label)* [1983] OJ C245/3; [1983] CMLR 173.

result became actually a step back for integration. Consequently, the use of economic theory and principles does not necessarily mean that the integration goal will not be fulfilled.²⁰

This system with dual goals of competition differs from other competition law systems, especially with the US antitrust law, which have only the economic goal to follow. However, in EC competition law it is suggested that economic analysis should be important if any concern is to be given to the efficient use of resources. This does not mean that it should always take priority, but whenever a decision results in that a commercial conduct is found contrary to the objectives of the common market, the decision must at least partially be based on some economic model to assess the competitive effects of the commercial conduct in question.²¹

²⁰ Bishop and Walker, *supra* note 15, p. 5-6.

²¹ Bishop and Walker, *supra* note 15, p. 13.

5 Economics in Competition law

As seen competition law is, wholly or partially, based on economic concerns, especially the rule of reason. Therefore, it is in order to briefly explain why economic theory and thinking is important to be able to determine if a restriction of competition really has occurred. Competitive markets are prone to lead to a higher level of consumer welfare. The term used in law is effective competition and the problem begins with the definition thereof. At the same time the definition is not that useful when assessing competition law. More important are the outcomes the competition produces than the form where competition takes place. What is meant by effective competition, however, facilitates the interpretation of the phrase “prevention, restriction or distortion of competition” in Article 81(1) EC. To be able to determine if a restriction of competition has occurred a comparison must be made to what is not a restrictive outcome. The knowledge of what outcomes effective competition produces helps to determine whether a market is subject to effective competition or not. For this reason, economic models like perfect competition, monopoly and oligopoly, are studied. At this stage the concept of market power is introduced. Welfare analyses suggest that market power is the fundamental difference between the different outcomes in perfect competition and monopoly.²² When everything comes around economics of competition revolves around market power and the questions of its definition, being and effects.²³

Effective competition is, usually, defined as the absence of market power and according to economic theory market power is defined as the ability to raise prices above the competitive price level. How to define the competitive price, on the other hand, is subject to various views, but the overall conclusion is that where there is no significant market power the market is subject to effective competition.²⁴

5.1 Effective competition

²² Bishop and Walker, *supra* note 15, p. 11-12.

²³ Faull & Nikpay, *The EC law of competition*, Oxford 1999, p. 9.

²⁴ Bishop and Walker, *supra* note 15, p. 4-5.

There are a few plausible definitions of effective competition²⁵ and the Commission seems to have defined effective competition as the absence of restraints. The problem with this definition is that all commercial contracts confer restraints on the parties and, therefore, are deemed to restrict competition. Such a wide definition does not correspond to economic thinking, but this definition has been applied by the Commission to determine whether or not an agreement falls under the scope of Article 81(1) EC, which have triggered the discussion of the need for a ‘rule of reason’ in EC competition law.

Effective competition is a goal because of the benefits it produces for the European consumers. The real question is therefore what outcomes effective competition respectively non-effective competition produces and the distinguishing between them. The answer can be found from the examination of different economic models of competition and the impact each model has on consumer welfare.²⁶ Analyses of these models are conducted under static environment, that is, factors as level of technology and innovation effects are assumed to be constant respectively ignored. The dynamic aspect of welfare analysis, on the other hand, includes such factors.²⁷

5.2 Economic models of competition

Neither of the economic models presented are perfect matches of the ongoing competitive process in the markets, but they can be used to show the basic economic concepts, which facilitates the decision whether or not enforcement of competition law is likely to increase consumer welfare.²⁸

In a market with perfect competition it is impossible for a competition authority to increase consumer welfare by any kind of enforcement due to the fact that such a market delivers both productive efficiency, that is with given resources maximum output is produced, and allocative efficiency, that is when marginal cost equals the consumers valuation of the product. The pursuit of profit maximisation is the incentive to reduce costs and with perfect competition a producer will lose money if it does not produce at the lowest possible cost. Only when a firm has market power it can afford to pursuit other goals.²⁹

²⁵ As the process of rivalry; as the absence of restraints; or where no firm can influence the market price.

²⁶ Bishop and Walker, *supra* note 15, p. 13-16.

²⁷ Faull & Nikpay, *supra* note 23, p. 9.

²⁸ Bishop and Walker, *supra* note 15, p. 16-17.

²⁹ Bishop and Walker, *supra* note 15, p. 17-19; also Faull & Nikpay, *supra* note 23, p. 12.

A monopoly³⁰ is the opposite extreme. The consumer welfare is lower in a monopoly, due to allocative inefficiency, than in perfect competition and that possible loss is what competition law should target at. Accordingly, the economic goal is to maximise consumer welfare. The possible existence of X-inefficiencies³¹ in a monopoly is something a competition authority cannot directly target at.³²

The above-mentioned models, however, fails to consider the interaction between companies that may alter the competitiveness in the market. To decide whether or not effective competition exists in the market, these interactions must be considered, as can be done in oligopoly models. The fact that many markets are more or less oligopolistic in nature it is the outcomes of oligopolistic models that should build the basis for a competition policy. To determine the market outcome non co-operative game theories are used, that is competition is evaluated with the prerequisite that each company is doing what it thinks is best subject to the actions of its competitors. The ‘prisoner’s dilemma’ is the most common example. The idea is to demonstrate that there is a dominant strategy prevailing, to compete, if effective competition exists in the market. However, oligopoly situations in real life are far more complicated than simple forms of game theories, but they are helpful for understanding the complexity of the interplay between collusion and competition.³³

5.3 Market power

The definition of market power is when a firm has the ability to raise price above the price that would prevail under competitive condition and in the process increase their profits. The question of an increase in profitability following an increase in price depends on the price elasticity of demand of the firm, which is defined as the proportionate decrease in sales resulting from an increase in price. Consequently, the ability for a firm to exercise market power depends on the

³⁰ A monopolist will sell less units at a higher price. There is allocative inefficiency in a monopoly and by lowering the price and increase output social welfare would increase. Social welfare consists of both consumer surplus and producer surplus, where consumer surplus is the difference between the consumer reservation price and the price actually paid.

³¹ That is, product inefficiency that will lead to welfare losses due to lack of effective competition.

³² Bishop and Walker, *supra* note 15, p. 20-21; also Faull & Nikpay, *supra* note 23, p. 10 and 21-24.

³³ Bishop and Walker, *supra* note 15, p. 22-23; also Faull & Nikpay, *supra* note 23, p. 24-33; and Furse, Mark, *supra* note 6, p.105-106.

firm's price elasticity of demand. The more inelastic a firm's demand curve is, the greater is the ability to exercise market power.³⁴ To assess whether or not a firm is exercising market power the current price level may be an inadequate benchmark due to the fact that the firm would already have raised the price to maximise the profit.³⁵

The assessment of a firm's elasticity of demand should be carried out at the competitive level. The elasticity itself depends on a number of factors.^{36 37}

The 'hard core' clauses of Article 81(1) EC, price fixing etc., bear no relevance to market power while other restrictive agreements can be anti-competitive if the undertakings involved have significant market power or attains it through the agreement. How to define significant market power, however, remains a bit unclear, but the economic tools mentioned helps to fight inefficiencies in a market more effectively without the risk of interfering with both static and dynamic efficiency gains. However, you cannot forget that economic theory and models are based on various assumptions. Therefore, economic theory can, in general, only contribute to the making of the most plausible story.³⁸

5.4 Economics of Article 81 EC

Competition law, in its essence, is concerned with how markets work. Thus, economic analysis is required if the law is going to be applied in a sensible way. The question and the problem is, however, how far into economics should competition law go?³⁹

Article 81(1) EC prohibits agreements, which have 'their object of effect the prevention, restriction or distortion of competition'. As stated, this formulation covers literary almost every agreement between undertakings. Criticism has been raised towards the formalistic approach, taken by the Commission, where the

³⁴ The cross-price elasticity, on the other hand, is important when defining the relevant market, but it is the own-price elasticity that determines the existence of market power.

³⁵ Bishop and Walker, *supra* note 15, p. 27-32.

³⁶ The factors are: the concentration and market shares of the market; the availability of substitutes and product differentiations, which have the effect of decreasing price competition; barriers of entry and the level of threat of potential competition: the level of sunk costs and the expected profitability of the entry; and the nature of the oligopolistic interaction.

³⁷ Bishop and Walker, *supra* note 15, p. 34-44.

³⁸ Faull & Nikpay, *supra* note 23, p. 4 and 60.

³⁹ Whish, Richard, *Competition Law*, Second edition, London 1989, p. 47.

outcome depends on the specific provisions rather than the economic context of the agreement.⁴⁰

Economically speaking, the question is when competition in reality is being restricted by an agreement. As has been shown above the economic theory says that an undertaking must possess and exercise market power in order to affect competition adversely. Consequently, where no undertaking possesses market power in the market, the agreement cannot restrict competition. It is the impact on the market that should matter. However, the structure of Article 81 EC implies that paragraph 3 contains the elements of economic assessment in order to give exemptions and this is seen to a certain extent illogical, as we will see below. Others think that the scope of Article 81(1) EC is purely academic; the important thing is that an economic assessment is done at some stage.⁴¹

Competition law is in reality application of economics in legal form and the application of economics in EC competition law and especially under Article 81(1) EC has increased the last decade. In the past, the Commission and, to some extent, the ECJ have only applied economic principles in an ad hoc manner.⁴² However, the ECJ has held that an agreement must be assessed in its economic context under Article 81(1) EC. What this means will be analysed below.

5.5 Vertical agreements

It is true that vertical agreements confer restraints on one or both parties of the agreement, but do they restrict competition? The Chicago School has held that no vertical restraint should be subject to competition law, but nowadays economists tend not to make any generalisations.⁴³ Vertical restraints are often used as a substitute for vertical integration and for the same reasons undertakings integrate vertically, undertakings establish vertical agreements. The reasons for vertical integration are that the integration enhance the efficiency of the undertakings operation in some way, either through reducing the transaction costs or by solving difficulties the undertaking is experiencing with external parties. The general approach among economists is that where vertical integration is pro-competitive

⁴⁰ Bishop and Walker, *supra* note 15, p. 75-77.

⁴¹ Bishop and Walker, *supra* note 15, p. 77-78; also Furse, Mark, *supra* note 6, p. 110-111 and 122.

⁴² Bishop and Walker, *supra* note 15, p. vii, xi, 2-3.

⁴³ Furse, Mark, *supra* note 6, p. 102.

the same vertical restraints in an agreement are pro-competitive.⁴⁴ Although the Commission has preferred a formalistic approach to Article 81(1) EC, the Court has on several occasions declared in its judgements⁴⁵ that the applicability of Article 81(1) EC to vertical agreements that lacks a clear anti-competitive intent cannot be assessed by its formal terms.⁴⁶

The effect of vertical agreements differs from horizontal agreements because the products or services complement each other in a vertical relationship, whereas they are substitutes at the horizontal level. In a vertical relationship each undertaking wants the other to lower the price, whereas the incentive is to raise price at the horizontal level.⁴⁷

The possible anti-competitive effect of a vertical restraint is generally not found in the restraint itself, but through the effects the restraint has on the horizontal level. When inter-brand competition or intra-brand competition⁴⁸ is significantly reduced by a vertical restraint it may be considered to be anti-competitive. As said, generally, vertical restraints are not a real concern for competition and an important factor that they in fact are subject to competition law is due to the integration goal of the EU. This is particularly true when considering the circumstances around the famous *Consten and Grundig*⁴⁹ case. This was the first real case where the ECJ dealt with the question if Article 81(1) EC was applicable on vertical restraints.⁵⁰

There are several reasons to way a manufacturer want to impose a vertical restraint on a retailer; usually this is the case when inefficiencies occur. The question is what approach competition law should have towards vertical agreements?⁵¹ The Commission's new view is that vertical agreements are not presumed to be suspicious, but not presumed to fall outside Article 81(1) either. See more about this under chapter 7.1.

⁴⁴ For a good examination of this aspect, see Bork, R. *The Antitrust Paradox, A Policy at War with Itself*, Basics Books, 1978 p. 297-298.

⁴⁵ For example, case *Société Technique Minière*, supra note 5.

⁴⁶ Bishop and Walker, supra note 15, p. 86-87; also Furse, Mark, supra note 6, 102.

⁴⁷ Bishop and Walker, supra note 15, p. 88-89.

⁴⁸ Inter-brand competition means competition between brands and intra-brand competition means competition between the same brands sold in different outlets. Generally, inter-brand competition causes more concern.

⁴⁹ Case *Consten and Grundig*, supra note 5.

⁵⁰ Bishop and Walker, supra note 15, p. 90; also Furse, Mark, supra note 6, p. 102 and 124.

⁵¹ Bishop and Walker, supra note 15, p. 94; also Furse, Mark, supra note 6, p. 157-158.

5.6 Horizontal agreements

There are obvious reasons why horizontal agreements are prone to be more of a concern for effective competition than vertical agreements. However, not all of them constitute obvious restrictions on competition. There are kinds of co-operation agreements that may have efficiency gains. The efficiency gains may be the spreading of costs and risks, sharing expertise etc. This limitation also corresponds to the Commission's Draft Guidelines on the Applicability of Article 81 to Horizontal Co-operation, where agreements on research and development, production, purchasing, commercialisation, standardisation and environment are dealt with.⁵² The hazard with horizontal agreements is the 'inherent' risk of anti-competitive co-operation to the detriment of consumer welfare and the integration goal of the EU. Therefore, the cautiousness is validated because of the risk of spill over effects from otherwise beneficial effects. The fact that the undertakings in question are competitors may be enough for finding an infringement of Article 81(1) EC. Co-operation on the horizontal level tends to lead to co-ordination of commercial policies.⁵³

Co-operative joint ventures are considered to be a legal chameleon. It does not depend on the legal form and a distinction has to be made between co-operative joint ventures and concentrative joint ventures, which are dealt with under the Merger Regulation.⁵⁴

⁵² June 2000, at para 10.

⁵³ Furse, Mark, *supra* note 6, p. 133.

⁵⁴ See the Commission Notice on the concept of concentration (1998) OJ C66/5; Merger Regulation, *supra* note 17.

6 The notion of restriction of competition

6.1 Introduction

Whether or not an agreement restricts competition is and has been the subject for debate among the commentaries. It is argued that the Commission's application of Article 81(1) EC is too wide and misunderstood. Pro-competitive agreements are being dragged in under Article 81(1) EC only to be exempted under Article 81(3) EC resulting in unnecessary burdens on both the undertakings and the Commission. These exemptions are often delivered through comfort letters, which do not deliver enough legal certainty and does not constitute the proper procedure of Regulation 17.⁵⁵ This situation confers a restraint on the commercial freedom due to the formalistic approach of the Commission. This is evident when considering section 4.2 of Form A/B, the notification form, specifically asks for the identification of any provisions contained in the agreements that may restrict the parties' freedom to take independent commercial decisions. Clauses that limit the commercial freedom are, however, neither necessary nor a sufficient condition for the application of Article 81(1) EC. According to some commentators, the ECJ has indicated that Article 81(1) EC is subject to some sort of 'rule of reason' analysis. The Commission on the other hand has tried to distinguish these cases from this approach.⁵⁶

However, the majority can agree on that Article 81(1) EC cannot cover all agreements and this implies that the notion of restriction of competition must have a more narrow meaning. On one extreme side the arguments are that competition can only be restricted where an agreement may possibly harm consumer welfare in the economic sense. The other extreme we have already ruled out. Whish explains the key to this conundrum 'that it is not possible to give an abstract meaning to the expression 'restriction of competition'. Rather, it is necessary to interpret this term in the overall context in which it is used.' Thus, it is implied that there can be no definition on the notion of restriction of competition 'in abstracto'; the notion can only be defined in a specific case.⁵⁷

⁵⁵ Council Regulation 17/62 implementation articles 85 and 86 of the Treaty.

⁵⁶ Faull & Nikpay, *supra* note 23, paras 2.57, 2.77-78.

⁵⁷ Whish, *supra* note 39, quote at p. 45, other p. 44-45.

Mostly the discussion has evolved around whether there should be a rule of reason under Article 81(1) EC. Forrester and Norall have put another approach forward, namely: ‘the lack of actual, predictable application and enforcement of the competition rules in everyday business life...’⁵⁸ The debate about the rule of reason has, therefore, been distorted. In the United States the ‘rule of reason’ contains both the substantive aspect, when deciding on reasonableness, and the procedural aspect, where no official authorisation is necessary. While it is claimed that Article 81(3) EC contains the substantive aspect to decide on reasonableness, the commercial world is more interested in the procedural aspect; the question of whom should decide on the reasonableness. Accordingly, the commercial world wants that businessmen, lawyers and judges should, without any obligation to clear it through a competition authority, examine competition problems.⁵⁹

Comparing the US rule of reason with what is going on under Article 81(1) EC is a complex operation and has to some commentators a doubtful value. As said, the analysis made under Article 81(3) EC is similar to the United States ‘rule of reason’, but the ‘in or out’ differs. A ‘rule of reason’ approach under Article 81(1) EC would remove the Commission’s control and flexibility under Article 81(3) EC and would at the same time reduce the cost of aligning agreements in conformity with the structure of Article 81. In the Modernisation White Paper the Commission admitted that ‘rule of reason’ type arguments have been applied to a limited extent under Article 81(1) EC to a few practices, but stated at the same time that any greater use is prevented by the structure of Article 81 EC.⁶⁰ The Commission is of the opinion that it would be ‘paradoxical’ to cast aside Article 81(3) EC for the benefit of a ‘rule of reason’ under Article 81(1) EC, when Article 81(3) EC contains all the elements of a rule of reason.⁶¹

6.2 The academic debate on the notion of restriction on competition

⁵⁸ Forrester and Norall, *supra* note 3, p. 11.

⁵⁹ *Ibid*, p. 13.

⁶⁰ 1999 White Paper on Modernisation of the Rules Implementing Articles 85 and 86 (now Articles 81 and 82) of the EC Treaty Modernisation White Paper COM/99/101 final, Commission programme 99/27 approved on 28 April 1999 at para 57.

⁶¹ Furse, Mark, *supra* note 6, p. 148-149.

6.2.1 Introduction

The enforcement and compliance of Article 81 EC is held to be conducted in different ways than what the framers of the Treaty expected. No enforcement mechanisms were implemented in the Treaty, but it gave the Council four years to adopt the implementing legislation. Regulation 17⁶² was the result by which the Commission was given the exclusive right to grant exemptions, without any support from the Treaty. Indeed, the transitional provisions in the Treaty gave the authorities in Member States authority to rule on Article 81(3) EC in the mean time. However, that was not the path that was chosen and that is what we have to work with.⁶³

The academic debate on the status of Article 81(1) EC, in reality, contains several topics. Namely: whether or not Article 81(1) EC should contain a rule of reason approach à la United States of America; the question of who should decide on issues of competition; and whether or not the current system can survive as it is. There are of course two sides to this debate. On one end, the arguments are in favour of a ‘rule of reason’ under Article 81(1) EC, alternatively in favour of a stronger economic approach. This position can possibly be divided into two groups, one arguing that the Courts already has applied some kind of ‘rule of reason’ approach in a few cases and one only arguing that there should be a ‘rule of reason’ approach.

The opposing view is, mainly, of the opinion that the structural differences in the antitrust laws of United States and EU hinders a ‘rule of reason’ approach of the kind present in Section 1. However, it may be more correct to state that the same terminology used in the United States cannot be used in EU without conferring misunderstandings and confusion to the notion of restriction of competition in EU. It is held that the ECJ has developed its own notion of restriction of competition in its jurisprudence. In fact, most of the commentaries on the other side have acknowledged this, but they criticises the current system, especially the Commission’s formalistic approach, to score points in favour for a ‘rule of reason’ approach.

6.2.2 Arguments in favour of a rule of reason approach

⁶² Supra note 55.

⁶³ Forrester and Norall, supra note 3, p. 19-20.

Several commentators⁶⁴ have argued that the Commission, and occasionally the Community Courts, have far too often held that agreements, which by their nature are pro-competitive, restrict competition within the meaning of Article 81(1) EC. Especially, the Commission has taken this formalistic approach. It is argued that the possibility to grant an exemption has caused difficulty in the system and has encouraged the Commission and the Courts to adopt a wide interpretation of Article 81(1) EC with the result that many agreements are caught by the prohibition.⁶⁵ If the agreements were analysed in an economic realistic way it would result in less findings of restrictions. However, there is always a possibility for exemption, but that procedure is argued to be time-consuming and costly. Moreover, the element of uncertainty might irritate the beneficial objectives sought.⁶⁶

The illogical application of Article 81 EC is also put forward in this respect. Economic analyses are frequently made to determine if Article 81(3) EC is applicable. The issue here is whether or not, or to what extent, a competitive analysis should be made under Article 81(1) EC. The Commission has granted exemptions under Article 81(3) EC, usually justified by the agreements pro-competitive effects. This leads to the fact that the Commission states that the agreement in question both restricts and promotes competition, which from an economic perspective is unacceptable.⁶⁷ For example, the grant of exclusive territories are said to be necessary under Article 81(3) EC but are still judged as restrictive under Article 81(1) EC. Steindorff stresses that a rule of reason can only exist within Article 81(1) EC and not under 81(3) EC. This is because the rule of reason can only come into effect where not agreements are 'plainly' anti-competitive, but where an assessment is required in order to find a restriction.⁶⁸ The criticism towards the Commission's approach to Article 81(1) is heavy, especially this difficulty to reconcile the Commission's findings under Article 81(1) EC with its findings under Article 81(3) EC. The question put forward then is: How can the obligation have had the object or effect of restricting competition in the first place? Every restriction cannot be anti-competitive because the very nature of an agreement restricts the parties' freedom of action. The lack of

⁶⁴ Hawk, Barry E. 'System Failure: Vertical Restraints and EC Competition Law' (1995) *ECLR* 32, p. 973-989; Korah, *supra* note 4; Bishop and Walker, *supra* note 15; Forrester and Norall, *supra* note 3.

⁶⁵ Korah, Valentine, *An Introductory Guide to EC Competition Law and Practice*, Fifth edition, London 1994, p. 58.

⁶⁶ Which, *supra* note 39, p. 234; also Riley, Alan J. 'Vertical Restraints: A Revolution?' (1998) *ECLR*, p. 484.

⁶⁷ Bishop and Walker, *supra* note 15, p. 101.

⁶⁸ Steindorff, Ernst 'Article 85 and the rule of reason' (1984) *CMLR* 21, p. 642.

economic analysis or sufficient economic analysis in the majority of the Commission's decision is, therefore, considered to be regrettable.⁶⁹ For example, the integration goal includes the idea that undertakings expand into other Member States. A territorial protection then is needed.⁷⁰

Another point made in this respect is that it seems odd with a system where exemptions are the rule. It does not entirely co-insist with the restrictive use of exemptions elsewhere in the Treaty. For example, countries that have imported the EC model of Competition law do conduct the substantive analysis under the prohibition paragraph. A Hungarian official posed the following question: 'does it make more sense to condemn all vertical restraints and then exempt 90 % à la Brussels, or to accept 90% and condemn only 10% à la Budapest?'⁷¹ The presence of an exempting possibility should not be seen as a weakness. It offers a flexibility which the Sherman Act lacks. It is stressed that some kind of rule of reason approach within Article 81(1) EC does not have to mean that Article 81(3) EC would be useless. It should be seen as an advantage to be able to consider certain trade policies.⁷²

The Commission's monopoly to grant exemptions under Article 81(3) EC is a particular problem. A more flexible approach to Article 81(1) EC is required because of the lack of resources in the Commission to have monopoly on giving exemptions. The system with notifications and exemptions has broken down. The Commission is delivering very few formal decisions, which was the sole mechanism of exemption intended by Regulation 17. At the same time the number of notifications are substantial, leaving the Commission with a massive backlog. In order to survive this unbearable situation the Commission introduced two mechanisms. First, block exemptions, clearing the most common agreements that always was subject to an exemption. The objection to this approach has been that they were too legalistic and too narrow in scope making it hard to fit an agreement under a block exemption. However, recently the approach has changed and the new block exemptions are flexible drawn after an economic approach. Secondly, comfort letters, an informal statement of the Commission's broad opinion about the agreement. It is argued that comfort letters may be of little use when market conditions have changed. The fact that very few exemptions are given the formal way, especially those with 'ancillary' restraints, has begun to undermine the

⁶⁹ Hawk, *supra* note 64, p. 974-980.

⁷⁰ Korah, *supra* note 65, p. 57, 269-271.

⁷¹ Hawk, *supra* note 64, p. 980.

⁷² Forrester and Norall, *supra* note 3, p. 41; Peeters, Jan 'The Rule of Reason Revisited: Prohibition on Restraints of Competition in the Sherman Act and the EEC Treaty' in *American Journal of Comparative Law* (1989) Vol. 37, p. 523.

contract law in EU. Korah stated in this regard: ‘Competition law presupposes that there are markets and markets presuppose that there are rights to be traded and that contracts are enforceable. Otherwise products will not flow to their most strongly desired use.’⁷³

If the Commission has monopoly to apply Article 81(3) EC it results in the national authorities and courts inability to grant such exemptions. This inability creates problem that occurs in national courts when parties want to enforce restrictive clauses, which are ‘ancillary’ to an otherwise pro-competitive agreement. Korah said: ‘Unless a national civil court can enforce restrictive clauses that are reasonable ancillary to pro-competitive kinds of collaboration the lack of legal certainty may prevent industry in the common market from keeping up in international markets.’ If an agreement has not been notified before the national proceedings the Commission is unable to grant an exemption.⁷⁴ If then the national court uses the same approach as the Commission to Article 81(1) EC many good agreements would become void under Article 81(2) EC. This is called the ‘Euro-defence’, a defence strategy developed by the current systems flaws. If, on the other hand, the agreement has been notified the national court have to adjourn and await the Commission’s decision. The massive use of comfort letters complicates the picture. They do not bind the national courts, but the letters may be taken into account. Due to that the Commission enjoys monopoly on granting exemptions the parties to an agreement are entitled to insist on a formal exemption.⁷⁵ Therefore, in the case of national proceedings the Commission may be asked to re-open a file, which results in slow litigations. Furthermore, it is said that a bearer of a comfort letter might not be safe due to the inherent uncertainty in a comfort letter. The Commission is entitled to change its opinion when the conditions have changed.⁷⁶

The perhaps strongest pushed argument is that agreements with overall desirable consequences should not be controlled. There are wishes to see a more clear distinction between naked and ancillary or horizontal and vertical restraints in EC competition law. The distinction is needed because of the effects on competition differ depending on the parties relationship. Under the American case law ancillary restrictions need only to be reasonably necessary. The EC approach is stricter, but it is not necessarily the case that there is a difference in substance.

⁷³ Hawk, *supra* note 64, p. 984; Korah, *supra* note 65, p. 58-60, 272-273, 277-279, quote at p. 273; also Whish, *supra* note 39, p. 234.

⁷⁴ This has to some extent changed.

⁷⁵ Case T-28/90 *Automec v. Commission* (No. 2) [1992] 5 CMLR 431.

⁷⁶ Korah, *supra* note 65, p. 273-274, quote at p. 60.

The lack of economic reasoning in the Commission's decision in conjunction with the Courts reluctance to review anything other than a 'manifest error in law' has created an uncertainty which has resulted in difficulties for the legal advisors when businessmen asks what the Commission and the Courts attitude is to their arguments. However, the CFI has showed occasionally that it is more willing to examine the Commission's economic analysis. Furthermore, the lack of legal certainty in the prevailing system has been stressed. The Commission can make changes to, or impose conditions on, agreements sometimes years after they were concluded. The bargain power may then have shifted and clauses in the agreement may enable a party to renegotiate the whole deal in case of partial nullity. This conduct by the Commission has been criticised, especially for not considering this aspect of the contract process and for the failure to give reasons why that particular change is needed.⁷⁷

A common opinion is that restrictions should be untouched whenever sunk costs is incurred and protection from free riders is needed. The Community courts have met this critic to some extent by the introduction of a kind of ancillary restraint doctrine, where restrictions necessary for some lawful purposes falls outside the scope of Article 81(1) EC. Furthermore, it is frequently stressed by the Community Courts that agreements should be assessed in their legal and economic context under Article 81(1) EC. There is, however, a clash occurring in this sense with the block exemptions. Parties to an agreement might never know if they are out of Article 81(1) EC or benefits from a block exemption, especially now with the new block exemptions. Consequently, the Community Courts have cleared a few restrictions when either the market was competitive or the ancillary restraints were necessary. As said a problem is that the Community Courts have no jurisdiction to rehear the cases, only power for judicial reviews.⁷⁸ It is, then, hard to correct the Commission failure to assess agreements in their economic context. Therefore, it is argued that such control should not be conducted by an authority; that task should be left to the businessmen, lawyers and ultimately the Courts.⁷⁹

6.2.3 Arguments against a rule of reason approach

⁷⁷ Hawk, *supra* note 64, p. 983; Korah, *supra* note 65, p. 151, 255, 267-268, 274-276; also Whish, *supra* note 39, p. 234.

⁷⁸ Korah, *supra* note 65, p. 230-234.

⁷⁹ Forrester and Norall, *supra* note 3, p. 13.

The arguments made in this respect target different aspects of why a rule of reason does not belong under Article 81(1) EC. These are related to: the structural differences between Section 1 of the Sherman Act and Article 81 EC; the difference in the procedural approach between the two systems; the different solutions made in the jurisprudence of the notion of restriction on competition respectively the notion of restraint of trade; and the undermining of Article 81(3) EC in the case of a rule of reason approach under Article 81(1) EC. These aspects are also connected to each other.

To wide definition might bring almost every agreement within Article 81(1) EC and too narrow definition would reduce the jurisdiction of the Commission. It is therefore stressed that it is necessary to decide whether Article 81(1) EC is designed to give jurisdiction or if an assessment of individual agreements should take place to determine if a restriction has occurred. Goyder states: 'it is obvious that many more agreements will need scrutiny by the Commission than will ultimately be adjudged to have failed to pass whatever substantive criteria are applied to them. This will not necessarily imply, however, that a 'jurisdictional' Article should be read with total adherence to a strictly literal meaning, bringing within its grasp every kind of agreement or concerted practice with the smallest impact on competition.'⁸⁰ He further says that the ECJ has taken the jurisdictional approach to Article 81(1) EC, but has occasionally narrowed the scope of Article 81(1) EC. To use the American terminology of the rule of reason to this limitation would be misleading since it is not comparable to what is going on under Article 81(1) EC. Section 1 contains both the jurisdictional and the assessment approach whereas the assessment primarily takes place under Article 81(3) EC in EU. Therefore, the discussion of a rule of reason under Article 81(1) EC, which only contains a limited assessment element, would only lead to further confusion. According to Goyder the object of Article 81 EC is to eliminate or reduce the number of agreements, which restricts third parties freedom of choice and to distinguish within this category the agreements, which have beneficial effects of the kind set out in Article 81(3) EC.⁸¹ There must be a careful market analysis of the effect on competition conducted, unless the effect of such restrictions is so obvious that no individual assessment is needed or the agreement is restrictive by object.

The rule of reason under the Sherman Act means that the agreement is assessed in its economic context in order to establish if a restraint of trade exist.

⁸⁰ Goyder, D.G. *EC Competition Law*, Second edition, Oxford 1993, p. 116-117.

⁸¹ *Ibid*, p. 116-118; last sentence also Peeters, *supra* note 72, p. 537-538.

When doing this anti-competitive effects are balanced against the pro-competitive effects and if the end result is pro-competitive the agreement is held to fall outside Section 1. We have already seen why some commentaries are arguing for a rule of reason under Article 81(1) EC pointing at the Community Courts' judgements forms its notion of restriction of competition. It is acknowledged that a more narrow meaning of the notion of restriction of competition has been adopted. However, when analysing the Courts' judgements it is argued that it is evident that there is no correspondence to the American rule of reason. The two competition law systems are materially different and the fact that the Community Courts has delivered 'reasonable judgments does not mean that it has adopted the rule of reason.'⁸² The Community Courts has, therefore developed their own jurisprudence. The ECJ has found some restrictions to be 'ancillary' to legitimate business practices, which falls outside the Article 81(1) EC. This is also the general meaning among the commentators. It is stressed that the ECJ has refused to apply a rule of reason in Article 81(1) EC. It has only used an 'ancillary' approach and 'de minimis' requirements to narrow down the scope for the prohibition. The legitimate business practices are held to be: *exclusive distribution*, where it may be necessary to protect wholesalers from intra-brand competition; *franchising*, where it may be necessary to protect the know-how and image and reputation of the trademark; *selective distribution systems*, where it may be necessary to impose qualitative standards on the wholesalers/retailers; *sale of business*, where a reasonable non-competition restriction on the vendor may be necessary; *exclusive purchasing*, where it may be necessary to limit the retailers ability to purchase from other suppliers; and *exclusive licensing of intellectual property*, where some form of 'open exclusivity' may be needed in case of launching new products.⁸³ This is also the case with joint ventures in very special circumstances.

Korah acknowledged two concepts in order to escape the prohibition. First, that the competition excluded was not possible without the agreement and secondly, that only if the agreement substantially foreclosed other dealers would it infringe Article 81(1) EC. Which has also made a distinction: First, restrictions that are objectively necessary for the attainment of a particular type of agreement. Secondly, when the commercial risk is so great that some exclusivity must be conferred in order to induce him into the market. This distinction is made in respect of that the first categories' restrictions will always be necessary, whereas

⁸² Whish, *supra* note 39, p. 236.

⁸³ Goyder, *supra* note 80, p. 122-123; also Peeters, *supra* note 72, p. 541.

in the latter market analysis is needed in order to decide on the level of exclusivity required.⁸⁴ Similarly, Peeters refers to the market opening concept and the ancillary restraint concept.⁸⁵

The Commission gets support from Peeters when he is declaring that the major difference between the two systems, in United States and EC, is the procedural level. To introduce a rule of reason should therefore not be done without letting go of the exclusive control conferred on the Commission.⁸⁶ Accordingly, the debate of whether there should be a rule of reason is in reality not about the terminology or language, 'it fundamentally concerns who shall interpret and apply the competition rules,' as Forrester and Norall putted it.⁸⁷

6.2.4 Advocate General Lenz in the Bosman case⁸⁸

Advocate General Lenz gave his view on the notion of restriction of competition within the meaning of Article 81(1) EC in the famous Bosman case. This view is considered to be one of the clearest examples of when an agreement may fall outside Article 81(1) EC. The case concerned the UEFA rules on foreign football players and the rules on transfer of football players, which were considered to restrict competition between the football clubs in the sense that the sources of supply became limited and that transfer fees restricted the possibility for football clubs to attain players. Both UEFA and the Italian government argued that the restrictions in question were overall pro-competitive. They referred to the 'rule of reason' to support the opinion that the restriction would fall outside the reach of Article 81(1) EC. For this reason Advocate General Lenz explored the possibilities of using a rule of reason approach under Article 81(1) EC. Advocate General Lenz began to state that the United States antitrust law did not have any possibility of exemption by an official decision and faced with those prerequisites the 'rule of reason' was developed in the United States. The differences between the legal systems did not allow the US doctrine to be implemented under Article 81(1) EC and no case law had until that date proven otherwise. '[O]nly restrictions of competition which are *indispensable* for attaining the legitimate

⁸⁴ Whish, *supra* note 39, p. 236-238.

⁸⁵ Peeters, *supra* note 72, p. 567.

⁸⁶ Peeters, *supra* note 72, p. 535.

⁸⁷ Forrester and Norall, *supra* note 3, p. 37.

⁸⁸ Case C-415/93 Union Royal Belge des Societes de Football Association ASBL v. Jean-Marc Bosman [1995] ECR I-4921 at paras 262-269.

objectives pursued by them do not fall within Article 85(1) [now Article 81(1)],⁸⁹ he concluded. He referred to three cases to prove his point. First, in *Remia*⁹⁰ a non-competition clause in the event of the sale of an undertaking is considered to be indispensable for the legitimate objective ‘the sale of an undertaking’ as long as the duration of the clause is reasonable. Secondly, in *STM*⁹¹ the ECJ declared that when the competition to be protected would not be possible at all without the restraints Article 81(1) EC did not apply. Finally, in *Gottrup-Klim*⁹² the ECJ stated that a prohibition of dual membership in co-operative associations in direct competition with each other did not necessarily restrict competition within the meaning of Article 81(1) EC and might in fact have beneficial effects on competition. This, according to Advocate General Lenz, shows that the Court ‘attach[es] weight to the concerns on which the rule of reason doctrine is based.’⁹³ However, the bound of such concerns under Article 81(1) EC is also shown, when the Court continued and stated that such restrictions would only escape the prohibition if they were ‘necessary’ to ensure the proper function of the co-operative association in the sense that it maintained its contractual power.

6.3 Object or effect and appreciability

The requirement that an agreement must have as its ‘object or effect’ the restriction of competition in Article 81(1) EC is alternative and not cumulative. First it is necessary to determine the purpose of an agreement and only if the object of the agreement were not sufficiently clear it would be necessary to assess the effects of an agreement. Furthermore, the question if an agreement is restrictive by object does not refer to the subjective intent of the undertakings, but to terms of the agreement and in which economic context it was concluded. Once object has been established there is no need to show any effect of the agreement. Mainly this is the case only for the ‘hard core’ objectives.⁹⁴ Restriction by effect is more relevant for the purpose of this thesis, where a more exhaustive analysis is needed. This will be further analysed below.

⁸⁹ Ibid, at para 269.

⁹⁰ Case 42/84 *Remia v. Commission* [1985] ECR 2545 at para 20.

⁹¹ *Société Technique Minière*, supra note 5, at p. 250.

⁹² Case C-250/92/82 *Gottrup-Klim v. Dansk Landbrugs Grov-vareselskab* [1994] ECR I-5641 at paras 31-36.

⁹³ *Bosman*, supra note 88 at para 269.

⁹⁴ Case 45/85 *VdS v. Commission* [1988] 4 CMLR 264 at para 39; *Faull & Nikpay*, supra note 23, paras 2.60-61; *Furse*, supra note 6, p. 119-120; *Whish*, supra note 39, p. 230; and *Goyder*, supra note 80, p.119-120.

According to the jurisprudence the effect on competition must be appreciable in order to fall under Article 81(1) EC. This view does not correspond in any way to the rule of reason in the sense that the restraint may be reasonable. While the appreciability to a large extent rests on a formalistic approach, in the form of a low market share threshold, the rule of reason rests on a full fledged economic analysis. Thus, even if an agreement is restrictive by object some economic analysis is needed to determine if it has an appreciable effect on competition. In the *Völk* case⁹⁵ a vertical exclusive distribution system conferring absolute territorial protection fell outside the scope of Article 81(1) EC. The agreement was restrictive by object, but the producer's market share was only 0.6 percent and had, consequently, 'an insignificant' effect on the market. The Notice on agreements of minor importance, the 'de minimis' notice,⁹⁶ introduced market share thresholds on the application of Article 81(1) EC. For horizontal agreements the aggregated market shares cannot exceed five percent, respectively ten percent for vertical agreements. In case of uncertainty in the classification of an agreement five percent prevails. However, these thresholds are only guidelines and can conversely differ in a specific case. Thus, there is a grey zone around these thresholds. Furthermore, Article 81(1) EC does not automatically apply when the thresholds are exceeded. Adequate reasons must also be provided for the application of Article 81(1) EC.⁹⁷

6.4 The ancillary restraint doctrine

Even if there are clauses that restrict the rivalry between undertakings the agreement may fall outside the scope of Article 81(1) EC if the clauses are objectively necessary for the implementation of a lawful agreement. This is known as the ancillary restraint doctrine. For reason of clarity ancillary restraints are restraints, which are directly related to the agreement, objectively necessary for its existence and at the same time subordinate in importance to the main purpose of the agreement. Furthermore, it seems that the ancillary restraint doctrine may not

⁹⁵ Case 5/69 *Frantz Völk v. Ets Vervaecke SPRL* [1969] CMRL 273 at para 3; also Case 22/71 *Beguelin* [1971] ECR 949 at para 16.

⁹⁶ Commission Notice on agreements of minor importance which do not fall under Article 85(1) of the Treaty establishing the EC OJ (1997) C 372/13.

⁹⁷ Case T-374/94 *European Nigh Services v. Commission* [1998] ECR II-3141 at para 102; *Faull & Nikpay*, supra note 23, paras 2.82-86; *Furse*, supra note 6, p. 146-147; *Whish*, supra note 39, p. 231.

apply to all types of restraints or even to the same restraint in slightly different environments.

In order for an agreement to be able to receive an exemption under Article 81(3) EC, besides the generation of benefits of which a fair share are passed on to the consumers, the restrictive provisions must be indispensable to the attainment of those benefits. This criterion is very similar to the ancillary restraint doctrine or a narrow form of the rule of reason. The difference may not be apparent in results, but in ‘academics’. The indispensability test analyse whether or not the provision is necessary for the attainment of the benefits intended whereas the ancillary restraints doctrine analyse whether or not the provision is necessary for the existence and implementation of the agreement. There is a hazard in relying on the ancillary restraint doctrine from a legal certainty perspective. You may never know when it is appropriate to use the doctrine due to the inconsistency in its application. The lack of case law on these issues under Article 81(1) EC complicates the picture further.⁹⁸

6.5 Restriction of competition – a case study

The case study deals with the cases or decisions that are particular important for the notion of ‘restriction of competition’. The cases will be presented under their ‘legitimate business practice’ heading. These are: exclusive distribution agreements, selective distribution agreements, exclusive purchasing agreements, franchising, sale of businesses, licensing of intellectual property, and co-operative joint ventures. It is all about grasping market opportunities.

6.5.1 Exclusive distribution agreements

The rationale behind an exclusive distribution agreement is that a producer agrees to supply a sole distributor in a particular territory. In order to get a distributor to market a product in the particular area it may want some protection from other distributors to be able to endure the cost of marketing. This can be done by imposing some level of export bans on the producer’s distributors or by designate trademark rights to the distributor in the particular territory. It might also be beneficial to the producer in the sense that he does not have to distribute to

⁹⁸ Faull & Nikpay, *supra* note 23, paras 2.87-93, 2.165-168; Furse, *supra* note 6, p. 123-124.

multiple retailers, which reduces his transport costs.⁹⁹ According to economic theory anti-competitive effects may occur in such a situation if intra-brand competition is significantly reduced by the low number of supplied retailers in a market with weak inter-brand competition.¹⁰⁰ However, the Commission has often taken a formalistic approach towards exclusive territories without considering the economic context.^{101 102} Exclusive distribution agreements have been subject for the first judgements by the ECJ on the application of Article 81(1) EC.

6.5.1.1 *Consten and Grundig*¹⁰³

This case is still considered to be a significant key case in respect to vertical restraints despite the fact that it is a judgement from 1966. Grundig, a German manufacturer of radio, TV and recording equipment, had concluded an exclusive distribution agreement with the French wholesaler Consten. Consten was given absolute territorial protection in France. To obtain such a protection Grundig imposed an export ban, both directly and indirectly, on Consten and its other wholesalers and at the same time prohibited itself to supply any other than Consten in France. A supplementary agreement was also signed to further reinforce the exclusivity, giving Consten the right to the special trademark GINT, Grundig International, in France. In return, Consten was required to minimum purchases, to adequately promote the products and to provide adequate after-sales service including holding a supply of spare parts. Another firm, UNEF, was able to obtain Grundig products despite the export ban and sold them into France cheaper than Consten. Consten brought actions against UNEF, both under the French law on unfair competition and in respect for infringement of the GINT trademark. The French court proceeding was put on hold when UNEF had complained to the Commission claiming an infringement of Article 81(1) EC. Grundig then notified the agreement to the Commission seeking a negative clearance or an exemption if Article 81(1) EC was to be infringed. The Commission declared the agreement along with the assigned trademark contrary to Article 81(1) EC.¹⁰⁴ Both Consten and Grundig appealed the Commission's

⁹⁹ Craig, de Búrca, *supra* note 2, p. 926.

¹⁰⁰ Bishop and Walker, *supra* note 15, p. 92.

¹⁰¹ For example, Commission decision IV/32.290 Newitt/Dunlop Slazenger [1992] OJ L131/32.

¹⁰² Craig, de Búrca, *supra* note 2, p. 926-27; also Bishop and Walker, *supra* note 15, p. 90-91.

¹⁰³ Consten and Grundig, *supra* note 5.

¹⁰⁴ Decision of 23 September 1964 Re Grundig's Agreement 64/566/EEC [1964] CMLR 489.

decision and had support from the intervening governments of Italy and Germany basing itself upon the ‘rule of reason’.

An important discussion about the applicability of Article 81(1) EC on vertical restraints was held in the opinion of Advocate General Karl Roemer. He was troubled by the fact that the Commission only had addressed the object and not the effect of the agreement. He felt that Article 81(1) EC required a comparison between the market situation with and without the agreement in order to assess the effects of the agreement. An exclusive distributor can be the only way of effectively entering a market and in this case the Advocate General Karl Roemer indicated that without the exclusivity imposed by the agreement the offer of Grundig’s products in France would have been ‘noticeable’ reduced.

The German government argued that the focus on competition was misguided. The Commission had only focused on intra-brand competition effects and Advocate General Karl Roemer was of the opinion that this negligence of inter-brand competition was wrong. In fact, competition from other similar brands was intense and a study showed that price on Grundig’s products had decreased occasionally in regard to this. Therefore, the Advocate General Karl Roemer felt that the Commission’s reasoning was insufficiently based in regard to restriction of competition within the meaning of Article 81(1) EC.

On the question whether Article 81(1) EC was applicable to vertical restraints the ECJ referred to the Treaty text, which did not make any distinction between vertical and horizontal agreements and concluded therefore that in principle no distinction should be made where the Treaty does not make any distinction. In regard to the sole focus on the object of the agreement the ECJ referred to the basic aim of the Treaty, namely the integration goal. When the aim is to suppress the barriers between the Member States, private undertakings cannot be allowed to restore such barriers. On the German government’s argument that sufficient inter-brand competition would take away the negative effects on intra-brand competition the ECJ answered:

“Although competition between producers is generally more noticeable than that between distributors of the same make, it does not thereby follow that an agreement tending to restrict the latter kind of competition should escape the prohibition of article 85(1) [now Article 81(1)] merely because it might increase the former.”¹⁰⁵

The ECJ also stated the following concerning the interpretation of Article 81(1) EC:

¹⁰⁵ Consten and Grundig, supra note 5, at p. 342.

“The decisive criterion for the coming into force of the prohibition mentioned in Article 85(1) [now Article 81(1)]...consists of the finding that the agreement interferes with the freedom of action of the parties or with the position of third parties on the market not only in a theoretical but also in a perceptible manner.”¹⁰⁶

The ECJ upheld the findings of the Commission, but partly annulled the decision in the sense that, in this case, only the restrictive clauses could be condemned and not the entire agreement.

6.5.1.2 *Société Technique Minière*¹⁰⁷

Société Technique Minière (STM) had the exclusive right to sell grading equipment in France produced by the German undertaking MBU. The agreement was an exclusive distribution agreement similar to the one used in *Grundig*, but did not impose any export bans and thus parallel trade was not hindered. After a dispute between STM and MBU, STM decided to argue that the ‘Euro-defence’, that is claiming an infringement under Article 81(1) EC with the result of automatic nullity of the agreement under Article 81(2) EC. If an agreement has not been notified it cannot get an exemption under Article 81(3) EC. The national court asked for a preliminary ruling.

The ECJ began by stating that the notion of object or effect is alternative requirements. Therefore, there is a need to establish the purpose of the agreement in the economic context in which it is to be applied. Furthermore, the restriction of competition must follow from all or some of the provisions in the agreement and where the effect of such clauses does not seem to be ‘sufficiently deleterious’ a more thorough analysis is needed to establish if competition has been restricted. When the actual context in which the agreement would apply is assessed then the clause ‘granting an exclusive right of sale’ can be assessed to decide whether or not it is a prohibition by object or effect. However, said the ECJ:

“...it may be doubted whether there is an interference with competition if the said agreement seems really necessary for the penetration of a new area by an undertaking.”¹⁰⁸

¹⁰⁶ Consten and Grundig, supra note 5, at p.326.

¹⁰⁷ *Société Technique Minière*, supra note 5.

¹⁰⁸ *Ibid*, p. 250.

6.5.1.3 Concluding remarks

The aim of the agreement was, according to the ECJ, to isolate the French market through the imposing of an absolute territorial protection and thus constituted a restriction by object. It was acknowledged that the ECJ did not see the need for an economic analysis of the relationship between inter- and intra-brand competition when the agreement had as its object the restriction of competition, while Korah is of the opinion that the ECJ was wrong in not consider inter-brand competition. She even suggested that the ECJ had developed a ‘per se’ rule against absolute territorial protection.¹⁰⁹ Amato compared the judgement with what was going on in the United States at the time. The ECJ stated that ‘competition among wholesale distributors of products of the same make enlivens the downstream market of sales to final consumers.’ The United States courts at that time, later overruled in the *Sylvania* case,¹¹⁰ protected intra-brand competition for the right of wholesalers or retailers to exercise freedom of trade without restraints. The ECJ, however, did it for two reasons according to Amato. The explicit reason was protection of competition on all market levels, while the implicit reason was the higher goal of market integration, especially when the absolute territorial protection followed the borders of Member States.¹¹¹ This approach towards vertical restraints had enormous consequences in all fields of distribution. Suddenly, a large number of common agreements were prohibited.¹¹²

Although *STM* seems to be referred to as the case that first clarified the terms ‘object or effect’, which to some opened the scope for the rule of reason. *STM* does not confer, in the author’s opinion, some sort of rule of reason.¹¹³ The Court stated that ‘the competition in question must be understood within the actual context in which it would occur in the absence of the agreement in dispute.’¹¹⁴ Similarly in *Brasserie de Haecht*: ‘Thus, in order to examine whether it is caught by Article 85(1) [now Article 81(1)] an agreement cannot be examined in isolation from the above context, that is, from the factual or legal circumstances causing it to prevent, restrict or distort competition.’¹¹⁵ By this the ECJ meant that the competitive context in the market must be vigorously assessed when the effects of an agreement is not ‘sufficiently deleterious’, in order to see if the ‘said

¹⁰⁹ Peeters, supra note 72, p. 537-538; Korah, supra note 4, p. 354.

¹¹⁰ *Continental TV Inc. V. GTE Sylvania Inc.* 433 US 36 (1977).

¹¹¹ Amato, Giuliano, *Antitrust and the Bounds of Power – The dilemma of liberal democracy in the history of the market*, Oxford 1997, p. 48-49.

¹¹² Forrester and Norall, supra note 3, p. 24.

¹¹³ See Faull & Nikpay, supra note 23, paras 2.71-76.

¹¹⁴ *STM*, supra note 5, p. 249.

¹¹⁵ *Case 23/67 Brasserie de Haecht v. Wilkin* [1967] ECR 407 at 415.

agreement seems really necessary for the penetration of a new area by an undertaking'. Contrary to *Consten and Grundig*, *STM* was a preliminary ruling. The ECJ could not judge the specific case; just give guidelines on the interpretation of the law governing the situation. In this judgement the ECJ opens the door for what appears to be some sort of ancillary restraints doctrine by the phrase: 'in particular it may be doubted whether there is an interference with competition if the said agreement seems really necessary for the penetration of a new area by an undertaking'.¹¹⁶ Consequently, you cannot really tell if an agreement is restrictive by object or effect without an assessment of the economic context, if it is not an obvious restriction by object as in *Consten and Grundig*. *Consten and Grundig* should, therefore, not be read as rejecting economic analysis within Article 81(1) EC, but rather as that such analyses are not needed in the case of an absolute territorial protection.

Thus, export bans will be judged seriously, as any attempt to confer absolute territorial protection. The block exemption on vertical restraints¹¹⁷ allows the obligation that the supplier himself is restricted from selling elsewhere into the particular territory along with restrictions on active sales on the distributors. Such restraints, however, does not necessarily even fall under the prohibition in Article 81(1) EC according to the ECJ's jurisprudence.¹¹⁸

6.5.2 Selective distribution agreements

Some manufacturers demand that its distributors invest heavily in some service connected with the product, often to cure inefficiencies. Economic theory identifies the problem as 'risk of free-riding'. If some retailers offer pre-sales services then other retailers can take advantage of the situation without having to endure the cost of having pre-sale services. The result would be that no retailer would have an incentive to offer the needed services to the detriment of both the consumers, they would not get the necessary help, and the manufacturers, the demand would decrease. Selective distribution resolves the inefficiency problem by only supplying to retailers who offers pre-sale services. The producer simply chooses to supply only certain distributors that meet the producer's criteria.¹¹⁹

¹¹⁶ *STM*, supra note 5, p. 250.

¹¹⁷ Commission Regulation No 2790/99 of 22 December 1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices, Article 4.

¹¹⁸ Craig, de Búrca, supra note 2, p. 911, 927-928.

¹¹⁹ Bishop and Walker, supra note 15, p. 90-91.

6.5.2.1 *Metro I*¹²⁰

SABA had set up a selective distribution system. SABA manufactured TV, radio and tape-recording equipment. The products were sold through specialist wholesalers and retailers within the Community. Some wholesalers were SABA subsidiaries and some were sole wholesalers and there were close co-operations between SABA and its wholesalers in order to plan the activities. The selective distribution system was arranged as follows: SABA products could only be sold by a limited number of selected dealers at each level of distribution. The selection was made according to general qualitative criteria and in addition according to the willingness to perform particular sales promotion and marketing services. The dealers were prohibited from selling SABA products outside the SABA network, dealing with competing products and from setting up branches outside their own territory. The proceedings were initiated by a complaint by Metro, a self-service wholesaler, which did not meet the requirements.

According to the Commission the restrictions not to sell outside the SABA system, imposed both on SABA and its dealers, restricted the commercial freedom and, therefore, constituted a restriction of competition to a perceptible degree. To qualify for a SABA dealer not only qualitative criteria needed to be met, but also a range of quantitative criteria. Therefore, qualified dealers who did not meet, or did not want to meet, the quantitative criteria were unable to deal with SABA products. The Commission granted an exemption.¹²¹

Metro was not happy with the Commission's decision exempting SABA's selective distribution agreements and appealed to the ECJ to get the decision annulled. Metro was a German self-service wholesaler with a cash-and-carry service, which enabled it to undercut the prices charged by other wholesalers. The ECJ upheld the Commission's decision. They sought that the market structure, high quality and technically advanced consumer durables, allowed a variety of distribution channels adapted to the specific characteristics and requirements of producers and consumers. With this in mind the ECJ said the following:

“...selective distribution systems constituted, together with others, an aspect of competition which accords with Article 85(1) [now Article 81(1)], provided that resellers are chosen on the basis of objective criteria of a qualitative nature relating to the technical qualifications of the reseller and his staff and suitability of his trading premises and that

¹²⁰ Case 26/76 *Metro-SB-Großmärkte GmBh & Co KG v. Commission and SABA* [1977] ECR 1875.

¹²¹ Commission decision of December 15 1975, *SABA*, OJ L28/19 [1976] 1 CMLR D61.

such conditions are laid down uniformly for all potential resellers and are not applied in a discriminatory fashion.”¹²²

Further obligations imposed by the agreement, the quantitative criteria, were not ‘justifiable by the needs of adequate distribution of the products concerned’ and constitutes a restriction of competition within the meaning of Article 81(1) EC. These restraints were evaluated and exempted under Article 81(3) EC.

In relation to the exemption the ECJ recognised that price competition could be reduced using selective distribution agreements, but absolute priority must not in all circumstances be accorded to that form of competition, as there are other effective forms of competition. Article 81(3) EC requires the maintenance of workable competition, which might include the safeguarding of different objectives. Thus, restrictions of competition are allowed if they are indispensable for the attainment of those objectives.

6.5.2.2 *Metro II*¹²³

The exemption granted had expired and SABA had got a renewal from the Commission, which again, Metro challenged. After the initial exemption was granted, SABA lifted the obligation of not selling outside the SABA system. It was enough that the outside dealers met the qualitative criteria. The reason for Metro’s appeal was that there had been a significant increase in the number of selective distribution agreements, which had the effect of eliminating wholesalers such as Metro from the relevant market. To this remark the ECJ stated:

“...the existence of a large number of selective distribution systems for particular product does not in itself permit the conclusion that competition is restricted or distorted. Nor is the existence of such systems decisive as regards the granting or refusal of an exemption under Article 85(3) [now Article 81(3)], since the only factor to be taken into consideration in that regard is the effect which such systems actually have on the competitive situation.”¹²⁴

The ECJ upheld the Commission’s exemption again.

6.5.2.3 *Concluding remarks*

¹²² Metro I, supra note 120, para 20.

¹²³ Case 75/84 Metro SB-Großmärkte GmbH & Co KG v. Commission (No. 2) [1986] ECR 3021.

¹²⁴ Ibid, para 41.

In order to escape the prohibition in Article 81(1) EC with a selective distribution agreement the following requirements have to be met: First, the product has to be of such kind that can justify a selective distribution system. The Commission or the Court has justified products that require specialist staff¹²⁵ and products where brand image is important.¹²⁶ Secondly, the retailer must be chosen on the basis of objective criteria of a qualitative nature. For example, the obligation not to sell outside the system was a restriction in the sense that qualitative qualified dealers could not deal with SABA products and not only that it restricted the commercial freedom of the parties. Finally, the agreements can never confer absolute territorial protection.

There seems to be a greater leniency by the Commission towards selective distribution agreements than to exclusive distribution agreements. This is explained by the integration goal of the Community as the latter confer greater risks of dividing markets along the national border than the former. However, compared to franchise agreements it is the other way around. Provisions cleared in franchise agreements may not even benefit from an exemption in a selective distribution system.¹²⁷ This difference may, however, be illusory by the fact that the restriction in hand has to be assessed in its economic context. Therefore, different outcomes should not raise that much concern.

Regarding the cumulative effects of selective distribution agreements it has been argued that it seems odd that the last agreement might be prohibited or that the entry of the last agreement takes all agreements into the prohibition.¹²⁸

6.5.3 Exclusive purchasing agreements

Exclusive purchasing is when one party to an exclusive purchasing agreement undertakes to buy all it needs of a product from a specific supplier. This is a normal conduct for petrol stations and public beer houses. However, there exist a possibility to use vertical restraints purely for anti-competitive reasons, especially

¹²⁵ Such as electronic equipment in case 107/82 AEG-Telefunken AG v. Commission [1983] ECR 3151; audiovisual equipment in case 210/81 Demo-Studio Schmidt v. Commission [1983] ECR 3045; and computers in Commission Decision 84/233 IBM Personal Computers [1984] OJ L118/24.

¹²⁶ Such as ceramic tableware in Commission Decision 85/616 Villeroy & Boch [1985] OJ L376/15; jewellery in Commission decision 83/610 Murat [1983] OJ L 348/20; and luxury cosmetics in case T-19/92 Groupement d'Achat Edouard Leclerc v. Commission [1997] 4 CMLR 612.

¹²⁷ Hawk, *supra* note 64, p. 985.

¹²⁸ Craig, de Búrca, *supra* note 2, p. 930-933.

when used to foreclose markets. A manufacturer might want to avoid inter-brand competition on the retail level. To accomplish this the manufacturer can sign exclusive dealership agreements or exclusive distribution agreements with all the retailers or at least with the best retailers, which makes it difficult for new producers to enter the market with their products. If there are barriers of entry into retailing as well the impact can be huge.¹²⁹

6.5.3.1 *Delimitis*¹³⁰

Exclusive purchasing is very common in the beer supply market, which was the subject in this case. The beer supplier Henninger Bräu had let a beer house to Delimitis and had imposed an obligation to buy all the beer sold in the beer house from Henninger Bräu in an exclusive purchase agreement. Delimitis was also required to buy a fixed quantity of beer, although he was allowed to buy beer from other countries. Delimitis obtained the premises of a fully equipped beer house and in return Henninger Bräu obtained a guaranteed outlet for its beer. A dispute arose at the time of termination of the agreement about the amount of money Delimitis owed Henninger Bräu. The German national court referred questions about the applicability of Article 81(1) EC on the matter.

The ECJ then quoted its judgement in *Brasserie De Haecht*¹³¹ where it had stated that ‘the effect of such agreement had to be assessed in the context in which they occur and where they might combine with others to have a cumulative effect on competition.’¹³² Furthermore, the cumulative effect was said to be only one factor amongst others, pertaining to the economic and legal context in which an agreement must be assessed, capable of foreclosing the market. Especially, the real concrete possibility to penetrate the bundle of agreements and the conditions under which competitive forces operated in the market must be examined. If the examination of the other factors present in the market showed that the cumulative effect of the agreements were not the reason for hindering market access for national and foreign competitors ‘the individual agreements comprising the bundle of agreements cannot be held to restrict competition within the meaning of’¹³³ Article 81(1) EC. If, on the other hand, the cumulative effect was the reason for foreclosure of the market the agreements imposed by a single brewery must

¹²⁹ Bishop and Walker, *supra* note 15, p. 92-94.

¹³⁰ Case C-234/89 *Stergios Delimitis v. Henninger Bräu AG* [1991] ECR I-935.

¹³¹ *Brasserie De Haecht*, *supra* note 115.

¹³² *Delimitis*, *supra* note 130, para 14.

¹³³ *Ibid*, para 23.

contribute to an appreciable extent to the cumulative effect to be caught by the prohibition in Article 81(1) EC. Consequently, the market position of the competitors must be assessed and, furthermore, the duration of the single brewery's agreements were important to really assess the foreclosure effect. The ECJ's answer to the national court was as follows:

“...a beer supply agreement is prohibited by Article 85(1) [now Article 81(1)] of the EEC Treaty, if two cumulative conditions are met. The first is that, having regard to the economic and legal context of the agreement at issue, it is difficult for competitors who could enter the market or increase their market share to gain access to the national market for the distribution of beer in premises for the sale and consumption of drinks. The fact that, in that market, the agreement in issue is one of a number of similar agreements having a cumulative effect on competition constitutes only one factor amongst others in assessing whether access to that market is indeed difficult. The second condition is that the agreement in question must make a significant contribution to the sealing-off effect brought about by the totality of those agreements in their economic and legal context. The extent of the contribution made by the individual agreement depends on the position of the contracting parties in the relevant market and on the duration of the agreement.”¹³⁴

The possibility to buy beer from other Member States diminished the tying effect unless the real possibility to do so were small, for example, if the minimum purchase requirement covered most of the capacity of the bar.

6.5.3.2 *Langnese-Iglo*¹³⁵

Mars had complained to the Commission about the difficulty to access the German market for impulse ice creams, sold in individual portions ready for immediate consumption. This because the undertakings Schöller and Langnese-Iglo had provided special freezers to many small outlets and had in return imposed an obligation on the retailers either not to store others ice cream in the provided freezer or not to sell others ice cream at all. The Commission had concluded that the agreements restricted inter-brand competition within the relevant market due to fact that the market share of the undertakings exceeded the market share threshold expressed in its Notice on Agreements of Minor Importance and thereby automatically fell into Article 81(1) EC. On appeal, the CFI considered the question whether the network of exclusive purchasing agreements fell into Article 81(1) EC.

¹³⁴ Ibid, para 27.

¹³⁵ Case T-7/93 *Langnese-Iglo GmbH v. Commission* [1995] ECR II-1533.

The CFI struck down on the Commission's use and interpretation of the Notice on Agreements of Minor Importance and declared that the notice is only intended to define those agreements that do not have an appreciable effect on competition. Thus, the notice could not with certainty imply that agreements not covered by it automatically restricted competition. The CFI then quoted the ECJ's judgements in *Delimitis* and *Brasserie de Haecht*, which required an assessment of the economic and legal context of the agreements. However, the CFI found that the agreements had an appreciable effect on competition and were caught by the prohibition in Article 81(1) EC. This mainly because of: the network effect of the two undertakings exceeded the tie-in of 30 percent of the relevant market; the obligation to use the provided freezers exclusively for the applicants products, which forced possible new entrants to either persuade the retailer to exchange the freezer installed by the applicant or to install an additional freezer into often very limited store space; a possible entrant with a limited product range would have trouble of persuading the retailer to terminate its agreement to be able to enter the market; the need to have access to a large number of retailers to be able to have a profitable distribution system; the lack of wholesalers in this segment of the market; the average duration of the agreements was two and a half years; and the applicants product brands were very well-known.

6.5.3.3 *Concluding remarks*

Beer and petrol differs from ice cream. In the former big investments are made by the supplier in the retailers business, which validates the tie for a while, when on the other hand a freezer does not seem to be much of an investment. What has the CFI done? Just followed the instructions in *Delimitis* to be safe? There seems not to be a legitimate aim in *Langnese-Iglo* as the ECJ's notion of ancillary restraints seems to require. To see why this case must be assessed as in the *Delimitis*, on the other hand, depends on the assessment of the relevant market that was limited to impulse ice cream purchase in special freezers. That is the whole market that should be assessed and not the entire store; even if other ice creams are sold there they do not gain access to the relevant market. In that sense it theoretically comes up on the same level as the *Delimitis* case where the obligation imposed applies for the whole bar. Still, is such a conduct really a legitimate business practice in the sense that the 'ancillary' restraints doctrine should be applied? In the authors mind the cumulative use of such agreements, in

this specific case, was on the border to be restrictive by object, provided that the relevant market was correctly assessed and slightly predictable.

6.5.4 Licensing of intellectual property rights

Licensing of intellectual property rights or technology transfer agreements are needed in the sense that they are important to let the consumers enjoy and have access to the protected rights. The existence of an intellectual property right is untouchable, but the exercise thereof is not. The essence of an intellectual property right is to grant absolute protection from third parties to the specific right; a feature competition law generally is designed to fight. However, the licensing of intellectual property rights is similar to exclusive distribution agreements in function.

Technology transfer agreements have been treated generally to fall within Article 81(1) EC, unless the licence only confirms the existence of a right.¹³⁶

6.5.4.1 Nungesser¹³⁷

The case concerned licensing of intellectual property rights. The French research institute INRA, specialized in the development of plant seeds, had licensed the right to new hybrid maize seed to the German supplier Eisele. The licensing agreement gave Eisele absolute territorial protection, a protection Nungesser also enjoyed through Eisele. INRA was obliged not to sell the seed to any other undertaking in Germany and had imposed an export ban on other licensees. As in the Consten and Grundig case, Eisele could use the plant breeder INRA's property right assigned to him to prevent third parties from selling into Germany. The Commission declared the agreement to be prohibited under Article 81(1) EC. On appeal, the applicants argued that the restraints imposed were necessary for the ability to access a new market with a new product in order to compete with existing interchangeable products. It was claimed that no undertaking would risk launching a new product without protection from competition from both the licensor and other licensees.

¹³⁶ Last sentence, Furse, Mark, *supra* note 6, p. 157-158.

¹³⁷ Case 258/78 L. C. Nungesser KG and Kurt Eisele v. Commission [1982] ECR 2015.

The ECJ, addressed with this issue, distinguished between an open exclusive licence and a closed exclusive licence, where the former only confer protection from the owner not to sell or licence the product in the assigned territory. After concluding the fact that INRA had spent years on research and experimentation to develop the new hybrid maize seed, which was unknown in the German market at the date of signing, justified the concern of the applicants, the ECJ stated:

“...in the case of a licence of breeders’ rights over hybrid maize seeds newly developed in one Member State, an undertaking in another Member State which was not certain that it would not encounter competition from other licensees for the territory granted to it, or from the owner of the right himself, might be deterred from accepting the risk of cultivating and marketing that product; such a result would be damaging to the dissemination of a new technology and would prejudice competition in the Community between the new product and similar existing products. Having regard to the specific nature of the products in question, the Court concludes that, in a case such as the present, the grant of an open exclusive licence, that is to say a licence which does not affect the position of third parties such as parallel importers and licensees for other territories, is not in itself incompatible with Article 85(1) [now Article 81(1)] of the Treaty.”¹³⁸

The clauses imposing the export ban to make the protection absolute, however, fell under the prohibition of Article 81(1) EC as in the *Consten and Grundig* case.

6.5.4.2 *Coditel II*¹³⁹

The *Coditel II* judgement was delivered a few months after the judgement in *Nungesser*. The case concerned licence agreements of intellectual property in the film industry. *Les Films la Boétie*, owner of all rights in the film ‘*Le Boucher*’ assigned the exclusive right to distribute the film in Belgium to *Ciné Vog Films* for a period of seven years. The German television, in the beginning of this period, broadcast the film on their first channel, which could also be seen in Belgium. *Ciné Vog Films*, in the believe that the commercial future of the film had been hampered, brought actions against both *Les Films la Boétie* and the *Coditel* companies arguing infringement of copyright. *Coditel* argued, on the other hand, that the exclusive licence agreement fell under Article 81(1) EC and was automatically void. The Belgian court asked for a preliminary ruling. In *Coditel I*¹⁴⁰ the ECJ only dealt with the question on the free movement, where it declared

¹³⁸ *Ibid*, paras 57-58.

¹³⁹ Case 262/81 *Coditel SA, Compagnie générale pour la diffusion de la television v. Ciné-Vog Films* [1982] ECR 3381.

¹⁴⁰ Case 62/79 *Coditel v. Ciné Vog Films* [1980] ECR 881.

that the national rules protecting intellectual property rights and the exercise of these rights did not constitute a disguised restriction on the freedom to provide services within the meaning of Article 49 EC. In the financing of a film an exclusive distributor often makes an advance payment and is compensated by keeping a percentage in the cinemas.

The ECJ looked at the characteristics of the cinematographic industry as the dubbing and subtitling, the possibilities of television broadcasts and the system of financing film production and concluded that an exclusive licence ‘is not, in itself, such as to’ restrict competition. The answer given to the national court was as follow:

“...a contract whereby the owner of the copyright in a film grants an exclusive right to exhibit that film for a specific period in the territory of a Member State is not as such, subject to the prohibitions... It is, however, where appropriate, for the national court to ascertain whether, in a given case, the manner in which the exclusive right conferred by that contract is exercised is subject to a situation in the economic or legal sphere the object or effect of which is to prevent or restrict the distribution of films or to distort competition with in the cinematographic market, regard being had to the specific characteristics of the market.”¹⁴¹

The ECJ also stated that it is important to establish whether the exercise of the copyright created barriers, which were ‘artificial and unjustifiable in terms of the needs of the cinematographic industry.’¹⁴²

6.5.4.3 Concluding remarks

Again, the restraints approved are ‘ancillary’ to the agreement and an absolute territorial protection can never be allowed in regard to the integration goal. If the economic theory says otherwise, such an evaluation is conducted under Article 81(3) EC. When the Court made careful distinctions between various types of provision in these two cases Forrester and Norall is of the opinion that a rule of reason type argument was made.¹⁴³ However, this may not necessarily have been the case. No balancing act was conducted, just a discussion of necessity.

Coditel II was solely based on the protection of intellectual property rights. There was a genuine need to obtain a just return on the investments made because of that property right. Therefore, it may be legitimate to afford greater

¹⁴¹ *Coditel II*, supra note 139, para 20.

¹⁴² *Coditel II*, supra note 139, para 19.

¹⁴³ *Forrester and Norall*, supra note 3, p. 39.

protection to intellectual property rights compared to ordinary exclusive distribution agreements.

6.5.5 Franchising

Franchising is really a mix of selective distribution and licensing of intellectual property rights. The franchisee gets to use certain intellectual property rights and know-how for which he pays royalty. In return the franchisee receives a complete and tried out business concept. Normally the franchisee has to comply with several obligation imposed by the franchisor in order to protect the business concept.

6.5.5.1 *Pronuptia*¹⁴⁴

The case concerned franchising agreements for wedding apparel. The franchisor undertook: to grant the exclusive right in a specific area, not to compete either directly or indirectly in that area, to give assistance in setting up the store, to provide know-how etc. In return the franchisee undertook: to use the Pronuptia name, to pay royalty, to purchase 80 percent of the wedding dresses from the franchisor, to take account of the recommended resale price and not to compete with any Pronuptia business. First, the ECJ acknowledge the different types (service, production and distribution) of franchise agreements and that this agreement constituted a distribution franchise.

Secondly, the ECJ declared that distribution franchise agreements has a legitimate aim and that ‘such a system, which permits the franchisor to take advantage of his success, is not by itself restrictive of competition.’¹⁴⁵ Thirdly, the ECJ addressed the question of which restraints that may be necessary. Accordingly, a franchisor must be able to provide his know-how without the risk of leaking the knowledge to competitors. Clauses that protect the know-how of the franchisor does not restrict competition within the meaning of Article 81(1) EC, which includes a prohibition on the franchisee to open a similar shop during and for a reasonable time after expiration of the franchise agreement and to sell the existing shop without the franchisor’s approval. Furthermore, the franchisor must be able to protect the identity and reputation of the trademark without falling

¹⁴⁴ Case 161/84 *Pronuptia de Paris GmbH v. Pronuptia de Paris Irmagard Schillgallis* [1986] ECR 353.

¹⁴⁵ *Ibid*, para 15.

into Article 81(1) EC. Obligations to apply the commercial methods and to utilise the know-how provided, includes obligations only to sell the covered products in premises set up and decorated according to given specifications in order to guarantee a uniform image. This goes for the location of the shop to. The control over the selection of goods is necessary for quality reasons when it is impractical to lay down objective quality specifications. Such circumstances takes a provision controlling the selection of goods out of Article 81(1) EC, but the possibility to purchase from other franchisees can never be prevented.

Finally, the ECJ addressed the issue of control over advertising and concluded that such control is necessary for image reasons as long as it only concerns the nature of the advertising. However, certain restrictions in the agreement restricted the competition between the members in the franchise network and were not necessary for the protection of know-how or the maintenance of the network's identity and reputation. Especially those provision which share markets or prevent the ability for price competition. In this case, the combination of the obligation not to sell the goods in other premises (prohibition from opening another shop) and the exclusive grant of business name or symbol (prevents both the franchisor and other franchisees to compete) results in the sharing of markets which restricts the competition within the network. The ECJ went on:

“As is clear from the judgement of 13 July 1966 (Joined Cases 56 and 58/64 *Consten and Grundig v. Commission* [1966] ECR 299), a restriction of that kind constitutes a limitation of competition for the purposes of Article 85(1) [now Article 81(1)] if it concerns a business name or symbol which is already well-known. It is of course possible that a prospective franchisee would not take the risk of becoming part of the chain, investing his own money, paying a relatively high entry fee and undertaking to pay a substantial annual royalty, unless he could hope, thanks to a degree of protection against competition on the part of the franchisor and other franchisees, that his business would be profitable. That consideration, however, is relevant only to an examination of the agreement in the light of the conditions laid down in Article 85(3) [now Article 81(1)].”¹⁴⁶

Price guidelines are not considered to be restrictive as long as there is no concerted practice between the members of the franchise network.

6.5.5.2 *Concluding remarks*

¹⁴⁶ *Ibid*, para 24.

Market sharing is a generally by object restrictive and needs no further examination in respect of Article 81(1) EC even if in some circumstances it might be necessary for the attainment of the agreement. However, this was a preliminary ruling, contrary to *Consten and Grundig*, and the Court wanted to give as much guidance as it could. Therefore, the ECJ speaks in general terms and gives examples. It assessed which provisions that fell under Article 81(1) EC and which provisions that were necessary. No evaluation in abstract could be made, only on case-by-case, depending on the legal and economic context the agreement applied in.

Franchise agreements typically afford territorial protection within the network. This protection may be necessary for any franchisee to get involved and invest money in the first place, but when the franchise network is well known by business name or symbol, such a restraint of competition is caught by Article 81(1) EC and can only be exempted through Article 81 (3) EC.¹⁴⁷ Peeters explains the ‘well-know’ as a referral to the ‘de minimis’ concept.¹⁴⁸

6.5.6 Sale of businesses

Not many would disagree on that there should be a market for the sale of businesses. A time-limited restriction on the vendor not to compete with the buyer certainly restricts the vendor’s ability to do businesses in that particular market. What about competition?

6.5.6.1 *Remia*¹⁴⁹

The case concerned the sale of businesses. The firm Nutricia sold its two subsidiaries Remia and Luycks to two separate buyers. Nutricia imposed a non-competition clause on the buyers, not to compete in the products sold by the other business. Remia produced sauce and Luycks produced pickles in the Netherlands. The Commission had acknowledged the need for a non-competition clause when selling a business, where not only material assets were transferred but also goodwill and clientele. However, in this case the duration for 10 years was not necessary and the Commission also refused to exempt the clause stating that four years had been reasonable. Also the geographical scope of a non-

¹⁴⁷ Faull & Nikpay, supra note 23, paras 2.90-92.

¹⁴⁸ Peeters, supra note 72, p. 566-568.

¹⁴⁹ Remia, supra note 90.

competition clause had to be limited to an extent, which was objectively necessary. Consequently, the excessiveness of the restraints made Article 81(1) EC applicable.¹⁵⁰

On appeal the ECJ upheld the Commission's decision and spoke in general terms about a non-competition clause in agreements concerning the sale of businesses. It was necessary to assess the level of competition between the vendor and buyer in the absence of the restrictions. The vendor would be in a favourable position if it were allowed to immediately engage in competing with the buyer. The buyer would seriously risk losing the customers of the bought firm back to the vendor with its specific knowledge of that particular firm. The ECJ stated:

“Against that background non-competition clauses incorporated in an agreement for the transfer of an undertaking in principle have the merit of ensuring that the transfer has the effect intended. By virtue of that very fact they contribute to the promotion of competition because they lead to an increase in the number of undertakings in the market in question. Nevertheless, in order to have that beneficial effect on competition, such clauses must be necessary to the transfer of the undertakings concerned and their duration and scope must be strictly limited to that purpose.”¹⁵¹

Clauses that complied with such condition did not fall into the reach of Article 81(1) EC. Regarding the duration of such clauses the ECJ only addressed the question whether or not the Commission had provided adequate statements of grounds for its decision and had wrongly assessed the facts in the case for the four years limitation on the non-competition clause. The ECJ did not find any error made by the Commission, but the Commission, in its decision, stated factors to consider when assessing the necessity of a non-competition clause:

“It is not possible to set any length of time as universally suitable as a period of protection. Each non-competition period must be judged in its context. ...the time it will take the purchaser of a business to build up a clientele; how frequently consumers in the relevant market change brands and type (in relation to the degree of brand loyalty shown by them); how long it takes before new products entering the market or new trade marks are accepted by the consumer; for how long, after the sale of the business, the seller, without a restrictive clause, would be able to make a successful comeback to the market and regain his old customer.”¹⁵²

¹⁵⁰ Commission decision of December 12, 1983 *Nutricia* [1983] OJ L376/22.

¹⁵¹ *Remia*, supra note 90, paras 19-20.

¹⁵² *Nutricia*, supra note 150, para 28.

As a rule of thumb, regarding the geographical scope, it should only cover ‘the markets where the products concerned were manufactured or sold at the time of the agreements...’¹⁵³ according to the Commission.

6.5.6.2 Concluding remarks

There is really not much to say about the ECJ’s findings in this case that have not already been said. It is a classic example of a legitimate business practice that needs a non-competition clause in order to exist in some circumstances. It serves as a confirmation from the ECJ that the sale of businesses belongs to the categories of legitimate business practices that are subject to the more narrow interpretation of Article 81(1) EC.

6.5.7 Co-operation agreements

While it is quite obvious why vertical restraints may escape the prohibition in Article 81(1) EC, this is not the case with co-operation agreements at the horizontal level. The co-operation can concern research and development, production, purchasing, commercialisation, standardisation and environment or a combination thereof. Still there may be circumstances, although very limited, that will rescue the agreement from the scope of Article 81(1) EC.

*6.5.7.1 The Odin decision*¹⁵⁴

The case concerned a joint venture between Elopak, a producer of cartons for milk etc., and Metal Box, a producer of metal closures, PET and polythene bottles etc. Together they were going to conduct, in the newly established joint owned undertaking Odin, research and development of a container with a carton base and separate closure and, if successfully, exploit this new form of package together with its filling and sealing machinery. It was expected that the new package could be filled with UHT processed foods, which would have a shelf-life of several month and which would preserve the quality of the food better than the

¹⁵³ Ibid, para 30.

¹⁵⁴ Commission decision of July 13, 1990, Elopak/Metal Box – Odin [1990] OJ L209/15; [1991] 4 CMLR 832.

sterilisation used in canning. The agreement was notified to the Commission seeking negative clearance or exemption under Article 81(3) EC.

In relation to Article 81(1) EC the Commission first examined what kind of joint venture and in what context it was going to exist. The Commission said that the new product probably would constitute a substitute for metal cans, glass jars and certain 'brick' type cartons, but could also win its own special market. The fact that Elopak and Metal Box were not competitors, actual or potential, in their relevant product market and that either party could not by itself effectively develop such a product gave the joint venture a legitimate aim, which by itself was not caught by the prohibition in Article 81(1) EC. The know-how of the two parties was not by themselves enough to launch the project individually. They had separate experience and knowledge that needed to be combined in order for the project to work, which would considerably reduce both the technical risks and the commercial risks involved. As the parent undertakings operated at different markets no competition concern could arise between the parents. Odin, on the other hand, risked becoming a competitor of Metal Box, but that did not cause any direct concern for competition as the joint venture's structure supported that holding. The Commission concluded the following:

“As the parties could not realistically be regarded as competitors, actual or potential, and the creation of the joint venture entails no foreclosure risk, and the agreement does not involve the creation of a network of competing joint ventures, the agreements to establish Odin do not fall within the terms of Article 85(1) [now Article 81(1)]. The specific provisions of the agreement must however be examined to ascertain whether such provisions restrict competition within the meaning of Article 85(1) [now Article 81(1)], or whether they are no more than is necessary to ensure the starting up and the proper functioning of the joint venture.”¹⁵⁵

Special attention had to be given to the possibility that Odin might become competitor to some extent with Metal Box. First, the grant to Odin of the exclusive right to exploit the proprietary know-how in the field of the project worked as a guarantee for full devoutness of the parents to the project. Together with the non-exclusive licence of improvements that might be granted by Odin to its parents ensured that Odin would obtain exclusivity on exploiting the know-how in the field of the project. To enjoy this exclusivity even after the starting point was necessary, according to the Commission, to be able to develop not only the new product but also the machinery and technology linked to it and to adopt to

¹⁵⁵ Ibid, paras 28-29.

possible changes likely to occur after the successful development. Furthermore, no explicit restrictions on price, quantity or territory existed even though the possibility of competition with Metal Box was present. The exclusivity was also narrowly defined and limited to the field of the project and the parents were not restricted to conduct their own research and development or exploitation.

Secondly, the grant to Odin of a non-exclusive licence to use its parents' know-how along with provisions on updating and secrecy were necessary. They guaranteed the secrecy of the know-how and prevented each parent from using Odin as a mean to obtain and use the other parent's know-how. Also, they did not restrict the possibility for the parents to engage in research and development closely related.

Thirdly, the obligation of the parents to licensing technology in the case of dissolution or break-up did not fall under Article 81(1) EC. In such a case the parents were free use and exploit all the know-how Odin possessed including the other parent's know-how although limited to the field of the project, which was necessary in respect of that the co-operation was limited. It worked as a protection for each parent's know-how not to be used by the other party outside the scope of the project in case of a break-up occurred. Furthermore, it also prevented Metal Box from hindering exploitation of products that might compete with its own products and to impose territorial restrictions on Odin's products. Elopak had no reason whatsoever to limit Odin's output or geographical scope and the Commission also believed there was no reason to suspect that Metal Box would try to use its co-control in such a manner.

Fourthly, the obligation on the parents not to allow a competitor of the other parent to use its know-how for a period of five years after break-up and the right of first refusal in the event of a further sale also escaped the prohibition along with the need for the other parent's consent in case of sale of its shares in Odin. Without those provisions, it was said, there would not be any co-operation in the first place and was necessary for the parents' willingness to properly invest in Odin.

Finally, the obligation on Odin to keep the parents' know-how secret were necessary to protect Odin's purpose and existence and the parents' wish to limit the project to a specific field. The Commission then concluded that:

“the provisions which in other contexts might restrict competition but which in the context of the present case do not[, s]ince such provision cannot be disassociated form the creation of Odin without undermining its existence and purpose and since the creation of Odin does not fall within the scope of Article 85(1) [now Article 81(1)], these specific

provisions also fall outside the scope of Article 85(1) [now Article 81(1)].”¹⁵⁶

A negative clearance decision was given.

6.5.7.2 *Gottrup-Klim*¹⁵⁷

In this case, which was a preliminary ruling, the ECJ was asked whether a joint buying co-operative which prevented its members from buying through other co-operative organisations in direct competition with that association could fall under Article 81(1) EC.

The ECJ first stated that whether or not Article 81(1) EC catches a provision in an agreement depends both on its content and the economic conditions prevailing on the market. Co-operative purchasing associations, in markets where prices vary depending on the volume, can constitute an important counterweight to the contractual power of large producers and thereby eliminate the producers ability to use its market power for the benefit of competition.

The ECJ then discussed possible consequences of a dual membership and concluded that it can diminish the strength of the association to the detriment of the other members and thereby jeopardising the proper functioning of the association. With this in mind the ECJ stated:

“ Prohibition of dual membership does not, therefore, necessarily constitute a restriction of competition within the meaning of Article 85(1) [now Article 81(1)] of the Treaty and may even have beneficial effects on competition. Nevertheless, a provision in the statutes of a cooperative purchasing association, restricting the opportunity for members to join other types of competing cooperatives and thus discouraging them from obtaining supplies elsewhere, may have adverse effects on competition. So, in order to escape the prohibition laid down in Article 85(1) [now Article 81(1)] of the Treaty, the restrictions imposed on members by the statutes of cooperative purchasing associations must be limited to what is necessary to ensure that the cooperative functions properly and maintains its contractual power in relation to producers.”¹⁵⁸

The national court also had to examine whether the minimum period of membership was unreasonable and if the sanctions for non-compliance were disproportionate. The ECJ carried on by giving somewhat detailed guidance to the national court. First, the restriction only covered fertilisers and plant protection

¹⁵⁶ Ibid, para 36.

¹⁵⁷ Gottrup-Klim, supra note 92.

¹⁵⁸ Gottrup-Klim, supra note 92, paras 34-35.

products. These were the only products purchased by the association where a direct relationship between sales volume and price existed. Secondly, non-members were allowed to purchase the whole range of products offered at the same price and terms as members, but were not entitled to the yearly discount on the total amount purchased. Finally, members were allowed to purchase fertilisers and plant protection products outside the association as long as it was not through another association. To the ECJ, such a restriction did not 'go beyond what is necessary'.¹⁵⁹ Furthermore, as the association treated the excluded plaintiffs only as non-members and as the membership period was set at five years the ECJ did not, in their eyes, think it was either disproportionate or unreasonable.

*6.5.7.3 European Night Services*¹⁶⁰

The facts of the case are rather complex and involve a joint venture between several railway companies in different Member States with the intention to provide and operate overnight passenger rail services on routes from points in the United Kingdom and the Continent through the Channel Tunnel. The first agreement notified concerned the formation of European Night Services (ENS) and the second group of agreements concerned the operating of ENS in which each rail way undertaking agreed to provide ENS with certain services, including locomotive, train crew, path, cleaning services, equipment services and passenger-handling services over its network. One of them also agreed to provide the services through the Channel Tunnel. To be able to operate the night services the railway undertakings had produced, through ENS, specialised rolling stock suitable for running on the different rail system and through the Channel Tunnel. The specialised rolling stock was financed through long-term leasing arrangements over 20 years with a total cost of £ 158 million. The applicants argued that it was subject to competition from air, coach, ferry and car transport and that ENS's market share would be insignificant in that perspective. Furthermore, non-of the applicants could alone provide the same comparable services and that there were no additional barriers of entry created by the agreements.

The Commission found that the co-operative joint venture restricted competition, existing and potential, between the parent companies, between ENS and the parent companies, vis-à-vis third parties and that a network of joint ventures in which many of the parents were participants enhanced the restriction.

¹⁵⁹ Gottrup-Klim, supra note 92, para 40.

¹⁶⁰ European Night Services, supra note 97.

However, the joint venture got an exemption under Article 81(3) EC for the duration of eight years, attached with a condition to allow all competitors to have access to the same necessary rail services, at the same terms, the parents supplied ENS. The four parents appealed to the CFI asking the Court to annul the decision for four reasons: the ENS agreements did not restrict competition; the Commission had wrongly applied Directive 91/440; the Commission had imposed a disproportionate condition; and that the duration of the exemption was too short. All because of inaccurate and incomplete assessment of the facts, manifest error in law and failure to state reasons by the Commission.

The CFI struck down on the Commission's findings on all points. First, there were misconceptions about the definition of the relevant market and whether or not ENS's market share was evidence alone of an appreciable effect on trade between Member States. The CFI could not, due to insufficient statement of reasons, rule on the ENS's market shares on the relevant markets. The Court cited the ECJ's judgements in *Völk* and *Langnese-Iglo* to support the conclusion that an agreement might fall outside the scope of Article 81(1) EC if it only had an insignificant effect on the market and that even if the market threshold, set out in the Notice on Agreements of Minor Importance, was reached it was not possible to conclude 'with certainty' that the agreement was caught by Article 81(1) EC. The market shares of ENS were around five percent which is the threshold for horizontal agreements. Without the needed statement of reasoning concerning the market shares the CFI could not either rule on the question of appreciable effect on trade. This was a ground for annulment.

Secondly, in relation to the overall assessment of the ENS agreements the applicants argued, by referring to case law, that 'the pro-competitive effects of an agreement must be weighed up against its anti-competitive effects. If the pro-competitive effects outweigh the anti-competitive effects and the latter are necessary in order to implement the agreement, then the agreement cannot be regarded as having as its object or effect'¹⁶¹ the restriction of competition within the meaning of Article 81(1) EC. This statement was challenged by the Commission claiming that the application of a 'rule of reason' to balance pro- and anti-competitive effects was only required under Article 81(3) EC and not under Article 81(1) EC, but acknowledged, in relation to the United Kingdom's intervention, that an analysis of an agreement under Article 81(1) EC must take account of its economic context. In regard of this the CFI saw the need to clarify the assessment process under Article 81(1) EC. The Court stated:

¹⁶¹ *Ibid*, para 119.

“in assessing an agreement under Article 85(1) [now Article 81 (1)] of the Treaty, account should be taken of the actual conditions in which it functions, in particular the economic context in which the undertakings operate, the products or services concerned by the agreement and the actual structure of the market concerned (judgements in *Delimitis*, cited above, *Gottrup-Klim*, cited above, paragraph 31, Case C-399/93 *Oude Luttikhuis and Others v Verenigde Coöperatieve Melkindustrie* [1995] ECR I-4515, paragraph 10, and Case T-77/94 *VGB and Others v Commission* [1997] ECR II-759, paragraph 140), unless it is an agreement containing obvious restrictions of competition such as price-fixing, market-sharing or the control of outlets (Case T-148/89 *Tréfilunion v Commission* [1995] ECR II-1063, paragraph 109). In the latter case, such restrictions may be weighed against their claimed pro-competitive effects only in the context of Article 85(3) [now Article 81 (3)] of the Treaty, with a view to granting an exemption from the prohibition in Article 85(1) [now Article 81 (1)]. It must be stressed that the examination of conditions of competition is based not only on existing competition between undertakings already present on the relevant market but also on potential competition, in order to ascertain whether, in the light of the structure of the market and the economic and legal context within which it functions, there are real concrete possibilities for the undertakings concerned to compete among themselves or for a new competitor to penetrate the relevant market and compete with the undertakings already established in it (*Delimitis*, cited above, paragraph 21).”¹⁶²

Furthermore, the CFI pointed to the Commission Notice of 1993 concerning the assessment of co-operative joint ventures pursuant to Article 85 [now Article 81] of the Treaty where it, in paragraph 18, acknowledged that ‘an economically realistic approach is necessary in the assessment of any particular case’.

Thirdly, after the declaration of the state of law the CFI began to examine whether the Commission’s assessment was correct. Due to the length and many aspects in the assessment I will just briefly state the findings of the Court. Concerning the alleged restriction on competition among the parent undertakings the special characteristics of the market, especially the obligatory trading partners in an international grouping operating an international route,¹⁶³ made a restriction of competition quite impossible among the parents. As for potential competition among them the Commission had claimed that there were, in theory, no legal obstacle for a parent to establish itself in another Member State to compete with ENS. However, the CFI stated that the Commission had failed to take account of the economic context, as such theoretic possibility would be unrealistic and economies of scale made it unprofitable. The CFI held that inadequate reasoning and/or error of assessment vitiated the Commission’s findings on this part.

¹⁶² *Ibid*, para 136-137.

¹⁶³ See Article 10 of Directive 91/440.

Concerning the alleged restriction on competition vis-à-vis third parties the Court stated that the assumption that a special relationship between ENS and its parents would place other operators at a disadvantage to enjoy the necessary rail services provided by the parents rested on the presumption that the market for rail passenger transport was divided into two parts, one upstream and one downstream market, which would require that the services provided by the parents were classified as essential facilities. Furthermore, regarding the access to train path through the Channel Tunnel the Commission's findings rested on its Eurotunnel decision, which had been annulled. Again the Commission's findings contained errors of facts. Concerning the alleged aggravation of the restrictive effects on competition caused by the presence of a network of joint ventures the Court pointed out that the Commission could not specify and had no knowledge of any other joint venture, in which the parents were participating, concerning passenger transport services although there were some in the market for transport of goods. The Commission's reasoning did not, therefore, contain sufficient statement of reasons.

Finally, the CFI also stated that the condition imposed was disproportionate mostly because of the error to categorise ENS as a transport operator and not as an international grouping according to Article 3 of Directive 91/440. Furthermore, the eight years exemption was unreasonable due to the fact that the financing of the joint venture had a 20 years payment plan.

6.5.7.4 Concluding remarks

Odin is a rare example of when special circumstances in combination with a carefully written agreement can clear a joint venture from Article 81(1) EC. *Odin* concerned co-operation in research and development, production and commercialisation. Almost all formal decisions taken by the Commission on joint ventures have been exemptions, with few exceptions such as *Odin* and *Koncertium*.¹⁶⁴ Shortly, after the *Odin* decision, however, the Commission did not clear a similar case.¹⁶⁵

In *Gottrup-Klim* the Court first acknowledged the legitimate aim of a co-operative purchase agreement and stated that such a restriction on its members

¹⁶⁴ Commission decision *Koncertium* ECR 900 [1992] 4 CMLR 54; Korah, *supra* note 64, p. 259.

¹⁶⁵ Commission decision *KSB/Goulds/Lowara/ITT* 91/38 (1991) OJ L19/25.

did not necessarily restrict competition. After the establishment of the legitimate aim of the conduct, the CFI then discussed possible effects of when a member belongs to two competing associations, showing that such a prohibition does not necessarily restrict competition within the meaning of Article 81(1) EC. Whether or not the provision restricted competition did not depend on a balancing act, but on the necessity in that specific case. It restricted the members' ability to purchase through other channels and depending on the specific characteristics of the case the restriction has to be necessary for the proper functioning.

The statement in *ENS*, paragraphs 136-137, was really nothing new. The fact that an agreement must be assessed in its economic context does not mean that a balancing of pro- and anti-competitive effects in the sense of a rule of reason is required. Just to assess the effects of the agreement to see if it has effects on competition which might be judged as a restriction. The annulment of the Commission's decision was due to assumptions and lack of sufficient reasoning about the economic context in which the agreement is applied. Thus, the Commission has assessed the agreements in the wrong economic context and nothing more. In the authors opinion there existed a possibility that the agreements would not be caught by Article 81(1) EC because of the very special characteristics of the market, which makes the railways companies in different Member States not necessarily competitors to some extent, meaning that they were not realistically competitors even if they were in theory. Furthermore, economic of scale and the fact that no undertaking alone could do it along with the novelty of the services created additional competition to other means of transport, especially transport by air.

7 The new policy on vertical and horizontal restraints

7.1 The Commission's new policy on vertical restraints

A new block exemption on vertical restraints¹⁶⁶ has entered into force 1st of June 2000, where a new approach towards vertical restraints is laid down. The former block exemptions were considered not to be flexible enough with their form-based approach. With the form-based system agreements that were anti-competitive could pass and vice versa and they did not cover intermediate goods or services. The Commission recognised these problems with its old policy, although confirming that the policy had been successful for some 30 years in its Green Paper on Vertical Restraints.¹⁶⁷ In May 2000 the Commission also published its Guidelines on Vertical Restraints, which provides a good view of how the Commission intends to apply Article 81 on vertical restraints.¹⁶⁸

The new policy involves more economic thinking than before and focuses on the effects of the vertical restraint on the market in question. The most significant change is the focus on market power. Many commentators have welcomed this. Vertical restraints are no longer regarded as per se suspicious, but at the same time they are not regarded as per se pro-competitive as many economists would like. The Commission intends to assess vertical restraints on a case-by-case basis and recognises that anti-competitive effects are only likely where inter-brand competition is weak and there are barriers to entry at either producer or distributor level. The Commission wants to concentrate its efforts on vertical restraints in this area where market power exists. Therefore, the new block exemption introduces a market share threshold set at 30 percent. According to the Commission, Article 81(1) EC would now catch fewer agreements. Especially those in markets that are not concentrated, HHI index less than 1.000,¹⁶⁹ will be

¹⁶⁶ Supra note 119.

¹⁶⁷ Green Paper on Vertical Restraints in Competition Policy (COM(96) 721 final, 22 January (1997) at paras 1-3.

¹⁶⁸ Ibid, at paras 119-136.

¹⁶⁹ The Herfindahl Hirshman Index measure the concentration in the market with respect of the number of undertakings and their individual market shares, $\sum sn^2$, where sn is the market share of undertaking n.

assumed not to have an appreciable effect within the meaning of Article 81(1) EC. Still there are ‘hard-core’ clauses in the new block exemption, like absolute territorial protection, RPM¹⁷⁰ and restriction of parallel trade, which has no place in the economic perspective. These hard-core clauses have to some extent their foundation in the integration goal. Furthermore, the Commission is of the view that a combination of vertical restraints is, in general, more likely to have anti-competitive effects than a single one.¹⁷¹ Some commentators argue that there is less legal certainty with the new block exemption, but the economic view is that the undertakings are now more free in their commercial decisions than they used to be.¹⁷²

Although the new block exemption will confer greater legal certainty, more commercial freedom and the reduction of legal fees the key question is, according to Riley, whether the Commission has abandoned its broad interpretation of Article 81(1) EC. He is not so sure of that.¹⁷³

7.2 The Commission’s new policy on horizontal restraints

The Commission’s Draft Guidelines on the Applicability of Article 81 to Horizontal Co-operation deals with agreements on research and development, production, purchasing, commercialisation, standardisation and environment.¹⁷⁴ The hazard with horizontal agreements is the ‘inherent’ risk of anti-competitive co-operation to the detriment of consumer welfare and the integration goal of the EU. At the same time the Draft Guidelines acknowledges the ‘need to respond to increasing competitive pressure and a changing market place driven by globalisation, the speed of technological progress and the generally more dynamic nature of markets. Co-operation can be a means to share risk, save costs, pool know-how and launch innovation faster. In particular for small- and medium-sized enterprises co-operation is an important means to adapt to the changing market place.’¹⁷⁵ The economic context of the agreement as: the nature of the agreement,

¹⁷⁰ Resale Price Maintenance.

¹⁷¹ Furse, *supra* note 6, p. 131-133, 153.

¹⁷² Riley, *supra* note 66, p. 490; Bishop and Walker, *supra* note 15, p. 95-97.

¹⁷³ Riley, *ibid*, p. 490-492.

¹⁷⁴ Commission Draft Guidelines on the Applicability of Article 81 to Horizontal Co-operation, at para 10.

¹⁷⁵ *Ibid*, para 2.

the undertakings combined market power and other structural factors determine if the agreement in hand will be caught by competition rules.¹⁷⁶

The nature of an agreement concerns factors such as the area and objective, the competitive relationship and the extent to which they combine their activities. Agreements that, in general, do not fall under Article 81(1) EC, according to the guidelines, are co-operation between undertakings that are not competitors, co-operation between competing undertakings that cannot independently carry out the project or activity covered by the co-operation and co-operation concerning an activity far removed from the marketing level (such as improving environmental conditions). The *Odin* decision is a good example where the undertakings were non-competitors and unable to independently carry out the activity. In such circumstances the co-operation cannot restrict competition as it evolves a new product/service and/or increases the competition in another market. The fact that there are co-operations between undertakings at the horizontal level does not necessarily mean that the competition will be restricted, but the Commission stresses in the Guidelines ‘while recognising the economic benefits that can be generated by co-operation, [the Commission] has to ensure that effective competition is maintained.’¹⁷⁷ Agreements in-between these types of agreements and the ones with hard-core provisions need further analysis to determine the applicability of Article 81(1) EC.¹⁷⁸

Where the undertakings have a weak market position or one party’s market power is insignificant, taken account to both combined and individual market shares, it is unlikely that Article 81(1) EC will apply. The market concentration is also a factor of importance. The HHI is used as an indicator where below 1.000 is low, 1.000-1.800 is moderate and above 1.800 is high. By analysing these factors other factors¹⁷⁹ may have to be taken into account for a full analysis. Consequently, an economic analysis is required under Article 81(1) EC in respect of horizontal agreements, even though this is true only to a limited kind of agreements.¹⁸⁰

Research and development (R&D) agreements have been encouraged by the Commission and do not fall within Article 81(1) EC if the joint venture does not go beyond what is necessary to successfully achieve the research and to exploit

¹⁷⁶ *Ibid*, paras 17-19.

¹⁷⁷ *Ibid*, para 4.

¹⁷⁸ *Ibid*, paras 20-26.

¹⁷⁹ Such as the stability of market shares over time, entry barriers and the likelihood of market entry, the countervailing power of buyers/suppliers or the nature of the products.

¹⁸⁰ *Supra* note 173, paras 27-31; also *Furse*, *supra* note 6, p. 133-135.

the result. It is provisions that limit the parties freedom afterwards and agreements in concentrated markets that are of concern.¹⁸¹

7.3 The Modernisation White Paper

The Modernisation White Paper¹⁸² has suggested that Article 81(3) EC should be directly applicable to national courts and competition authorities. This may bring a risk of inconsistencies in the application, but the difference in application is expected to be acceptable. Furthermore, the notification system would be abolished and ‘Article 81 would become a unitary norm comprising a rule establishing the principle of prohibition, unless certain conditions are met’.¹⁸³

This would mean that the Commission would no longer have monopoly on granting exemptions under Article 81(3) EC, which has raised specific concern towards the system governing the application of Article 81 EC.

¹⁸¹ Furse, supra note 6, p. 160.

¹⁸² Supra note 60.

¹⁸³ Furse, supra note 6, p. 145-146.

8 Conclusions

What we have to deal with is Article 81(1) EC and its statutory language. The interpretation of the notion of restriction of competition can on the one hand include almost all agreements and on the other, the rule of reason à la United States. It is evident that the structure of Article 81 EC differs from the structure in the Section 1 of the Sherman Act. However, despite this structural difference, Article 81(1) EC cannot be allowed to catch all the agreements. This means that there have to be some sort of mechanism to distinguish agreements that fall under the prohibition from the ones that fall outside. This mechanism exists, but has been used in an inconsistent way. To this dilemma there are several solutions, but mainly two are discussed; ancillary restraints and the rule of reason. The structure of Article 81, as it has developed since the introduction of Regulation 17, is best suited for some form of the ancillary restraints doctrine. Before that other solution were possible, as is evident by looking at the application of the exported EC competition regime.

The case law on this subject has not yet been as developed as needed in order for a clear concept to emerge. The Sherman Act has been in force for over 110 years without any problem of an exemption clause. The notion of ‘per se’ and ‘rule of reason’ is rather clear in the US, but they are still struggling with the difficulty of classifying an agreement in the specific case. That struggle, however, may never go away. A difference in development of the EC competition law is that we do not have any clear concept to rule agreements in or out of Article 81(1) EC. The ancillary restraints doctrine, a narrow rule of reason, a wide rule of reason, an own rule or nothing at all are all concepts that have been suggested. The trend, however, is a movement towards a more narrow scope of Article 81(1) EC, which can be seen in the CFI’s and the ECJ’s judgements.

The fact that the Commission has not followed the ECJ’s development, to some extent, has in reality been the subject for most concern. The Commission has, usually, not bothered to conduct a full assessment of the economic context. Instead it has been more formalistic in its approach making generalisations and assumptions. You could expect this conduct to be a by-product of the Commission’s double role as ‘prosecutor and judge’. A prosecutor does not win all the cases. More likely is that the Commission stresses the jurisdictional aspect of the paragraph to a greater extent than the Court has. The real problem here is, however, that the Commission sits in the driving seat instead of the Court. The

Community Court's ability to get involved in shaping the competition policy is not as great as the Commission's.

The majority of the commentators, points to the Courts movement towards more economic analysis under Article 81(1) EC and, in general, they agree that we are dealing with a form of ancillary restraint doctrine to certain kinds of business practices. However, the rule of reason accusations generally concerns the process when the Courts have been given its reasons to why a particular business practice is considered to be legitimate. To imply that a rule of reason approach has been adopted is, however, misguided, but it is true as the Advocate General Lenz said that the ECJ 'attach[es] weight to the concerns on which the rule of reason doctrine is based'. This statement means, in the author's opinion, just that such concern can be found in the discussions of the legitimacy of the practice. This was evident already in the ECJ's judgment in *STM*, delivered in 1966, but the number of approved business practices has increased over the years. These are: exclusive distribution, selective distribution, exclusive purchasing, licensing of intellectual property rights, franchising, sale of businesses and to some extent joint ventures at the horizontal level.

Once a legitimate business practice, as such, is declared not necessarily falling into Article 81(1) EC the examination of specific provisions begins to determine whether they are necessary or not. Sometimes there are 'hard core' provisions that are always examined under Article 81(3) EC, partly in consideration of the integration goal. The rest depends on the economic and legal context in which the agreement is applied. The *Odin* decision is a good example. First, the joint venture's intention as it was conducted did not necessarily fall within Article 81(1) EC. Then the specific provisions were examined to see if they are absolutely necessary. This pattern is evident in all the cases studied in this thesis.

As said, this is not the same as the rule of reason, where pro- and anti-competitive effects are being balanced against each other. Of course the legitimate business practice must certainly have pro-competitive effects. Otherwise it might not have been legitimate, but no balancing is conducted in relation to the restrictive provisions; just examination of what is necessary for such an agreement to exist at all in the specific economic and legal context. The mistake of 'reading out' a rule of reason discussion should not be made, although such a reading would most certainly clear the agreement too. The difference is the approach to the restrictive clauses and there is more room for restrictive clauses in a rule of reason because of the balancing act. The necessity is what could keep you out of 81(1) EC and the net effect is what could qualify as an exemption in EC competition law.

A comparison can be made with the development of the notion of restraint of trade in the United States. The general development is that the classification of agreements has shifted from 'per se' towards more rule of reason. The formalistic approach with many agreements caught by the prohibition in EC competition law has also moved towards a more lenient approach to legitimate business practises.

Moreover, the means to align application to economic considerations can differ. Section 1 of the Sherman Act uses the balancing act whereas in Article 81(1) EC the Court chose to acknowledge certain legitimate business practices with a strict condition that the restrictions are objectively necessary. If not necessary, any further assessment takes place under Article 81(3). Consequently, the procedural aspect differs in the sense that the Commission has the control over the 'balancing act' instead of the businessmen, lawyers and Courts.

The question of what is necessary also depends on what kind of risk takers the undertakings are. Thus, what is necessary to some might not, taking an objective view in consideration of economic theory and competition policies, be necessary in the eyes of the Commission or the Courts. Taking risks is inherent in the commercial world and undertakings cannot expect to protect themselves to 100 percent when expanding its businesses. The question on what is necessary for the attainment of a legitimate business practices is always arguable, but that does not change the fact that the provisions are restrictive. In this regard, the distinction made between objectively necessary/ancillary and commercial risk/market opening concept by Whish and Peeters may simply be explained by different opinions of necessity.

According to the author this is the position of the law governing 81(1) EC today, but the author is not willing to say that there is not room for a rule of reason under 81(1) EC. This is simply a question of policy that would of course diminish the role of Article 81(3) EC and at the same time take away the administrative burden on the Commission. However, at the practical level good flexible block-exemptions can match the result of a rule of reason and such blocks have now been introduced. Furthermore, the Modernisation White Paper can take away the Commission's monopoly on Article 81(3) EC in the near future. This development, however, does not change the fundamental question of what constitutes a restriction of competition within the meaning of Article 81(1) EC. The Commission seems to have wanted to respond to the economic arguments put forward, but did it on their own terms.

Instead of declaring a new approach towards Article 81(1) EC the block exemptions are drafted in a way that the agreements, which according to the case law may not fall under Article 81(1) EC are at the same time exempted from the

application of the same article. This way of dealing with the change in policy may be validated by the fact that assessments under Article 81(1) EC cannot be made 'in abstracto' whereas the block exemptions are just that. A change of policy under Article 81(1) EC must include some form of rule of reason and such a change is bigger in scope than the Commission's solution.

Any further debate, hereinafter, will therefore mostly be, just an academic debate. Free from the prohibition or exempted by a block does not really matter now for the majority of agreements. The businessmen with their lawyers can now more freely adopt their agreements to business practices instead of to the former narrowly drawn and inflexible block exemptions and thus, the procedural aspect of competition law has, practically not theoretically, to an extent shifted from the Commission to the businessmen. The dilemma, however, still exists on the fundamental level. The formal control still lies with the Commission.

Consequently, with flexible broad block exemptions exempting agreements according to economic theory the power of some of the arguments made in favour of a rule of reason will fade away. Notification will probably significantly be reduced leaving the Commission's resources free for targeting the real competition problems. The notion on restriction on competition is still going to be the same as will be especially obvious for the agreements that exceeds the market share thresholds in the block exemption. It is indicated, however, that there is a larger scope for 'insignificant effect' within the new block exemption. The case law on the notion of restriction of competition has not been extensive. The future borderline cases will probably diminish even further with this new approach. Only the really large undertakings may have an incentive and the possibility to appeal to the Community Courts. Maybe an increase in national proceeding will help shaping the future concept of a restriction of competition within the meaning of Article 81(1) EC.

Thus, this change in policy will not alter the notion of restriction of competition within the meaning of Article 81(1) EC, but it will take away the power from some of the arguments made in favour of a rule of reason approach. In the future when the Modernisation White Paper has introduced the 'modernisation reform', as intended, even more arguments will be weaker as the Commission's monopoly will expire leaving national authorities and courts room to grant exemptions.

The 'system failure' described in Hawk's article seems to be on the verge to be corrected, although the notion of restriction of competition remains the same.

Bibliography

Literature

- Amato, Giuliano *Antitrust and the Bounds of Power – The dilemma of liberal democracy in the history of the market*, Oxford 1997
- Bishop, Simon and Walker, Dr. Mike *Economics of E.C. Competition Law: Concepts, Application and Measurement*, London 1999
- Bork, R. *The Antitrust Paradox, A Policy at War with Itself*, Basics Books, 1978
- Craig, de Búrca *EU law: text, cases, and materials*, Second edition, Oxford 1998
- Faull & Nikpay *The EC law of competition*, Oxford 1999
- Furse, Mark *Competition Law of the UK & EC*, Second edition, London 2000
- Goyder, D.G. *EC Competition Law*, Second edition, Oxford 1993
- Korah, Valentine *An Introductory Guide to EC Competition Law and Practice*, Fifth edition, London 1994
- Whish, Richard *Competition Law*, Second edition, London 1989

Periodicals

- Forrester, Ian and Norall, Christopher *'The Laicization of Community law: Self-help and the Rule of Reason: How Competition law is and Could be Applied'* in CMLRev (1984) 21, p. 11-51
- Hawk, Barrey E. *'System Failure: Vertical Restraints and EC Competition Law'* (1995) ECLRev 32, p. 973-989

- Korah, Valentine *'The Rise and Fall of Provisional Validity – The Need for a Rule of Reason in EEC Antitrust'* (1981) 3 NW J Int. L and Bus, p 320
- Peeters, Jan *'The Rule of Reason Revisited: Prohibition on Restraints of Competition in the Sherman Act and the EEC Treaty'* in American Journal of Comparative Law (1989) Vol. 37, p. 521-570
- Riley, Alan J. *'Vertical Restraints: A Revolution?'* (1998) ECLR, p. 483-492
- Steindorff, Ernst *'Article 85 and the rule of reason'* (1984) CMLRev 21, p. 639-646.

Official documents

Council Regulation 17/62 on the implementation articles 85 and 86 of the Treaty

Commission Regulation 4064/89 of 21 December 1989 on the control of concentrations between undertakings, as amended by Regulation 1310/97

Commission Notice on agreements of minor importance which do not fall under Article 85(1) of the Treaty establishing the EC OJ (1997) C 372/13

Commission Notice on the concept of concentration (1998) OJ C66/5

1999 White Paper on Modernisation of the Rules Implementing Articles 85 and 86 (now Articles 81 and 82) of the EC Treaty Modernisation White Paper COM/99/101 final, Commission programme 99/27 approved on 28 April 1999

Commission Regulation No 2790/99 of 22 December 1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices

Commission's Draft Guidelines on the Applicability of Article 81 to Horizontal Co-operation (June 2000)

**Interviews conducted by Mark Furse for the Internet course
Competition Law of the European Union held at Lund's
University**

Michael G. Cowie, Howrey Simon Arnold & White, LLP, Washington D.C April 2000

Ray V. Hartwell, III, Hunton & Williams, Washington D.C April 2000

Roxanne E. Henry, Howrey Simon Arnold & White, LLP, Washington D.C April 2000

Table of Cases

ECJ

Joined cases 56 and 58/64 Etablissements Consten SARL and Grundig-Verkaufs-GmbH v. Commission [1966] ECR 299.

Case 56/65 Société Technique Minière v. Maschienbau Ulm GmbH [1966] ECR 235.

Case 23/67 Brasserie de Haecht v. Wilkin [1967] ECR 407

Case 5/69 Franz Völk v. Ets Vervaecke SPRL [1969] CMRL 273 at para 3;

Case 22/71 Beguelin [1971] ECR 949

Case 26/76 Metro-SB-Großmärkte GmbH & Co KG v. Commission and SABA [1977] ECR 1875

Case 258/78 L. C. Nungesser KG and Kurt Eisele v. Commission [1982] ECR 2015

Case 62/79 Coditel v. Ciné Vog Films [1980] ECR 881

Case 210/81 Demo-Studio Schmidt v. Commission [1983] ECR 3045

Case 262/81 Coditel SA, Compagnie générale pour la diffusion de la television v. Ciné-Vog Films [1982] ECR 3381

Case 107/82 AEG-Telefunken AG v. Commission [1983] ECR 3151

Case 42/84 Remia v. Commission [1985] ECR 2545

Case 75/84 Metro SB-Großmärkte GmbH & Co KG v. Commission (No. 2) [1986] ECR 3021

Case 161/84 Pronuptia de Paris GmbH v. Pronuptia de Paris Irmagard Schillgallis [1986] ECR 353

Case 45/85 VdS v. Commission [1988] 4 CMLR 264

Case C-234/89 Stergios Delimitis v. Henninger Bräu AG [1991] ECR I-935

Case C-250/92 Gottrup-Klim v. Dansk Landbrugs Grov-vareselskab [1994]
ECR I-5641

Case C-415/93 Union Royal Belge des Societes de Football Association ASBL
v. Jean-Marc Bosman [1995] ECR I-4921

CFI

Case T-28/90 Automec v. Commission (No. 2) [1992] 5 CMLR 431

Case T-19/92 Groupement d'Achat Edouard Leclerc v. Commission [1997] 4
CMLR 612

Case T-7/93 Langnese-Iglo GmbH v. Commission [1995] ECR II-1533

Case T-374/94 European Nigh Services v. Commission [1998] ECR II-3141

Commission decisions

Commission decision of December 15 1975, SABA, OJ L28/19 [1976] 1
CMLR D61

Commission decision Distillers Company plc (Red Label) [1983] OJ C245/3

Commission decision 83/610 Murat [1983] OJ L 348/20

Commission decision of December 12, 1983 Nutricia [1983] OJ L376/22

Commission decision 84/233 IBM Personal Computers [1984] OJ L118/24

Commission decision 85/616 Villeroy& Boch [1985] OJ L376/15

Commission decision of July 13, 1990, Elopak/Metal Box – Odin [1990] OJ
L209/15

Commission decision KSB/Goulds/Lowara/ITT 91/38 (1991) OJ L19/25

Commission decision Koncortium ECR 900 [1992] 4 CMLR 54

Commission decision IV/32.290 Newitt/Dunlop Slazenger [1992] OJ L131/32

American case law

Standard Oil Co. of New Jersey v. United States (1911) 221 US 1

Chicago Board of Trade v. US (1918) 246 US 231

Continental TV Inc. V. GTE Sylvania Inc. (1977) 433 US 36