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Increasing the requirements to show antitrust harm in modernised effects-based analysis: an assessment of the impact on the efficiency of enforcement of Art 81 EC

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Citation for published version (APA):

Lankhorst, M. (2010). *Increasing the requirements to show antitrust harm in modernised effects-based analysis: an assessment of the impact on the efficiency of enforcement of Art 81 EC*. Amsterdam Center for Law & Economics.

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The Impact of Modernisation on Legal Certainty

5.1 Introduction

This chapter considers a number of important *outward features* of the Commission's modernisation programme. Our focus remains on its consequences for legal certainty. But, here, the emphasis is not on the *content* of the message sent by the legal standard (that is, case law, decision practice and guidelines) to firms as to the legality of their contracts. Instead, we inquire what sources of information are available to firms and what their relative value will be. In this regard, we pay particular attention to the implications of the shift from *ex ante* screening to *ex post* control. Adding to the concerns raised in Chapter 4, it is argued below that the way modernisation is currently being put into effect by the Commission works so as to reduce legal certainty, whilst increasing the need for it.

The Chapter is organised as follows. In Section 5.2 we study the number and types of decisions that have been adopted since the beginning of the substantive reforms and consider the impact on legal certainty. Next, in Section 5.3, we examine the effects of the procedural reforms. Section 5.4 makes the case for adjusting the effects-based standard of Art 81 EC to improve firms' ability to assess the legality of their intended contracts.

5.2 The impact of substantive modernisation

5.2.1 The shift from a rule-based to a standard-based system

By their very nature the Commission's substantive reforms put some amount of pressure on legal certainty. The shift in focus from legal form to actual effects signifies a change from a rule-based regime to reliance on a standard. Recall that these two forms of legal commands differ as to whether the law is given content *ex ante* or *ex post*.¹ The old approach was to list specific contractual clauses thought either to be distortive (black lists) or beneficial (white lists). After modernisation – in as much as individual assessment is concerned – only a general rule applies that prohibits harmful restraints. The determination of whether an agreement actually hurts consumers is left over to adjudication. This means that modernisation has changed the way in which firms assess the legality of contracts they intend to conclude. Rather than basing themselves on information that is available at that time, the clauses contained in the contract, they are called to make a prediction of its effects and, crucially, of the evaluation of those effects in legal proceedings.

The difference can be easily appreciated by considering the changes announced for both phases of the analysis under Art 81 EC (and by abstracting, for a moment, from our findings in Chapter 4 about how the modernised system functions in practice). We saw that prior to the reforms the Commission's approach under Art 81(1) EC was mixed. In many cases it relied on the notion of a restriction of commercial freedom to infer a violation of this provision. In other cases market structure was examined as well. As regards the first group of cases, it can easily be appreciated that predicting the outcome of the Commission's definition of the relevant market and its subsequent assessment of the agreement in light of market structure (the new approach) will be more difficult than assessing whether the agreement is such that it limits the freedom of the signatories or third parties (the old approach). With respect to the second group, it is important to point out that the way the Commission describes market structure analysis in its guidelines is different from its prior practice. Rather than finding a restriction if the parties' share of the market is larger than *de minimis* (5%), it is suggested that some more comprehensive form of

¹ See Chapter 3, Section 3.3.

assessment of market power will take place. By comparison, the outcome of the latter exercise will be harder to foresee.²

The effects of the reforms made to the analysis under Art 81(3) EC are similar. Rather than on the form given to the agreement, fulfilment of the first condition of this provision depends on whether it will produce tangible benefits in terms of cost reductions, innovation or the variety or quality of goods and services. Likewise, the outcome of the balance of positive and negative effects depends on the circumstances of the case and not on the question whether an agreement does or does not possess certain outward features. These observations indicate that, for potential offenders, the evaluation of just how much more permissive the new approach is will not always be straightforward. Two remarks must be made here, however.

The first is that the law regarding some types of agreements was already governed by a standard. The pre-modernisation block exemption regulations were directed at specific forms of agreement.³ Numerous types of vertical and horizontal agreements were not covered and, although legal form will have played a significant role in the individual assessment of these types of arrangements under Art 81(1) EC, the assessment under the third paragraph depended on case by case evaluation rather than predefined rules. The new approach in the field of horizontal cooperation remains fragmented,⁴ but Regulation 2790/99 covers all forms of vertical agreements. Firms that use arrangements that were previously not block exempted, such as selective distribution, and who do not exceed the relevant market share thresholds, must therefore currently find themselves in a better situation. It should be noted, also, that firms whose agreements will be individually assessed can now at least rely on the guidelines issued by the Commission.⁵

² The level of uncertainty firms experience will depend on their size. Initially, the larger firms are, the more uncertain they will be. As they head towards a position on the market associated with dominance, the level of uncertainty experienced as regards the outcome of the assessment under Art 81(1) EC will decrease. Given that the block exemption regulations confer *per se* legality upon agreements concluded by small and medium-sized enterprises, most firms subject to individual assessment – even those that do not exceed the thresholds by much – can be expected to experience some form of uncertainty.

³ See the discussion in Chapters 2, Section 2.3 and 2.4.

⁴ There are block exemptions for separate categories of agreements: Regulation 2659/2000, on the application of Article 81(3) of the Treaty to categories of research and development agreements, [2001] OJ L 304/7 and Commission Regulation 2658/2000, on the application of Article 81(3) of the Treaty to categories of specialisation agreements, [2001] OJ L 304/3.

⁵ See the discussion in Chapter 2, Section 2.4, and the Guidelines on vertical restraints, [2000] OJ C291/1; the Guidelines on the applicability of Article 81 to horizontal co-operation agreements (*supra*, footnote 229); the Notice on the application of Art 81(3) EC, [2004] OJ C101/97, and the Notice on the definition of the relevant market for the purposes of Community competition law, [1997] OJ C372/03.

Second, a loss of legal certainty is not necessarily an argument against the use of a legal standard. We saw, in Chapter 3, that standards are used to regulate complex factual situations. There can be little discussion that the impact of restrictive agreements concluded by larger firms, which depends on a multitude of possible factors, can be classified as such.⁶ In such cases clear rules are either prohibitively costly to formulate *ex ante* or seriously inaccurate in their *ex post* application and ultimate effects. In this regard, one can think of the compliance costs imposed on firms under the notification regime, which paid for the scrutiny of large amounts of innocuous agreements and of the straight jacketing effect of the black and white lists.⁷ Any inefficient behaviour resulting from uncertainty generated by the shift to a legal standard may, thus, wholly or partially be compensated for. It is very important to realise, also, that the more the standard is applied in practice, the more information firms will have at their disposal about the precise implications of the new approach (that is, the lower the level of uncertainty will be). In the following two sections we look at this latter issue in particular. We identify a number of limitations of the two principle sources of information available to firms, the Commission's guidelines and its decision practice, which fortify the concerns about legal certainty that were raised in Chapter 4.

5.2.2 The guidelines and developments in Industrial Organization

The Commission's Guidelines chart possibilities; they are less useful when it comes to assessing probabilities. Essentially, these documents identify a range of potential anti-competitive and beneficial effects of restraints and, thus, describe the general framework of analysis applied in individual assessment under the effects-based standard. For firms engaged in *ex ante* assessment of the legality of their agreement, particularly where restrictions are combined with efficiencies, more is needed. They require some indication of the likelihood of one effect prevailing over the other or, to complicate matters further, some indication of how the Commission is likely to appraise the ultimate result. Apart from discussion of the market share screens contained in the block exemption regulations, however, references to such estimations are virtually absent in the guidelines.

⁶ See the discussions in Chapter 2, Section 2.4.2, and Chapter 3, Section 3.3.1.

⁷ See the discussion in Chapter 2, Section 2.3.2, and in particular the text accompanying footnote 117.

This is understandable if developments in Industrial Organization and the way in which they were incorporated into policy are considered. Faced with a gradually swelling stream of often competing explanations for known forms of behaviour, European policymakers have apparently adopted a somewhat cautious stance in refining substantive law. Although the Commission has internalised the models advanced by economists as instruments for case by case analysis, it is reluctant to commit, in advance, to any specific outcome. The following, stylised, description of developments in the Industrial Organization branch of economics in more detail will help to substantiate this argument.⁸

Early thought, Ordo-liberalism, and the Harvard School

Discussions of the concept of competition in economics generally start with the work of the classical economist Adam Smith.⁹ In his book entitled *The wealth of nations* (published in 1776) he argued that the process of competition is a force that drives economies to the best outcomes feasible or, in other words, to a harmony of all interests. If all sellers are free to rival with their colleagues over the prospects of gain that comes with satisfying the needs of buyers and if all buyers are free to choose what they consider to be the best offer, that is, if all are free to act in their own best interest, society as a whole will benefit. Competition, in this view, is as an 'invisible hand' that reconciles the pursuit of private interests with the social good. The emphasis on personal freedom in this classical economic theory of competition has direct implications for the role of the state in the economy. Classical economists generally considered that this role should be limited to ensuring that all persons are able to exercise their freedoms, notably by protecting law and order.¹⁰

Over time, as economic science progressed, different schools of thought have emerged concerning competition and the scope for government intervention in market behaviour. The origins of these schools can be traced back to a fundamental debate

⁸ The following discussion provides a brief and incomplete overview of the developments in thought about competition. The focus is on the main traditions that have influenced European antitrust policy (Ordo-liberalism, the Harvard and Chicago Schools and, to a lesser extent, post-Chicago developments), which is sufficient to illustrate that clear rules regarding agreements that exhibit multiple tendencies (positive and negative) are difficult to draw up *ex ante*. For detailed discussions of developments in economic thought about competition, Hildebrand (2002), Neumann (2001), and Van Cayseele and Van den Bergh (2000).

⁹ See e.g. Van Cayseele and Van den Bergh (2000), Hildebrand (2002: 110), and Scherer and Ross (1990: 17). See e.g. Neumann (2001), McNulty (1990), and Van Cayseele and Van den Bergh (2000) about Smith's predecessors and contemporaries in thinking about competition.

¹⁰ See Hildebrand (2002: 110) and more generally Gerber (1998: Chapter II).

that was waged by economists, both in Europe and the US, in the second half of the 19th century. This was a debate about the proper way to gain insights about the effects of competition and restrictions on it.¹¹ On one side were scholars that stood in the Anglo-American tradition of neo-classicism, who combined a theoretical approach with a strong distaste for government intervention.¹² Fundamentally changing the discourse of economics, they developed a mathematical expression of Smith's theory of the invisible hand, in the form of the model of perfect competition, which played a crucial part in demonstrating the ill effects of interference.¹³ On the other side were the so-called historicists; a school of German origin.¹⁴ Although they accepted the basic understanding of the forces that shape market behaviour that was developed in classical economics,¹⁵ they were deeply distrustful of the explanatory powers of models and abstract principles because in practice all markets show some degree of imperfection. Instead, historicists emphasised detailed observation of economic behaviour in its historical and social context. This approach – that looked at competition with fewer pre-conceptions – left more room for government intervention. In Germany, in particular, historicism instilled a tradition of cartel regulation (as opposed to prohibition) that would last until the Second World War.¹⁶

¹¹ The following description is to a considerable extent informed by Gerber (1998). In Chapter II, he provides a detailed account of the impact of industrialisation and the world wide economic depression of the 1870s and 1880s on popular and academic thought about competition. He offers explanations, also, relating to the history and cultures of these countries, for why scholars in the UK, Germany, and Austria developed their thoughts in different directions.

¹² This 'Methodenstreit' also involved scholars working in the Austrian neo-classical tradition. In this regard, see Chapter III of Gerber (1998) and Hildebrand (2002: 154). Several members of this school fled to the US and the UK during the Nazi-period. The works of these neo-Austrians is generally more radical than that of the Chicago School discussed below.

¹³ The work by the British scholar A. Marshall played a crucial role in this regard. See Hildebrand (2002: 112) and Zablotsky (1995). The turn to mathematics in economics somewhat shifted the interest from competition as a process to competition as the state of a market. See e.g. Van Cayseele and Van den Bergh (2000), Neumann (2001), and Hildebrand (2002). Recognising that few real-life markets are perfectly competitive, scholars working in this tradition developed a considerable number of other models to describe the outcomes generated by departures from this ideal. These include oligopoly (pioneered by A. Cournot and J. Bertrand) monopolistic competition (associated with the names P. Sraffa, E. Chamberlin and J. Robinson), monopoly and monopsony.

¹⁴ See Gerber (1998: 84). The Historical School's central claim was that economic knowledge was historically conditioned and that, as a result, abstract general principles concerning economic behaviour – such as Smith's invisible hand – had limited value. Economic conduct occurred within specific cultural and historical contexts, they argued, and it could not be understood without understanding these contexts.

¹⁵ See Gerber (1998: 86).

¹⁶ On pre-World War II competition policy in Germany see Chapters II, IV and V of Gerber (1998). See in particular his discussion (at p. 91 and following) of the Saxon Wood Pulp case of 1897, which established the legality of cartels under German law and remained authoritative for more than 50 years.

It was in reaction to these failed policies of the Weimar period and the abuses of the Nazis that a group of lawyers and economists at the University of Freiburg developed a body of thought concerning the economy, competition, and law that was to have a profound impact on European antitrust policy.¹⁷ These scholars, often referred to as Ordo-liberals, faulted historicists for being unguided in their analysis and theoretical economists for being out of touch with the complexities of real-life markets.¹⁸ In their view, also, the strong links that had existed between industry and the state contributed significantly to the derailment of Weimar-Germany's political institutions in the 1930s.

Law played a crucial part in the bold new theory that the Ordo-liberals developed for ordering the state and the economy, notably by regulating the interaction between these two spheres.¹⁹ Thus, the scope for state intervention in the market would have to be clearly circumscribed and, more importantly, the law would be used as an instrument to ensure the dispersal of economic power. This is a vital element of the Freiburg agenda. Law and law enforcement were intended to reshape the economy and create the conditions of perfect competition.²⁰

The primary function of antitrust law in this legal framework was to rigorously protect the contractual freedom of market participants, so that private regulation of business affairs would not substitute competition. This idea is clearly reflected in the wide notion of a restriction that the Commission adopted to the analysis under Art 81(1) and in the design of the first generation of block exemption regulations.²¹ This influence of Ordo-liberal thought on EU antitrust is explained, at least in part, by the fact that several of its supporters played an important role in the negotiating process

¹⁷ For more detailed discussions on Ordo-Liberal thought and its influence on EU antitrust, see Chapter VII of Gerber (1998), Hildebrand (2002: 158), Razeen (1996), Streit (1992), and Möschel (1989).

¹⁸ Both approaches in economics, empirical and theoretical, which in their view had led largely separate lives, had to be integrated. In this regard, thinking in terms of 'economic orders' was fundamental to members of the Freiburg School. The basic idea was that that real-life markets, which – though endlessly complex, differentiated, and conditioned by historical circumstances – were governed by fundamental ordering patterns. These ordering patterns can be thought of as the rules of the game in an economy: how are values assigned to goods, who are the decision makers, what constraints do they face, etc. The task for economists, according to this tradition, was to discover these fundamental patterns.

¹⁹ Ordo-liberals realised that many rules of the game in an economy (in this regard, see footnote 62) were in fact anchored in law. They had to be, in a system based on free competition, since unchecked private power may lead to the destruction of the system itself. Government policies were needed to create and maintain a competitive system (in this regard, they used the distinctive term *Ordnungspolitik*). This realisation is at the core of the close link between law and economics in Ordo-liberal thought. In this regard, see Gerber (1998: 246), Razeen (1996), and Streit (1995: 678).

²⁰ See Gerber (1996: 250 a.f.).

²¹ See the discussions in Chapter 2, Section 2.3.

that lead to the founding of the EC Treaty and that others went on to occupy important positions within the new competition directorate.²²

Ordo-liberalism, however, was not the sole influence on the concept of competition that underlies EC antitrust policy. The ECJ's earliest cases on effects-based analysis, such as *Société Technique Minière*²³ and *Brasserie de Haecht*,²⁴ prescribe a broader framework of analysis in which legal form is but one of the circumstances to be taken into account. These and later cases on Art 81 EC, in particular the 1999 ruling in *Delimitis*,²⁵ appear to reflect concepts developed in the Harvard tradition in Industrial Organization.²⁶

Early work at the Harvard School drew considerable inspiration from German historicism.²⁷ By comparison, however, it was less hostile to theory and developed a more focused research agenda. Harvard scholars shared with neo-classicists the fundamental idea that the number and characteristics of the participants on both sides of the market determine their behaviour and thus the outcomes generated on that market (in terms of prices, quality, and innovation). But, rather than trying to capture variations in structure in rigid models to understand the nature of the outcomes that each type (monopoly, oligopoly, differentiation) would generate, they engaged in empirical research of actual markets and industries to try to identify what combination of these factors leads to unacceptable results or, in other words, what would constitute *effective* competition.²⁸ Initially, this involved mostly detailed case studies of particular industries, mostly those where antitrust proceedings had produced the

²² See Gerber (1998: 263 a.f.).

²³ *Société Technique Minière v. Maschinenbau Ulm*, Case 56/65, [1966] ECR 35.

²⁴ *Brasserie de Haecht v. Wilkin*, [1967] ECR 407).

²⁵ *Stergios Delimitis v. Henninger Bräu*, [1991] ECR I-935).

²⁶ This is different for Art 82 EC. The concept of abuse employed there, to prevent dominant firms from engaging in conduct that market forces would not have allowed them to under competitive conditions, has strong roots in Ordo-liberal theory. Regarding Ordo-liberal thought on dealing with dominance, see Gerber (1998: 252). For authors who argue that EU antitrust law in general should be interpreted in light of the Harvard tradition, see Van Cayseele and Van den Bergh (2000), and Martin (2001).

²⁷ See Hovenkamp (1989-1990).

²⁸ This term was introduced by J.M. Clark. In earlier works, notably Clark (1941) he used the term workable competition. The basic idea behind this concept is the following. The assumptions underlying the neo-classical model of perfect competition are so exacting that they will never be met in real-life markets. At the same time, it was realised that even imperfectly competitive markets might perform in a way that could not be improved by means of government intervention. Clark, therefore, set out to identify factors that led to the closest thing to perfect competition that was possible in the real world. For a discussion, see Hildebrand (2002: 120). It is worth noting, also, that this term is frequently used in the ECJ's case law. See e.g. *Metro SB-Grossmärkte v. Commission*, case 26/76, [1977] ECR 1875, at point 20 a.f.

revealed the necessary information.²⁹ Around the middle of the 20th century, these efforts changed in character. The first step in this process was the development of the Structure-Conduct-Performance framework.³⁰ The next step came with the turn to inter-industry statistic studies, which made it possible to analyse data drawn from many markets.³¹ This approach was used in particular to test the hypothesis that high levels of concentration were related to elevated profits and, thus, poorer performance.³² The many hundreds of studies carried out in this tradition were, for a long time, generally interpreted to confirm this hypothesis. Later work (roughly from the early 1980s onwards) raises questions about the correct inferences to be drawn from these studies and indicates that the correlation is rather between sellers' individual market shares and profits.³³

Still, the general implications for the scope of government intervention in markets are clear: antitrust enforcers should focus on markets with a structure that is weakened by the presence of large firms. There can little doubt that this line of work provides much of the basis for the emphasis on structural analysis in European antitrust.³⁴ Note that the Harvard conception of the competition laws is considerably narrower than that advanced by Ordo-liberals, who, in their purest form, oppose any restriction of commercial freedom regardless of firm-size. A third source of inspiration for the generic (economic) objectives underpinning EC antitrust lies in the teachings of scholars working in the Chicago tradition. These scholars, who were able to demonstrate the potential for generating efficiencies of a range of practices whose effects on structure were regarded as suspicious by Harvardians, advanced yet another

²⁹ See Schmalensee (1989: 952) and Hovenkamp (1989-1990).

³⁰ The Harvard-based economist E. S. Mason was instrumental in the development of this framework. For a discussion of his work, see Hildebrand (2002: 126 a.f.) As we saw in Chapter 2, Section 2.4.2, the SCP framework of analysis is based on the idea that the results achieved on a market (the welfare consumers derive from it, as well as the level of employment, and the advances in R&D), are dependent on the conduct engaged in by mainly the sellers on that market (pricing, investment, advertising etc), and this in turn is determined by the structure of a market (particularly the number and size of market participants, and entry conditions).

³¹ The initiative, in this regard, was taken by the economist J. Bain. For a discussion, see Chapter 11 of Scherer and Ross (1990), Schmalensee (1989), and Hildebrand (2002: 130).

³² More specifically, the main hypothesis tested in this tradition was that given the pricing behaviour expected under monopoly or tight oligopoly, the average profit return realised by firms in highly concentrated industries will tend to be significantly higher than that of firms in more competitive industries (that is, with larger numbers of smaller sellers active on the market). See Chapter 11 of Scherer and Ross (1990).

³³ See Chapter 11 of Scherer and Ross (1990), Schmalensee (1989), and Van Cayseele and Van den Bergh (2000).

³⁴ See e.g. Hildebrand (2002), Martin (2001), and Van Cayseele and Van den Bergh (2000).

policy agenda, one that left almost no room for government interference in business behaviour.

Chicago and game theory

Like Ordo-liberalism, the Chicago Movement, which took off in the 1950s, was the fruit of close co-operation between economists and lawyers. The School did not start with a universal theory of antitrust, however.³⁵ Initially its participants challenged only specific elements of Harvard thought, basing themselves on neo-classical price theory. They used tailor-made models to examine the implications of restrictive practices, assuming always that firm behaviour is driven by a desire to maximize profits. By searching for rational explanations of firm behaviour, Chicago scholars were able to show that many policy implications derived from previous studies, which underemphasised conduct so as to focus on structure instead, led to over-inclusive results.³⁶

Telser's (1960) discussion of resale price fixing provides a classical example. Traditionally this practice was understood as an aid to collusion by dealers. If manufacturers are motivated by the desire to maximize profits, however, what reasons would they have to encourage that? In principle, raising prices at the retail level should be expected to hurt their business. To explain why minimum resale price maintenance could be attractive to them, Telser advanced the free-rider argument. The extra income for retailers may be intended to provide retailers an incentive to offer services that increase overall demand. The same argument has since frequently been advanced in relation to exclusive dealing and exclusive territories.³⁷ Efficiency explanations were similarly proffered for a host of other practices, including tying,³⁸ and vertical integration.³⁹

On the basis of these studies a more general agenda for antitrust emerged.⁴⁰ It reflected a much reduced image of the circumstances under which market failure may occur. Crucial in this regard, was the structuring of the notion of market failure by

³⁵ See Page (1989: 1231).

³⁶ Id.

³⁷ See Marvel (1982).

³⁸ See e.g. Director and Levi (1956), and Kenney and Klein (1983).

³⁹ See e.g. Bork (1978).

⁴⁰ The first encompassing overview of this agenda was provided by Bork (1978).

means of the concept of market power.⁴¹ Market power, as was suggested above, is the power to profitably restrict output, which harms consumers because they have to pay more, or have to turn to second-choice products. In addition, the scope for inferring such power was taken to be quite narrow, as Chicagoans defined entry barriers considerably more narrowly than was done in traditional theories.⁴² From a long-term perspective, it was argued, most markets could be seen to be (near to) perfectly competitive, despite temporary bouts of concentration.⁴³ Such concentration is, in fact, most likely to be indicative of efficiency. The resulting scope for antitrust intervention, as perceived by Chicago scholars, was extremely limited in comparison to the policy agenda advocated by the Harvard School. A telling example is provided by Posner's (1981) call to treat certain vertical restraints as *per se* legal.⁴⁴

The influence of this school of thought is clearly reflected in the various documents in which the Commission describes its modernised approach to competition analysis. The Vertical and Horizontal Guidelines show that the Commission is open to many of the new efficiency explanations, such as the free-rider argument. But its prior beliefs as to the relative frequency with which a certain type of practice will produce positive and negative effects have evidently not been neatly rearranged along the lines set out by Chicago. The new generation of block exemption regulations confers *per se* legality upon vertical restraints and certain forms of horizontal co-operation, but only when small and medium sized enterprises are involved. Where individual assessment is concerned, it is obvious that the new efficiency scenarios are not considered to cancel out the old restrictive interpretations.

⁴¹ See e.g. Easterbrook (1984), for the importance attached to the concept of market power as a 'screen' in US antitrust analysis.

⁴² For a discussion on this topic see Van Cayseele and Van den Bergh (2000). Bain (1956) argued that entry is conditioned by the advantages of established sellers in an industry over potential sellers and identified three types of advantages (barriers): economies of scale enjoyed by incumbents (which force the new firm either to invest in a very large plant which would depress price levels or to produce smaller quantities at higher costs), product differentiation and absolute cost advantages. Stigler (1968), on the other hand, defined entry barriers exclusively as production costs that must be borne by an entrant but not by an incumbent.

⁴³ For further references on the theory of contestable markets, see the discussion in Van Cayseele and Van den Bergh (2001).

⁴⁴ At the time, adherents of the Harvard School (and policymakers) were suspicious of vertical restraints. They could lead to higher prices charged by unchecked distributors, facilitate collusion amongst them, and could serve to fracture the Common Market, to name just a few. A supplier would normally have no legal interest in protecting its dealers from competition between each other. The lower the price they charge, the more units would be sold, and, *ceteris paribus*, the more profit would be made upstream. Only under specific and limited circumstances, for example to protect an investment in the distribution by the manufacturer or to secure such an investment by the distributor, could an exception be granted. See Van den Bergh (1996).

Rather, the two are seen as alternative possibilities, neither of which can be ruled out in advance. Understandably, then, the Guidelines indicate the conditions that must pertain in order for a certain effect to materialise,⁴⁵ but remain inconclusive as to the outcome in cases where opposing effects occur (for example, a restriction of inter-brand competition in a distribution agreement that contributes to improving quality).

It is worth mentioning that the results of more recent research in Industrial Organization can only work to reinforce this effect. The distinguishing characteristic of this contemporary work lies in its reliance on game-theory. Game-theory delves deeper in understanding firm behaviour than price-theory does, by analysing the different strategies that market players can adopt and underscoring the importance of the information available to them. Topical as most of these models are, this approach does not yield a unified vision of the scope for antitrust intervention. Krattenmaker and Salop (1986), for instance, show circumstances under which vertical restraints can be used as a strategy to gain or fortify market power.⁴⁶ Other studies, however, have clearly confirmed efficiency explanations advanced by Chicago.⁴⁷

Implications for the usefulness of the Guidelines

Each of these different schools advances a different theory of what constitutes harm to competition, what factors may contribute to causing such harm, how frequently it may be expected to occur (*ex ante*), and how instances of market failure may be identified (*ex post*). The Commission's guidelines – which set forth ideas that appear to fit in the Harvard tradition and ideas that fit in the Chicago tradition – reflect this multiplicity. The Notice on the application of Art 81(3) EC describes the general framework of analysis. The Vertical and Horizontal Guidelines and the Market Notice fill in the picture by listing different factors and associated categories of evidence that may have a bearing on the ultimate outcome.⁴⁸ Understandably, given the range of possibly relevant considerations, they do not indicate in any measure of detail how different

⁴⁵ See e.g. paragraphs 103 to 119 of the Vertical Guidelines (*supra*, footnote 5).

⁴⁶ In our discussion of the case of *Van den Bergh Foods* ([1998] L246/1), above in Chapter 4, Section 4.3.2, we saw that the Commission's argumentation in this case could be said to be inspired on the 'raising-rivals'-costs-scenario' that these authors developed. By comparison, the use of game theory is more common in the US. See e.g. Ten Kate and Niels (2002), Scherer (2001), Hovenkamp (2001), Coate and Fischer (2001), Pierce (2000-2001), Brennan (2000-2001), Kobayashi (1997), and Sullivan (1995).

⁴⁷ See the discussion by Van Cayseele and Van den Bergh (2001).

⁴⁸ *Supra*, footnote 5.

combinations of such factors will be appraised.⁴⁹ This remains a question for ex post assessment.

The above should not be taken to suggest that the description of the analytical framework laid out in the Guidelines can be of no use to potential offenders. The point made is that – on their own – they cannot fully compensate for the deficit in legal certainty that was created by the shift from a rule-based system to a genuine legal standard. Decisions taken after the reforms – and reflecting these reforms – are an indispensable complement. This is because they provide essential information on how the Commission proceeds in the evaluation of cases where multiple tendencies are present, in particular by giving hints about the probability with which one or several of these tendencies can be expected to outweigh others in given circumstances. Together, a substantial body of decision practice – or at least an expanding body of precedents – and a set of detailed guidelines could be expected to keep the negative effects on legal certainty caused by the almost simultaneous substantive and procedural overhauls in check. The following sub-section takes a closer look at the available post-reform decision practice.

5.2.3 Substantive modernisation in practice

A decade after modernisation was announced in guidelines and notices, it can be said that there is a general paucity of insightful decisions reflecting the new approach (and, as we saw, much of what is available suggests that modernisation is not practiced exactly as preached). Let us start with the small number of detailed decisions. To begin, a distinction should be made between the value of the information that potential offenders can be expected to glean from infringement decisions on the one hand and exemption or commitment decisions on the other. As a rule, infringement decisions will offer considerably more insight. This is the case for the simple reason that infringement decisions tend to be much more thoroughly reasoned on matters of fact and economic evaluations. Particularly commitment decisions, the equivalent of the exemption with conditions under the new enforcement regime, tend to be motivated in abbreviated form.⁵⁰ It is indicative, for instance, that the commitment

⁴⁹ It should be mentioned that the Horizontal Guidelines (supra, footnote 5) do contain examples illustrating the interaction between different factors. As is indicated by several of the organisations that reacted to the Commission's consultation on the functioning of its policies with regard to horizontal cooperation, these are quite abstract and, therefore, of little use in deciding complex cases.

⁵⁰ See Art 9 of Regulation 1/2003, [2003] OJ L1/1.

decisions thus far adopted count no more than 13 pages on average, compared with 241 pages for the most recent infringement decision.⁵¹ This difference in the intensity of scrutiny is understandable, given that in the former type of case the probability of appeal, and thus the risk of being overturned, is substantially reduced. It should be realised, also, that exemption decisions need not indicate the outer limit of the law. In the European context, such a decision may well sanction an effectively innocuous agreement; one that is less restrictive than ultimately permissible.

Infringement decisions are very few, however. Only four of the 32 pure effects-based cases listed in Appendix A lead to a finding that Art 81 EC was violated; one concerning a vertical restraint and three relating to horizontal co-operation. Four of the 28 remaining decisions involve commitments and 24 are exemptions.

The savings made in the motivation of the latter two groups of decisions affect a number of aspects of the Commission's analysis that are crucial to potential offenders in assessing the likelihood that their agreement will be challenged. As regards the assessment under Art 81(1) EC, it was shown in Chapter 4 that the Commission seldom completes the analysis of market power in the way described in its Guidelines.⁵² It defines the relevant market, at times moves over to consider market structure as well, but generally fails to develop a clear theory of harm that links the agreement to the structure of the market. Closely related is the fact that the Commission continues to rely on the legalistic approach that modernisation was meant to do away with. In several exemption decisions a restriction of contractual freedom is the only real argument that the Commission advances to support its finding that the agreement falls foul of Art 81(1) EC.⁵³ Lastly, in quite a number of cases that result in a finding that Art 81(3) EC applies, balancing isn't really engaged in at all. In such cases, once the Commission finds plausible efficiencies, it concludes that the second condition of the third paragraph is met, without drawing the results of the investigation under Art 81(1) EC into the analysis.⁵⁴

⁵¹ The following commitment decisions (listed in Appendix A) were looked at: *DFB* (Commission decision of 19 January 2005 in case COMP/C-2/37.214), *PremierLeague* (Commission decision of 22 March 2006 in case COMP/C-2/38.173), *Repsol* (Commission decision of 12 April 2006 in case COMP/B-1/38.348), and *Cannes* (decision of 4 October 2006, published on the Commission's website). The number of pages of commitment decisions is given without counting the description of the commitments proposed by the parties. The infringement decision referred to is *Master Card* (decision of 19 December 2007, published on the Commission's website).

⁵² See Chapter 4, Section 4.3.1.

⁵³ *Id.*

⁵⁴ See Chapter 4, Section 4.3.2., and the cases referred to in footnote 125 of that chapter.

The record of infringement decisions also leaves crucial issues unaddressed. A detailed discussion of the possible implications of the agreement for consumer welfare (or of a differently conceived kind of harm) and the balancing of opposing effects is often avoided by claiming indispensability, that is, by arguing that – whatever the precise impact of the agreement – a less restrictive alternative was available to achieve the same efficiencies.⁵⁵ It is particularly important, also, to mention the cases of *Master Card*⁵⁶ and *Morgan Stanley / Visa*⁵⁷, since both infringement decisions were adopted after the publication of the Commission’s Guidelines on Art 81(3) EC in 2004.⁵⁸ We saw that these guidelines offer the most complete and integrated overview of the framework of analysis that the Commission relies on in effects-based analysis under Art 81 EC and that they clearly identify the effects produced on consumer welfare as the relevant benchmark in the assessment of restraints. In neither of these otherwise elaborately motivated decisions were arguments by the defendants – to the effect that the Commission’s allegations under Art 81(1) EC ignored clear indications that the agreement left output unaffected – picked up and subjected to serious scrutiny.⁵⁹ A crucial element in the new conceptual framework – how does the Commission establish that harm has indeed occurred – is thus left unclear. This is especially problematic since this element is somewhat underdeveloped in the guidelines themselves, which puts emphasis on aspects of the analysis that are dealt with at a later stage under the scope of Art 81(3) EC.

To understand the effects on potential offenders of the situation described above, we must first of all realise that exemption and commitment decisions are generally not simple clearances. A considerable number involves an implicit prohibition. In 19 of the 28 cases that fall into one of these categories, the clearance is subject to conditions of some form. In 11 of these cases the conditions involve obligations for the parties to refrain from certain type of behaviour or to engage in some form of action, thus

⁵⁵ See e.g. the decisions in *Van den Bergh Foods* (supra, footnote 46) and *EATA* ([1999] OJ L193/23), where the indispensability played an important role. Indispensability was also of crucial importance in two border-line infringement decisions that were not included in the list of effects-based decisions in Appendix A: *JCB* ([2002] OJ L69/1) and *Belgian Architects* (decision of 24 June 2004, published on the Commission’s website).

⁵⁶ Supra, footnote 51.

⁵⁷ Decision of 3 October 2007, published on the Commission’s website.

⁵⁸ Notice containing Guidelines on the application of Art 81(3) EC, [2004] OJ C101/97.

⁵⁹ See the discussion of the decision in the case of *Master Card* (supra, footnote 51) in Chapter 4, Section 4.3.2 (this case, and the point made here, is extensively also discussed in Chapter 7, Section 7.2). As regards the case of *Morgan Stanley / Visa* (supra, footnote 57), see Chapter 4 (at footnote 70) and, in particular, the extensive discussion in Chapter 7, Section 7.2.

modifying the original agreement. In addition, in 22 of these cases the original version of the agreement was amended during the proceedings so as to remove objections raised by the Commission.⁶⁰

Firms would be unwise, therefore, to ignore this part of the Commission's practice and focus solely on infringement decisions to discover the outer boundary of the law. As suggested, however, the Commission tends to motivate these decisions in abbreviated style that frequently invokes associations with the old expansive approach. And genuine infringement decisions – not entirely free of confusing elements themselves – appear to point in the opposite direction, by using language that is compatible with the framework of analysis set out in the Commission's new generation of guidelines. As a consequence, it is submitted, potential offenders will experience uncertainty about the legality of a wider range of behaviour than before. In particular, they will reckon with a non-negligible probability of being challenged over a range of behaviour that stretches between the old legal standard and the more permissive prescriptions of these guidelines. With help of the conceptual model developed in Chapter 3 it is argued below in Section 5.4 that this can be expected to lead to the conclusion of inefficient contracts. First, however, the reforms made to enforcement are examined, which suggests that potential offenders' demand for legal certainty has increased.

5.3 The impact of procedural modernisation

Procedural modernisation did not directly alter the calibration of the legal standard, as the substantive reforms did. But by changing the timing of legal intervention, from *ex ante* to *ex post*,⁶¹ it has affected firms' capacity to predict the outcome of proceedings. At the same time, by raising the level of expected fines the importance of being able to correctly assess the legality of intended agreements – that is, the demand for legal certainty – has grown.

It can easily be appreciated that concluding a contract on the basis of one's best guess as to the way its effects on the market would eventually be evaluated carries

⁶⁰ See Appendix A.

⁶¹ On the optimal timing of legal intervention, see notably Wils (2001, and 2004). Note, however, that these works compare the efficiency of *ex ante* screening and *ex post* intervention in the context of EC antitrust. The aim of this thesis, however, is not to determine whether the present enforcement regime produces better results than the former, but simply to evaluate the functioning of the present system as it has been put into practice.

more risk than seeking the Commission's endorsement before implementation. This was, in fact, one of the main points of critique that was raised against the Commission's proposal for reform of the enforcement regime.⁶² In reality, however, the contrast between the two systems is not quite as stark as it might seem. Due to the constraints on the Commission's capacity only a fraction of notifying firms actually got a formal clearance or exemption decisions; the bulk had to make do with the lower level of certainty provided by a comfort letter.⁶³ In addition, the span of time between notification and the adoption of such a formal or informal decision was generally much too long to wait with implementing the agreement.⁶⁴

But even if the old system did not swiftly provide full certainty about the legality of contracts, the decrease in legal certainty due to the introduction of Regulation 1/2003 is apparent.⁶⁵ Contacts between firms and the Commission played an important role in notification proceedings. A survey conducted by Neven et al. (1998) found that 69% of firms involved in notification procedures had contacts with the Commission before submitting their form. Such contacts allowed firms to discover the Commission's views on specific features of the intended agreements and to make the modifications necessary to remove obstacles to clearance. The survey showed that 59% of pre-notification contacts led to modifications. In 96% of the cases the modified version was cleared. Where necessary, such contacts continued after notification. We saw above that in 79% of decisions taken in the period between the two reform processes the original version of the agreement was amended during the proceedings so as to remove objections raised by the Commission.⁶⁶

Under the new system the possibilities for consulting the Commission prior to implementation have been seriously reduced. The only real option available to firms is to request a so-called guidance letter.⁶⁷ There is no provision in Regulation 1/2003 concerning such letters, but the possibility that firms wish to seek informal guidance

⁶² In this regard, see the Commission's summary of the observations submitted to its white paper for reform of Regulation 17/62 (of 29 February 2000, published on the Commission's website) and e.g. Pirrung (2004), Hawk and Denaeijer (2001), Jenny (2001), Bartosch (2001), Gustafsson (2000), Holmes (2000), Möschel (2000), Paulweber (2000) and the discussion in Chapter 2, Section 2.5.

⁶³ This was an informal decision indicating that the evidence available to the Commission gave no grounds for starting proceedings. See Chapter 2, Section 2.3.2.

⁶⁴ See the discussion in Chapter 2, Section 2.3.2.

⁶⁵ *Supra*, footnote 50.

⁶⁶ That is, 22 out of 28. See the text accompanying footnote 60.

⁶⁷ It should be mentioned, also, that pursuant to Art 10 of Regulation 1/2003 (*supra*, footnote 50) the commission may still adopt an express clearance decision. No such decision, however, has been adopted since the introduction of this regulation in 2004. It seems understandable that, in order to make the system of *ex post* control work, the Commission intends to use this instrument sparingly.

from the Commission is considered in the preamble.⁶⁸ This recital was introduced at the very end of the discussion in the Council, in order to meet the concerns expressed by some delegations and by many commentators.⁶⁹ The Commission has given effect to these words by issuing a notice, which imposes a number of strict conditions that must be met before a request for informal guidance can be made and emphasises the Commission's margin of discretion in evaluating the appropriateness of issuing a guidance letter.⁷⁰ The most important of these conditions are that the question must be novel and significant both to the parties and from the perspective of the development of Community competition law; in addition, it must relate to a real case (no hypothetical) and must be accompanied by sufficient facts so that an answer can be given without gathering further information.⁷¹

Until December of 2008, however, few requests for guidance have been made and no guidance letters have been issued.⁷² Given the many calls that have been made in response to the Commission's public consultation on the functioning of Regulation 1/2003 for increased guidance,⁷³ the explanation for these facts must probably be sought in the considerable risks involved with filing such a request.⁷⁴ The notice expressly indicates that the Commission remains free to initiate formal proceedings in relation to the facts described in the request,⁷⁵ that it may use information contained in the request in subsequent proceedings even if it is withdrawn,⁷⁶ that the Commission may share the information contained in the request with national competition authorities⁷⁷ and that if a guidance letter has been issued the Commission may subsequently re-examine the case.⁷⁸ Finally, it should be noted that the notice does not bind the Commission to a timeline for adopting a guidance letter.

⁶⁸ *Supra*, footnote 50, at recital 38: 'Legal certainty for undertakings operating under the community competition rules contributes to the promotion of innovation and investment. Where cases give rise to genuine uncertainty because they present novel or unresolved questions for the application of these rules, individual undertakings may wish to seek informal guidance from the Commission. This Regulation is without prejudice to the ability of the Commission to issue such informal guidance.'

⁶⁹ See Gippini-Fournier (2008: 54).

⁷⁰ Commission Notice on informal guidance relating to novel questions concerning Articles 81 and 82 of the EC Treaty that arise in individual cases (guidance letters), [2004] OJ C101/78.

⁷¹ *Id.*, at paras. 8-11.

⁷² See e.g. Gippini-Fournier (2008) whose report dates from June. For the additional period a search was made on the Commission's website.

⁷³ See the discussion of this consultation round in the next section.

⁷⁴ See e.g. Gippini-Fournier (2008). The same point is made in numerous observations submitted to the Commission in response to its consultation on Regulation 1/2003 (*supra*, footnote 50).

⁷⁵ *Supra*, footnote 70, at para. 11.

⁷⁶ *Id.*, at para. 18;

⁷⁷ *Id.*, at para. 16;

⁷⁸ *Id.*, at para. 24;

It is important to realise that the reduced possibilities of consulting the Commission has significant implications for the value of accuracy in adjudication. In a system based on broad spectrum *ex ante* screening, compliance does not necessarily depend on a high level of precision in the analysis and the motivation of decisions. To begin with, existing decision practice is not the sole source of guidance for firms designing new commercial agreements, possibly not even the most important source. And in the event that imperfections in existing decisions do lead potential offenders to inefficient results (that is, to sign undesired contracts), these can easily be filtered out in the notification process.

Under *ex post* control firms can no longer count on the Commission to provide them with ‘quick-look’ advice tailored to their specific circumstances. Therefore, the importance of existing decisions in evaluating the legality of an intended agreement increases substantially. Needless to say that with it grow the consequences of vaguely argued decisions; these are more likely to lead subsequent potential offenders to implement inefficient agreements. These difficulties for potential offenders are compounded by an increase in the level of expected fines.

Under the old regime firms were granted immunity from fines upon notification.⁷⁹ The rationale for this form of leniency is the following. Firms that were uncertain about the legality of their agreement might try to conceal it from the Commission out of fear for fines. The guarantee that no sanctions would be imposed served as an incentive for such firms to subject their contracts to scrutiny by the Commission. As a consequence, firms were relatively free to seek the edges of what they considered legal in designing and notifying their agreements.⁸⁰ If need be, they could always negotiate with the Commission during the course of the proceedings so as to fine tune the final version.

Regulation 1/2003 does away with pre-screening and extends the system of *ex post* control that was reserved for non-notified agreements to the field of effects-based analysis.⁸¹ Because in such a system only a fraction all agreements concluded by European firms can be expected to be scrutinised, the threat of sanctions is essential to create sufficient deterrence.⁸² As a consequence, seeking the edges of legality will

⁷⁹ See Art 15(5) of Regulation 17/62, [1962] OJ 13/204, and the discussion in Chapter 2, Section 2.3.1.

⁸⁰ In this sense, see Neven (2001) and Pirrung (2004).

⁸¹ *Supra*, footnote 50.

⁸² Barros (2002) and Neven (2001) make the same argument. Note that, since the introduction of Regulation 1/2003 (*supra*, footnote 50) fines have been imposed only in the case of *Morgan Stanley /*

involve more risk.⁸³ Arguably, the increased threat of fines can be linked to the dearth of well motivated effects-based decisions that was reported above. The higher the sanctions they face, the more willing defendants will be to offer commitments, and the lower the probability that its decision will be appealed, the fewer incentives the Commission will have to devote resources to an elaborate motivation.⁸⁴ Paradoxically, therefore, although both the procedural and the substantive reforms have increased potential offenders' demand for legal certainty, they engender the adoption of scantily reasoned decisions. In the next and final section of this chapter discusses ways to remedy this problem.

5.4 The case for increased requirements to show harm

The arguments presented in Chapters 4 and 5, which do not challenge the reasoning that led the Commission to reform European antitrust policy, raise questions about the way this programme was put into practice. Let us briefly summarise these arguments.

Modernisation as practiced

Over the course of the past century, Industrial Organization scholars have advanced competing explanations for a great number of vertical restraints and horizontal co-operation agreements. In many instances – specifically, in those cases that policymakers subject to effects-based analysis – neither outcome can be discounted in advance. In response, the substantive reforms eventually shifted the focus in antitrust proceedings from the terms of the agreement (a rule-based approach) to the effects that are actually produced (a standard). This has clear implications for the level of certainty with which firms can assess the probability of intervention. They will now

Visa (supra, footnote 57). As regards the decision in *Master Card* (supra, footnote 51), the second infringement decision adopted in this period, remember that proceedings in this case were started well before the introduction of Regulation 1/2003 and followed a long history of notifications.

⁸³ In this sense, see again Neven (2001).

⁸⁴ This can be illustrated as follows. Let us analyse what the defendant's options are once the Commission has signalled that it objects to his agreement, for instance after receiving a complaint. The defendant faces a choice between fully litigating the original agreement and negotiating a less restrictive alternative agreement with the Commission. To decide he will weigh the expected value of the two options. He will choose not to offer commitments and challenge the Commission's decision in appeal if $p\pi - C \geq 0$ that is, if $p\pi \geq C$ (where the term p stands for the chances of prevailing over the Commission, π for the extra commercial profits he will make if he manages to get the more restrictive original version of the agreement cleared, and C for the extra costs of litigation (including fines) that he incurs in case he decides to challenge the Commission's decision). Now, let us look at the effect the procedural reforms. A (perceived) increase in the level of sanctions (that is, C grows larger) will mean that challenging the Commission is an attractive option in fewer cases.

have to work on the basis of a prediction (of the effects), rather than on an evaluation of evidence that is available *ex ante* (the terms of the agreement). In addition, where before firms could rely on the advice of the Commission, they must now independently make this assessment, whilst the risks involved in assessing legality have increased as – upon the finding of an infringement – fines are more likely to be imposed in an enforcement system based on deterrence.

In predicting the likely appraisal of a contract by the Commission, firms may rely on the guidelines, to learn about the framework of analysis, and its decision practice, which gives crucial information about the weight that will be attributed in individual cases to the different types of arguments and evidence that are listed in those guidelines. We have seen that the decision practice has a number of shortcomings. To begin, a certain vagueness surrounds the use of the primary instrument at the disposal of firms to assess the legality of an agreement *ex ante*: the analysis of market structure to infer market power.⁸⁵ The analysis of market structure is particularly suited to study market power from an *ex ante* perspective, because significant elements of the analysis – the position of the defendants and their competitors on the market – will be known at that time. The Commission's record of exemption and commitment decision casts doubt on the importance of market power in the assessment. We have discussed several examples of clearance decisions where interventions are made in unconcentrated markets and where restrictions of intra-brand competition are not discussed in light of inter-brand competition.⁸⁶ And even in infringement decisions,

⁸⁵ See Chapter 4, Section 4.3.1.

⁸⁶ The Commission's Guidelines suggest that market power – the power to profitably restrict output in terms of volume, quality, or innovation – is the foremost indicator for intervention. In fact, in cases such as *UEFA* ([2003] OJ L291/25), *TPS* ([1999] OJ L90/6), *P&O / Stena Line* ([1999] OJ L163/61) the evidence presented by the Commission raises doubts whether market power could be made plausible at all. *UEFA* involved the joint selling of broadcast rights by football clubs participating in the UEFA Champions League. After carefully defining the relevant market (acquisition of TV broadcasting rights to football), the structure of this market and the impact of the agreement thereon are hardly considered. All that the Commission notes, in the context of examining the appreciability of the effect on competition (*de minimis* test), is that UEFA matches make up 20% of the money paid for broadcasting rights in the market. In the legal assessment that follows, the clause prohibiting individual marketing of broadcasting rights by clubs that is the focus of the Commission's attention is not discussed in light of these structural conditions, that is to say, it is not explained why UEFA's market position gives cause for concern about its joint selling arrangement, as, arguably, the Courts require it to do. *TPS* involved a joint venture to provide pay-television in France. The relevant market was, at the time, heavily dominated by one player, Canal+, with over 4 million customers. There were two much smaller competitors in the market, including the joint venture, which had some 400.000 customers. In the Commission's legal assessment – which contained a specific section devoted to the application of Article 81(1) EC to the contractual clauses – it found a provision in the agreement granting the joint venture the right of first refusal to programmes in the portfolios of its parents to be restrictive, without discussing market structure. *P&O / Stena Line* provides a possibly even more telling example. Even

defences based on indications that the adverse effect on the process or structure of competition that is advanced by the Commission does not result in a restriction of output and, thus, consumer harm, are seldom treated in detail.⁸⁷ This has implications for our ability to understand the way in which the Commission evaluates positive and negative effects. Since the restrictions of the process or structure of competition found in the analysis under Art 81(1) EC are conceptually distinct from the positive welfare effects identified in the assessment under Art 81(3) EC, the outcome of the weighing process is often scantily motivated.⁸⁸ Finally, it should be mentioned that only relatively few decisions have been adopted since the process of modernisation started and most of these are motivated in abbreviated style.

Some anecdotic evidence

These arguments suggest that modernisation – as it has been put into practice – has deteriorated firms’ capacity to assess the legality of an intended restrictive agreement, that is, the probability of antitrust intervention. It is interesting, in this regard to consider the submissions by law firms consultancy firms and industry organisations in response to the Commission’s public consultation in view of the evaluation of Regulation 1/2003.⁸⁹ Whilst most of respondents start by noting that they consider the shift from the notification regime to *ex post* enforcement a success, a very considerable portion notes that this shift has been accompanied by a significant loss of legal certainty.⁹⁰ Numerous contributions make a link with the state of development of substantive law.⁹¹ In this regard, consider the following quotes.⁹²

though the Commission found that the joint venture “would be unlikely to be able to raise prices without losing their competitors” it considered that its 30% market share was sufficient to find a restriction in the sense of Art 81(1) EC.

⁸⁷ See the discussion of the cases of *Bass* ([1999] L186/1), *Van den Bergh Foods* (supra, footnote 46), *Master Card* (supra, footnote 51), and *Morgan Stanley / Visa* (supra, footnote 57) in Chapter 4, Section 4.3.2.

⁸⁸ See Chapter 4, Section 4.3.2.

⁸⁹ At the time of writing the Commission has not yet published a summary of the observations made. The comments are published on the Commission’s website. The Commission has also launched a consultation procedure in view of the evaluation of its policy with regard to horizontal cooperation. The observations made in response to this call are largely similar to those reported below, where the substance of the law is concerned.

⁹⁰ In addition to the quotations below, consider the following observations submitted by the *Association Française des Entreprises Privées* (at p. 3: ‘After several years of practical experience, companies believe that this system conceal many uncertainties which are unfavourable to business and, in particular, create considerable legal insecurity. [...] Regulation 1/2003 has taken away the earlier procedural mechanisms which gave companies real legal security. These have not been replaced with any mechanism providing security, particularly for agreements between companies which require major financial investments and entail risktaking which is equally considerable.’); *Lovells* (at p. 1:

‘From our clients’ perspective, there has been a notable loss of legal certainty. Competition analysis is complex and turns on questions of judgment and often of inherently uncertain ex ante analysis. It is not unusual for experts to disagree on the correct analysis. Where planned commercial arrangements required significant investment, even where the competition risks were not judged to be particularly high, it was not unusual for clients to consider, pre-modernisation, that the costs and delay involved in notifying the arrangements to the Commission for formal clearance/exemption were justified given the importance of the arrangements and the significance of the investment required. In such cases, clients continue to look for legal certainty. The withdrawal of formal notification has eliminated the possibility for absolute legal certainty as regards the application of Article 81(3). Moreover, the impact of the loss of legal certainty through notification has been magnified by the Commission’s decision to narrow the scope of less formal consultation solely to novel questions – a procedure which has not in fact been used since Regulation 1/2003 came into force. Clients have found this sea change from the possibility of notification for clearance or exemption to

‘There is currently a large and expanding body of legal instruments and documents which facilitate self-assessment. [...] Despite the existence of these documents, however, we believe that the abolition of the notification system has led to a reduction in legal certainty for business in certain instances.’); the *European Banking Federation* (p. 1: [S]ome of our members believe that a greater legal uncertainty has been created for businesses as a result of the implementation of this regulation [...]. In the current legal framework, business have to assess themselves the legitimacy of their agreements and, regularly, at the end problems raised are not covered by the existing jurisprudence (case-law/statute law), considering the lack of sufficient cases (especially as regards to article 82 e.g.). The conditions laid down in article 81. 3 appear also to be subject to evolving interpretations, it is therefore difficult for a company to assess compliance with the rules just by looking to past decisions.’); the *Gesamtverband der Deutsche Versicherungswirtschaft* (p. 2: ‘It should be stressed, however, that the direct application of Art 81(3) EC involves considerable legal uncertainty for companies even four years after the Regulation has entered into force. Therefore, there is still a risk that desirable conduct is refrained from due to the legal risks involved.’); and the *The Associazione Nazionale delle Imprese di Assicurazione* (p.2: ‘EU antitrust law cannot be considered completely consolidated as for its general principles, and its perception by national Authorities is consequently still uncertain and troublesome in many cases. A higher legal certainty on the one hand and, on the other hand, a right balance between actions to be undertaken and the rights of defence, are still lacking.’).

⁹¹ Another cause for uncertainty that emerges from the observations is the perceived risk of inconsistent application by national competition authorities and courts. As explained in Chapter 2, Section 2.5, uncertainties caused by the decentralisation of enforcement are not considered in this thesis.

⁹² Most of these observations are laid down in reports that span several – and in some cases scores – of pages and which in many cases dedicate a significant portion to the issue of legal certainty (and its consequences). Here, there is room to present only short selections. To understand the full context in which these statements were made and, thus, their precise meaning, readers are advised to consult the full reports on the Commission’s website.

negligible opportunities for fact-specific consultation rather unsettling and it is certainly the case, in our experience, that the business community feels that there has been a loss of legal certainty as a result of modernisation.’

(Extract from the observations submitted by *Ahurst*)

‘[I]n our experience, direct applicability of Article 81 (3) EC and the abolition of the former notification system has increased legal uncertainty for undertakings. As undertakings are forced to self-assess the compatibility of agreements, decisions and practices with competition law we have seen an increase in the need for legal advice on competition matters. There also appears to have been an increase in compliance programs and trainings for employees in competition matters. Some clients expressed their concerns about the costs which these incur. The loss of legal certainty makes it more difficult for undertakings to decide whether their actions are compatible with competition law. This particularly applies to borderline cases. We have noted that in such cases undertakings are often not prepared to take the risks involved. They are in particular afraid of fines. Undertakings hence frequently over-comply and do not make use of the entire legal framework provided by competition law. They prefer to stay on the "safe side" of competition law. This substantially reduces their commercial freedom.’

(Extract from the observations submitted by the *CMS Competition Practice Group*)

‘CC does, however, have some concerns that certain aspects of the self assessment regime tend to deter businesses from entering into joint ventures and other commercial arrangements that may benefit from exception under Article 81(3). CC has been called on to provide legal opinions as to the applicability of Article 81(3) on relatively few occasions. In part, this is because many joint ventures can be structured so as to fall outside the scope of Article 81(1) without a significant loss of efficiencies. However, where this is not the case many clients have, in our experience, preferred to abandon commercial arrangements for which

there are prima facie good arguments for exception under Article 81(3), or to restructure them either so that they fall outside the scope of Article 81(1) - but with a loss of significant efficiencies that would have been passed on to consumers - or so that they constitute a full function joint venture, and can therefore benefit from the legal certainty afforded by a clearance decision under the EC Merger Regulation (or national equivalents). CC considers there to be two main reasons for this tendency, both of which pertain to business certainty. The first reason is the difficulty in arriving at a sufficient level of certainty that the Commission, a national competition authority ("NCA") or a court would adopt the same analytical approach as the parties and their business advisers to the theories of harm against which the economic effects of a particular agreement should be assessed, and to the assessment of those effects. [...]

While the Commission's Guidelines on the application of Article 81(3)¹ provide a useful framework for considering the applicability of Article 81(3), they are necessarily incapable of providing guidance in respect of specific circumstances in any given market, and the appropriate techniques of economic analysis in those circumstances (e.g. the determination of which costs and efficiencies should be taken into account). Moreover, while one of the justifications for the abolition of the notification procedure was that industry and practitioners could refer for guidance to the large number of Article 81(3) exemption decisions that had been published prior to the implementation of Regulation 1/2003, CC considers that many – if not most - of those decisions are of ever-decreasing value as precedents. In particular, while it is now widely recognised that the effects of a particular agreement that risks falling within the scope of Article 81(1) require detailed economic analysis, such analysis is not reflected in many Article 81(3) exemption decisions (older decisions in particular). Where decisions do contain detailed descriptions of the analytical approach taken by the Commission to the assessment of economic effects, it is often not possible to advise clients with a high degree of certainty that the same analytical approach would be followed today, given the (albeit gradual) evolution of economic theory in a number of areas. The second reason is that it is no longer possible to obtain the certainty of exemption

for a fixed period. [...] The result of the factors described above is that there is a (relatively small) number of cases in which the optimal commercial structure for a joint venture or information sharing arrangement is not pursued, with an attendant loss of consumer benefits.’

(Extract from the observations submitted by *Clifford Chance*)

‘[B]oth companies and their legal advisors usually remark that the existing Community case-law and Commission notices provide some guidance, but do not cover all issues which may have a practical relevance for the self-assessment of an agreement. Moreover, in application of article 81 to non hard-core cartels, proceedings by the Commission and by national competition authorities are often concluded with a commitment decision, which does not ascertain whether there has been an infringement or whether after the adoption of commitments the infringement has been brought to an end. The increasing use of commitment decisions, while contributing to a more rapid conclusion of proceedings, does not help to enrich the case-law to which companies may refer to obtain guidance.’

(Extract from the observations submitted by the *Associazione fra le società italiane per azioni – Assonime*)

‘[We] have been involved in cases where these guidelines and the Commission’s precedents have been of little assistance because the Commission has changed its previous approach, thereby undermining confidence in the guidelines. In such cases, the application of Article 81(3) is difficult and causes uncertainty to parties and their legal advisers. To minimise the incidence of such situations, we suggest that it would be useful for the Commission, when departing from analysis in a previous case, to indicate clearly the reasoning that has caused it to do so and to indicate whether it envisages that this change in approach is likely to apply only to cases of this kind or represents a broader change of policy.’

(Extract from the observations submitted by *Freshfields Bruckhaus Derringer*)

‘Regulation 1/2003 therefore abolished the cumbersome notification system for agreements. In the vast majority of cases, this has been a valuable reform [...]. Most cases are self-assessed without undue difficulty. However some agreements arise from highly-complex economic and market circumstances, where self-assessment can resolve the competition law questions only up to a point, and where no novel question of law arise where the Commission might be minded to issue a guidance letter [...]. Thus, in this small but economically significant category of cases, the injunction that “business is accustomed to taking risk and competition law risk is no different” is unhelpful, and may lead to a significantly chilling effect on innovation and economic development.’

(Extract from the observations submitted by *Bird & Bird International Competition Group*)

Raising the level of certainty

It must be acknowledged that, although we have good indications that uncertainty exists, this amounts to no more than indirect evidence of inefficient behaviour.⁹³ Our insights into the way firms make decisions under uncertainty about the location of the legal standard give good grounds to *expect* that the uncertainty generated by the way modernisation was put into practice leads to inefficient results. Firms may be led to sign harmful contracts – because they assess the risk of intervention not to be much higher than if they were to stay in the clear – or they might take socially excessive precautions so as to avoid intervention. We even have indications that such behaviour occurs. The Commission’s infringement decisions tell us that situations will arise where firms are under-deterred. Yet we cannot establish, by reference to these decisions, to what extent uncertainty contributed to this result, although the sheer length and complexity of these decisions suggest that this contribution may have been more than negligible. Similarly, the observations made by law firms, consultancy firms and industry organisations as to the performance of Regulation 1/2003 yield significant indications that uncertainty pushes other firms to opt for safe forms of agreements. Still, since the privately more beneficial alternatives that they were led to discard have not been subjected to Commission’s scrutiny, we do not know whether

⁹³ See also the discussion on methodology in Chapter 2, Section 2.5.

they might have passed the test and, thus, whether welfare was not created. It is submitted, however, that on balance it is more probable that some welfare is destroyed or foregone due to uncertainty. If the law itself is not able to communicate clearly, through *ex post* decisions, what constitutes inefficient behaviour, why should we assume that it nonetheless produces uniform *ex ante* incentives for firms to behave efficiently?

Note that without intervention the level of certainty provided to firms in (Art 81 EC) effects-based analysis cannot be expected to increase. It follows from the analysis made above that what is needed are more detailed insight as to the implications of the new analytical framework in practice and an end to the reliance on more restrictive standards. It is true that the reforms are still recent. In principle, therefore, one could expect the implications of the new system to become increasingly clear over the coming years. In EC antitrust, however, this evolutionary process is hampered by factors of an institutional nature.

In current practice, defendants (in the analysis under Art 81(3) EC) face an encompassing burden that is held against an exacting standard.⁹⁴ The increased difficulties in predicting the outcome of proceedings combined with an increased risk that fines will be imposed if they decide to oppose the Commission will make defendants relatively more prone to accept a settlement than before. As argued before, settlement decisions tend to contribute very little to firms' ability to locate the legal standard in subsequent cases. On the contrary, they may create confusion by appearing to suggest that more inclusive criteria than those applied in infringement decisions continue to be of relevance. Moreover, we saw in infringement decisions that the Commission's comparably low burden of proof under Art 81(1) EC gives it extra room in the assessment under Art 81(3) EC to invoke the indispensability requirement and avoid a thorough discussion on issues of antitrust harm. For these reasons, we cannot expect, as we ordinarily should, that expansion of the body of available decisions will mean that firms are better able to predict how the Commission will assess future cases.

It is submitted that the Commission, which has many enforcement priorities and institutional interests in other fields of competition policy, is not very likely to start, of its own accord, to reduce its reliance on commitment decisions, to devote more

⁹⁴ See Chapter 4, Section 4.3.2.

attention to the motivation of its decisions and to completely discard its less permissive standard. Some institutional change will be needed to ensure that EC antitrust policy is applied in a way that is faithful to the framework set out in the guidelines and that increases the understanding of these guidelines. These arguments tell us, also, that a simple expansion of the possibilities to consult with the Commission will not be an adequate solution to the problem of reduced legal certainty.⁹⁵ A commitment to issue more guidance letters will leave the Commission's bargaining power *vis-à-vis* firms unaffected and will not contribute significantly, therefore, to curtailing its ability to intervene in market behaviour of which it is dubious (at least without further explanation) whether it may result in harm.⁹⁶

This suggests that, to genuinely improve legal certainty, a change in the standard of proof is required. In principle, this can be envisaged in two ways. One option would be to lower defendants' burden of proof, the other would be to increase the Commission's burden of proof. Upon closer inspection it turns out that there is no distinction between the two. Conceptually, there are four phases in effects-based analysis: (1) the examination of the competitive process and structure, (2) interpretation of these findings – and of possible evidence of expanded market-wide output – to determine whether firms in question have exercised the capacity to inflict the type of harm that the antitrust provisions are designed to prevent, (3) an investigation of efficiencies, and (4) an assessment of the magnitude of these opposing effects to see which is stronger. The second of these phases, which in practice falls under the heading of Art 81(3) EC,⁹⁷ is often jumped over in decisions (and, as a consequence, the fourth phase is also surrounded by uncertainties). If we want to relieve the defendant of this part of his burden of proof and, at the same time, want to ensure that decisions will be more informative on this point, the only option is that the Courts hold the Commission responsible for this element of the analysis.

We saw in Chapter 3 the enforcement mechanism is complex and adjusting one part may produce effects elsewhere. It can easily be appreciated that requiring the Commission to make more effort in exposing the harmful effects of agreements will have a price in terms of the level of enforcement, that is, the number of cases the

⁹⁵ This solution is advanced by many of the law firms and organisations that responded to the Commission's call for submissions evaluating the performance of the current enforcement regime.

⁹⁶ It should be noted, also, that an ease in the requirements to obtain a guidance letters might lead to a flood of requests that would, once again, limit the Commission's capacity to deal with real infringements.

⁹⁷ See the findings made as regards the division of the burden of proof in Chapter 4, Section 4.3.2.

Commission can be expected to bring. This, in turn, may lower deterrence; possibly more so than the increase in accuracy can off-set. Part Three of this book examines the costs and benefits of improving legal certainty, the specific adjustments to be made to the legal standard, and the complementary measures that help to mitigate undesirable effects. To start, the next chapter develops our thoughts on the effects on the Commission and potential offenders of increasing the burden of proof under Art 81(1) EC.