DG Competition discussion paper on the application of Article 82 of the Treaty to exclusionary abuses (December 2005)

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I. General comments

The bulk of the comments below identify what I see as weaknesses in the discussion paper. While the main thrust of the discussion paper (a focus on the effects of a given practice) is to be welcomed, the discussion paper suffers from two related defects: (a) a lack of clarity as to the aim of the paper; (b) poor drafting.

(a) aims

The paper is torn between two positions: restating the law as is and identifying novel approaches to certain questions. This makes for some unusual drafting at times so that old cases are ‘restated’ with qualifications. However, there are no signals to the reader as to what is a mere codification of the case law and what are novel principles which the Commission wishes to set out.

The paper is written in the form of Guidelines apparently to facilitate readability (paragraph 7) but it is not clear whether the intention is to publish Guidelines or to indicate what new analytical tools the Commission wishes to use. I do not think the format of this document was satisfactory. A discussion paper should read like an essay which explains an argument. This reads like a statutory text, but it is not written with the attention to detail which is necessary to make it a workable statutory text.

The general criticism that emerges from the literature is that Article 82 is applied in a manner that is too aggressive. However the position taken in the discussion paper suggests that there may be a less aggressive stance towards some abuses, but a more aggressive stance towards others. This may surprise those who would like to see less Article 82 enforcement as a result of the Commission’s review. In my view the new theories of abuse (e.g. predation by reputation) should be deployed by the Commission when the evidence proves that harm is likely.

(b) drafting

There are two general drafting problems:

(1) the poor use of footnotes – sometimes the footnote does not support the point being made; sometimes there are no footnotes at all. The selective use of footnotes (their density is in proportion to the novelty of the point being made) is a symptom of the paper’s lack of purpose: is it an attempt to codify the law? If so one would expect a paper that is footnoted comprehensively to provide authority for each proposition set out. If it is about explaining the policy of DG Competition? then no footnotes to the cases seem necessary (see for example the lack of case references in the US Merger Guidelines); or is it about using this as an opportunity to rethink the case law? In which case the decisions need to be analysed in more detail and not just referred to.

(2) lack of definitions/lack of careful drafting. On a first reading the paper reads well, but it is difficult to use as a legal text because the drafting lacks precision. (For example the summary at paragraph 162 should go at the start and then each of the five points addressed under a separate heading). It is also unusual to refer to ‘companies’ and not ‘undertakings’ or to ‘objective necessity’ as opposed to ‘objective justification’. The former in particular is unhelpful given that the Treaty text speaks of undertakings and that there is ample case law on the meaning of that term.
II. Part 4 - Dominance

(a) from dominance to SMP

The paper probably wishes to alter the definition of dominance from that which has been used in the past. As I read it, dominance is henceforth to mean substantial market power (paragraph 28 seems to justify this interpretation).

However, there are a number of term used here that lack definition: the paper starts with the conventional definition at paragraph 20, then goes on to say that dominant firms have a ‘leading position’ (paragraph 22) and have ‘substantial market power’ (paragraph 23). What do these two phrases mean? Paragraph 24 goes on to define ‘market power’ – is this a definition of ‘substantial market power’? or is this a novel term?

Paragraph 24 makes two points that I think are distinct and should have been treated separately:

1. First it redefines dominance as substantial market power. (My worry here is that the notion of ‘substantial’ is too flimsy to be of practical use; moreover, why is there no reference to the Guidelines on SMP in the electronic communications sector? Surely some clarity as to how the concept of ‘SMP’ in that sector relates to SMP here is needed.)

2. Second it explains that market power is the power to exploit as well as the power to foreclose. I think the idea that market power is about the power to foreclose should be omitted or developed more fully. If the aim is to say dominance is ‘substantial market power’ then it is best to say that dominance is the ability to exploit one’s position, and that the power to exclude is an unnecessary addition.

In sum, while it may be a good idea to alter the concept of dominance so that it is more in line with economic concepts of market power, this needs to be achieved in a more direct manner in the paper.

(b) presumptive market shares?

Paragraph 31 seems to suggest that certain market share thresholds can be utilised. This might be interesting (by analogy with the market share thresholds in the Block Exemptions) but the position taken in this paragraph is puzzling to say the least. First, the case law does not support the position taken; second the conclusion seems to be that dominance can be found at lower levels than the case law seemed to suggest.

Below I have reproduced each sentence and I do not believe the case law supports the position taken.

<table>
<thead>
<tr>
<th>Sentence</th>
<th>Authorities cited</th>
</tr>
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<tbody>
<tr>
<td>Very high market shares held for some time = dominance.</td>
<td><em>Hoffmann La Roche</em></td>
</tr>
<tr>
<td>The case cited supports this</td>
<td><em>Hoffmann La Roche</em> – the proviso in the sentence is not explicit in this case, which refers to ‘exceptional circumstances’</td>
</tr>
<tr>
<td>This is the case when the market share is 50% or more, <em>provided</em> rivals hold a much smaller share.</td>
<td><em>AKZO</em> – says 50% is dominance save ‘exceptional circumstances’</td>
</tr>
<tr>
<td>The case law does <strong>not</strong> support this sentence</td>
<td><em>TACA</em> – restates <em>AKZO</em> <em>verbatim</em></td>
</tr>
</tbody>
</table>

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1 Commission guidelines on market analysis and the assessment of significant market power under the Community regulatory framework for electronic communications networks and services [2002] OJ C165/06
### Dominance

<table>
<thead>
<tr>
<th>Dominance more likely to be found in the 40-50% range than below 40%.</th>
</tr>
</thead>
<tbody>
<tr>
<td>The case law does not support this sentence. UBC exemplifies one finding of dominance below 50% and Gottrup Kilm is one obiter statement that market shares are not determinative of dominance in the 30% range.</td>
</tr>
<tr>
<td>United Brands 109-110 states: “This percentage does not however permit the conclusion that UBC automatically controls the market. It must be determined having regard to the strength and number of competitors.” Gottrup-Kilm merely states that market shares in the 30% range are not on their own evidence of dominance</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Unlikely to be dominant if below 25%</th>
</tr>
</thead>
<tbody>
<tr>
<td>The authority cited does not support this sentence.</td>
</tr>
<tr>
<td>ECMR states that concentrations whose market share is below 25% do not substantially impede effective competition.</td>
</tr>
</tbody>
</table>

In sum, the reading of the cases here is unpersuasive, even if one were to agree with the approach taken in this paragraph. This raises again the question of why there are footnotes to begin with, and is a symptom of the lack of clarity about the purpose of the discussion paper as a whole.

#### (c) Dominance by degrees?

One point that is noted at paragraph 59 is that the degree of dominance is a relevant factor in characterising abuse. This is a valuable insight, however this observation is not to be found in part 4. This is a missed opportunity to relate the concept of dominance with that of abuse. It seems to me that for some abuses the degree of dominance must be very high before there can be an anticompetitive effect.

#### (d) Other comments on dominance

Paragraph 27 qualifies the position taken by the ECJ in United Brands, this is a welcome approach.

Paragraphs 34-42: are these paragraphs an attempt to summarise in a comprehensive manner all the factors that may be taken into account to determine whether there is dominance? It is unclear to me why here no footnotes are provided.

### III. Abuse: general principles

Paragraphs 54-59 are to be welcomed in that they provide a helpful framework for conceptualising abuse. However, paragraph 60 is problematic. This seems to introduce the idea that there is some conduct which is anticompetitive by ‘object’ or ‘per se’ anticompetitive. This is in contrast to the main thrust of paragraphs 54-59. The paper starts by stating that effects have to be shown (by the party seeking to enforce Article 82) but that this heavy evidentiary burden can be omitted when the acts of the dominant firms are ‘clearly not competition on the merits’.

The problem here is about the burden of proof and goes to the heart of cases like Michelin 2 and BA/Virgin. It seems to me that if one were to apply the ideas in paragraphs 54-59 to these two cases, the party seeking to establish an abuse would need to provide much more evidence than was presented in those decisions. However, following paragraph 60 the party seeking to establish an abuse needs to show that the kind of rebate is ‘not competition on the merits’ and to then force the defendant to prove (with ‘convincing evidence’) that the conduct does not have an exclusionary effect. ‘Convincing evidence’, it will be recalled, is the standard set for the Commission by the ECJ in the merger case law. It seems that under paragraph 60 this heavy burden is shifted to the defendants.

The reference to AstraZeneca might suggest that paragraph 60 applies only exceptionally, however, the concept of competition on the merits seems to be part of the general abuse doctrine in Hoffmann La Roche.
IV. Defences

(a) the concept of a defence

I do not think that Article 82 admits defences in the way that they have been set out here. The Article 82 ‘defences’ that have been established by the case law suggest that on certain facts there is no abuse. Thus, there is no shift in the burden of proof: a finding of abuse requires an identification of a number of facts, some of these facts can point to a finding that there is no abuse, and it is possible for the defendant to bring such facts to the attention of the Commission.

Case T-203/01 Michelin 2 does not support the sentence in paragraph 77 which reads: ‘The burden of proof for such an objective justification or efficiency defence will be on the dominant company.’ The earlier passages in the judgment distinguish between unlawful ‘loyalty’ rebates and lawful ‘quantity’ rebates. The fact that the defendant offered evidence to try to prove that the rebates in question were quantity rebates does not mean that there is a reversal of the burden of proof. There was just a conflict between the parties as to whether the rebates were lawful or not.

Recital 5 and Article 2 of Regulation 1/2003 do not support the position on the burden of proof set out at paragraph 77.

- Article 2 first sentence states that the burden of proof for the infringement is on the party alleging the infringement. Article 2 second sentence is limited to the application of Article 81(3) and states that the burden of proof shifts to the defendant. However, the burden of proof does not shift in Article 82 cases according to Article 2.

- Recital 5 may offer more support because it refers to the ‘benefit of a defence’ without being specific, which may suggest that there are more defences than Article 81(3) but this is very thin ground on which to reverse the burden of proof.

Thus, neither the structure of Article 82, nor the case law in general, nor the authorities referred to in the paper support the position taken in the paper.

(b) The objective necessity defence (paragraph 80):

(1) why is this renamed? There seemed nothing wrong with the old label of ‘objective justification’

(2) The first sentence sits awkwardly with the last sentence. In fact given the thrust of the final sentence and the strong words of the ECJ and CFI in Hilti, it seems fairly clear that there is no scope for health and safety to be used as criteria to justify an abuse.

(c) meeting competition defence

I do not think that the final sentence of paragraph 83 is helpful because it seems to pre-judge the fact that there is no real scope for this defence. The sentiment in that sentence may be a correct reflection of the case law, but it offers little assistance.

As noted in paragraph 81 the meeting competition defence only applies to pricing abuses. Paragraph 83 seems to suggest that any form of below cost price is not going to benefit from the defence. We are then told at paragraph 176 that the defence does not apply for single branding, which leaves above cost pricing, which will not be an abuse in any event, unless it was discriminatory and we have yet to see the Commission’s position on price discrimination, although Irish Sugar suggests that the defence may not apply to selective discounts.

The meeting competition defence does not seem to exist in EC competition law. Perhaps a statement to this effect would be more apt.
(d) efficiency defence

I have sympathy with this defence however, as suggested above there is no scope for a ‘defence’.

Moreover, there is a better solution. We are told that the efficiency defence:
- does not apply in predatory pricing cases (paragraph 133);
- applies in rebate cases (paragraphs 172-175); tying cases (paragraphs 205-206); in cases of refusals to continue a contract (paragraph 224)

We are also told that Articles 81 and 82 can be applied simultaneously (paragraph 8).

Then, might it not be preferable, as has been suggested in the literature, to apply Article 81 to rebate and tying cases? That way the efficiency defence on Article 81(3) applies by using Article 81(3) directly. As I suggest immediately below, in the ‘refusal to start supplying an input’ cases the argument is not related to Article 81(3). The only gap to this suggestion is the efficiency defence in paragraph 224. However in paragraph 224 the paper does not require proof of all the Article 81(3)-type conditions. In which case the attempt to use Article 81(3) analysis in tying and rebate cases is unnecessary.

(e) the innovation defence

Paragraphs 235-236 do not fit easily within the analytical framework proposed in the section on defences. They seem to suggest an additional defence, which might be labelled the innovation defence. The reference to Joined Cases T-374/94 etc at footnote 139 is not support for any proposition on refusal to supply. Arguments like these were taken into account in Microsoft.

V. Specific abuses

(a) Predatory pricing

Paragraph 97, final sentence is suspect. The remainder of the paragraph is economically sound, and suggests that a high degree of dominance is required for the application of Article 82 to predatory pricing. It would have been helpful to relate this back to the section on dominance and identify the fact that the degree of dominance required for predation is much greater than that for rebates for example.

However, the problem is that the final sentence of paragraph 97 seems to want to make new law and seems related to the US case on predation over one airline route by an incumbent that is challenged by an airline over one route. This seems to be implied in the reference to ‘multiple markets’.

As I noted in part I(a) above, this final sentence embodies the problem of what this paper is about: the first few passages suggest that predation cases will not be taken unless market power is fairly high, and the last sentence suggests that predation by reputation is a theory that the Commission wishes to explore. Both of these claims suggest minor and not so minor departures from the case law, but are framed in a way that does not make it clear whether there is a change in policy. Both, in my view, are changes in policy.

Paragraph 109: I cannot see (although I accept that the majority of textbook writers agree with the statement in this paragraph) how the AKZO case provides for a presumption that prices below AVC are predatory.

Para 71 of AKZO says:

71 Prices below average variable costs (that is to say, those which vary depending on the quantities produced) by means of which a dominant undertaking seeks to eliminate a competitor must be regarded as abusive. A dominant undertaking has no interest in applying such prices except that of eliminating competitors so as to enable it

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2 See E. Rousseva ‘Modernising by Eradicating: How the Commission’s New Approach to Article 81 EC Dispenses with the Need to apply Article 82 to Vertical Restraints’ (2005) 42 CMLRev 587
subsequently to raise its prices by taking advantage of its monopolistic position, since each sale generates a loss, namely the total amount of the fixed costs (that is to say, those which remain constant regardless of the quantities produced) and, at least, part of the variable costs relating to the unit produced.

The first sentence seems to leave no space for any presumptive rule: prices below AVC are predatory.

**Paragraph 128:** I do not see why the exceptional circumstance in this paragraph does not apply when the dominance is held by a single dominant undertaking.

**(b) Single Branding and rebates**

The idea underlying this section (measuring foreclosure) is welcome. However its execution leaves much to be desired. In particular paragraphs 152-161 are very unclear. The boxes do little to help. (It is not clear to me for example in the box at page 46 whether the commercially viable amount was something that is calculated from the above figures or whether it is a ‘given’).

**(c) Refusal to supply**

**Paragraph 208:** the final sentence is to be welcomed because it refocuses United Brands so that the harm is to competitors of the dominant undertaking. However, the Court has regularly found that harm to distributors is a kind of harm for which Article 82 can apply. Is the discussion paper suggesting that this approach will no longer feature in Commission cases? (The same suggestion appears in the rebate discussion where foreclosure is the sole competitive harm that the section focuses upon, see paragraphs 139-141.)

**Paragraph 222:** this is a welcome refocusing of Commercial Solvents. However it is not clear how many theories of harm there are in this paragraph. I think there are two: (i) the penultimate sentence speaks of termination facilitating tacit collusion; (ii) the last sentence suggests a different theory whereby the reduction of supplies is about leverage.

**VI. Unnecessary paragraphs**

**Part 3: market definition**

This should be omitted. If at all the Commission may wish to redraft the Market Definition Notice to take into account the new ideas that are presented in this section.

**Part 4.3 Collective Dominance and all subsequent references to abuse of collective dominance**

The cases on exploitative abuses of collective dominance have so far been about legal cartels. It seems premature to explore the concept of collective dominance and abuse of collective dominance in the context of this paper which should be about explaining how the Commission wishes to reconsider the current Article 82 approach, rather than about exploring how Article 82 might be extended to novel settings.

**VII. Misleading footnotes**

This is a list of what I think is a misleading use of the case law. It is perhaps arguable that the case cited can support the legal principle set out in the text, but it cannot be assumed by merely using a footnote.

**Paragraph 8:** “Therefore, if the conduct of a dominant company generates efficiencies and provided that all the other conditions of Article 81(3) are satisfied (see below section 5.3.3), such conduct should not be classified as an abuse under Article 82 of the EC Treaty”

The footnote reference to case T-193/02 Piau para 119 does not support this sweeping statement. At most it supports the position that if an Art 81(3) exemption is granted then no abuse should be found (which is the point made in the earlier sentence). However the general point made in the passage above suggests that unilateral conduct (ie without an agreement) should not be an abuse if it fulfils the criteria of Article 81(3)
which is too sweeping a remark and which is not supported by the case cited, nor by the paragraph that is selected.

**Paragraph 31**: see part II(b) above

**Paragraph 77**: see part IV(a) above

**Paragraph 109**: see part V(a) above

**VIII. Minor drafting errors**

I have underlined words that need to be added and struck through words that should be deleted.

**Paragraph 34**: The first sentence should read:
‘If the barriers to expansion faced by rivals and the barriers to entry faced by….’

**Paragraph 143**: The first sentence should read:
‘The dominant position of the supplier will make that on average the buyers, even without loyalty enhancing measures, will buy a large part or even most of their purchases from the dominant supplier.’

**Paragraph 217**: The first sentence contains an inaccurate adjective:
‘efficient’ should be replaced by ‘profitable’

The choice of the word ‘efficient’ is misleading because it suggests that the termination of supply is *prima facie* efficient. This is not necessarily so.

**IX. Conclusions**

There are some very good ideas in this document. However it is unfortunate that this was not drafted like a discussion paper but as a series of Guidelines. It would be undesirable to codify a version of this paper as Guidelines, even if it were drafted more carefully. This is because change to the Article 82 doctrine of abuse and to the concept of dominance can only come about incrementally as the case law develops. The Commission cannot ‘legislate away’ the case law of the Court with a soft law instrument. A discussion paper written like an essay, identifying and explaining the Commission’s various changes in policy, would have provided greater certainty. It would also have allowed for greater clarity in the way the points are explained, for example the way the Commission understands foreclosure in rebate cases and the role of the ‘as efficient competitor’ test. In some areas the incremental approach has already borne fruit: the *Oscar Bronner* judgment has done much to alter some of the earlier precedents (e.g. *United Brands* and *Commercial Solvents*). In the long run, slow, judicially approved, incremental modifications are more likely to offer legal security than immediate, radical reformulations contained in a document that has no clear legal status.