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SHOULD THE EC ABANDON ARTICLE 81 (3) EC

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Summary:

In EC competition law the introduction of an *economic approach* can be observed in the Community case-law and decisions and notices published by the EC Commission. This has consequently affected both on the substantive and procedural content of EC competition law. The purpose of this dissertation is to examine how this development has influenced the content of article 81 (1) and whether the role of article 81 (3) has become surplus to requirements. This analysis is divided in three chapters. First, it looks at the economic debate behind EC competition law and the changing policy aims. Secondly, it discusses whether the EC courts have adopted the American rule of reason doctrine and what consequences this has for the function of article 81 (3). Lastly it considers whether article 81 should be modified. The analysis is based on the examination of the CFI's and the ECJ's published decisions, EC regulations and notices and relevant academic literature.

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Thanks to my family for always standing by and encouraging me.

Introduction:

Last year the EU celebrated its 50th anniversary. During these years competition law has developed into a complex and well established brand of law. However, there continues to be problems and disagreements about the correct and preferable application of competition related issues. One debate that has been on the agenda for several decades, is the correct interpretation of article 81 (1) and the role of article 81 (3).

Article 81 (1) prohibits “agreements, decisions by associations of undertakings and concerted practices”¹, which may affect trade between member states and which have as their “object or effect” the prevention, restriction or distortion of competition. Article 81 (3), on the other hand, exempts agreements from prohibitions if four cumulative conditions are fulfilled; two positives and two negatives. First, the agreement must “contribute to improving the production of goods or to promoting technical and or economic process”. Secondly, consumers must receive a “fair share” of the resulting benefits. Thirdly, the restriction must be “indispensable” to achieving these objectives. Lastly, the agreement must not lead to a substantial elimination of the competition in question.

The debate about the correct interpretation of article 81 (1) and the role of article 81 (3) can be viewed as a consequence of the different competition standards, concepts and philosophies in EC and American competition law. This dissertation will therefore first examine the economic debate behind EC and American competition law, the different shifts in policies and how American antitrust law has influenced the modern face of EC competition law.

The EC’s shift towards a more economic approach has lead many academics to argue that the EC should adopt the American “rule of reason” doctrine. I will, in chapter 2 of my dissertation, discuss whether the CFI² and the ECJ³ have adopted this testing standard and what the role of 81 (3) is under the current enforcement system.

After establishing whether there exists a rule of reason doctrine in the CFI’s and the ECJ’s application of article 81 (1), I will ask in chapter 3 how competition law should be shaped and formed, and whether article 81 should be modified from a more normative perspective.

In the end I will summarize my findings and propose some conclusion on the issue whether article 81 (3) should be abandoned.

¹ From now “agreements”

² Court of First Instance

³ European Court of Justice

Chapter 1: Changing policies and goal of EC competition law:

1.1: The ordoliberal concept of economic freedom and formalistic rules:

The Freiburg School and the ordoliberal concept of economic freedom⁴ is generally recognized as the leading theory behind EC competition law. The ordoliberal view of competition law is based on the idea of protecting rivals' opportunities to access and compete on the market place with equal legal treatment, voluntary exchange and freedom of contract.⁵ From the ordoliberal perspective market participants should not face overwhelming constraints from either private or political power.⁶

The ordoliberal vision of competition law is based on legal rules and government intervention. This legal framework is meant to control private economic power, and thereby enhance the competitive process. Ordoliberals believe this is best achieved if competition law prohibits conduct that restrains the autonomous behaviour of the market participants.⁷ Instead of focusing on specific intervention the ordoliberals are proponents of general standards which, in their view, create legal certainty and increased predictability.⁸

Ordoliberalism's influence over EC competition law can first be seen in the drafting of the provisions in the Treaty. The policy aims of EC law are according to article 2 EC, among others, the establishment of a common market and a sustainable development of economic activities. To achieve these goals, the Community shall ensure "that competition in the common market is not distorted"⁹. Willimsky defines competition as a "struggle for superiority in the market place".¹⁰ Competition is therefore synonymous with business rivalry and the policy goal of protecting the "competitive process" can therefore be read directly out of the principles of EC law.

Article 81 (1) prohibits agreements that restrict competition. This provision can be understood as prohibiting any restraints on autonomous economic behaviour on the market place. A similar philosophy of competition law can also be read in article 81 (3). This provision allows for the competition authorities and courts to exempt agreements from prohibition under article 81 (1) because of increased efficiency. Two of the cumulative conditions are that the resulting efficiencies

⁴ The theory was developed by Walter Eucken, Franz Böhm, Wilhelm Röpke, Alexander Rüstow and Ludvik Ehrhard in the period 1930 to 1950

⁵ Alberto Pera: Changing views of competition, economic analysis and EC antitrust law, *European Competition Journal*, June 2008, Page 145.

⁶ Monti: Article 81 EC and Public Policy, *Common Market Law Review* 39: 1057-1099-2002, page 1059

⁷ Alberto Pera, *supra* note 5, 145.

⁸ Arndt Christiansen & Wolfgang Kerber: Competition policy with optimally differentiated rules instead of "per se rules vs. rule of reason", *Journal of Competition law and economics* 2(2), 2006, 215-244, 219

⁹ EC primary legislation, article 3 (g)

¹⁰ Willimsky, S: The concept of competition, *ECLR* 1, 1997, p. 54

are sufficiently passed on to consumers, and that competition on the market place is not eliminated. Monti is of the opinion that this concept of “distributive justice” is a direct reflection of the ordoliberal concern with the accumulation of economic power.¹¹ The condition that competition must not be eliminated reflects the view that economic freedom outweighs any efficiency gain.

The ordoliberal vision of competition law can also be detected in the decisions published by the Commission and the European courts in the years after the enforcement of the Rome Treaty.¹² The Commission interpreted article 81 (1) narrowly and in a formalistic matter and the adoption of the Council regulation no. 17/62 only strengthened the approach.¹³ Under that regulation firms had to notify the Commission about new agreements or draft the agreements in accordance with the block exemptions for them to be eligible for exemption under article 81 (3).¹⁴ Vertical restraints¹⁵ were also presumed anti-competitive under this regulation.¹⁶ Considering the efficiency enhancing effect that these sorts of agreements often result in¹⁷, this strict enforcement system reflects the Commission’s preference for an analysis based on economic freedom and autonomous behaviour.

In *Consten and Grundig v Commission*¹⁸, Consten, a French distributor entered into an agreement with a major electrical and electronic manufacturer; Grundig. The agreement hindered parallel trade. That combined with the fact that Consten got exclusive rights for the trademark GINT in France gave them absolute territorial protection. The ECJ found that the agreement was in conflict with article 81. The Court stated that the agreement would increase inter-brand competition¹⁹, but that this did not outweigh the restraints on intra-brand competition²⁰.

The case has later been criticized for not considering the economics behind intra-brand competition and vertical restraints, for being too formalistic and for focusing on the establishment of the common market as an end in itself.²¹ Opponents of the case argue that territorial protection was necessary for Consten to accept the risk marketing a new product would entail and that the vertical restraint

¹¹ Monti, supra note 6, page 1061

¹² Rome Treaty came into force in 1957.

¹³ Alberto Pera, supra note 5, page 148

¹⁴ Council Regulation 17/62: Implementing Article 85 and 86 of the Treaty, article 4 (1)

¹⁵ Vertical agreements are defined in Article 2 (1) of Commission Regulation no 2790/1999 as “agreements or concerted practices entered into between two or more undertakings each of which operates, for the purposes of the agreement, at a different level of the production or distribution chain, and relating to the conditions under which the parties may purchase, sell and resell certain goods or services.”

¹⁶ Alberto Pera, supra note 5, page 148

¹⁷ See, “Commission notice on guidelines on vertical restraints”, (2000/C 291/01)

¹⁸ *Etablissements Consten SA and Grundig GmbH v Commission* (Case 56 & 58/64) 1966, ECR 299

¹⁹ Competition between different brands

²⁰ Competition within the same brand.

²¹ Renato Nazzini: Article 81 between time present and time past: a normative critique of “restriction of competition” in EU law, *Common Market Law Review*, 43: 2006, 508

was necessary to remove the free rider effect.²² A possible side-effect of prohibiting these sorts of agreements is that firms prefer vertical integration which presumably eliminates all intra-brand competition. When a manufacturer integrates the retail-market it is likely that he will terminate his supply-contracts to enable him to reduce output and charge monopoly prices.

The reason why ordoliberalism influenced EC competition law to the extent that it did in the years after the enforcement of the Rome Treaty is a result of several factors. First, it was the competition policy of Germany, the strongest European economy, and the only European country that had a modern competition regime.²³ Secondly, the European economy had been dominated by high levels of state control, legal cartels and protectionism.²⁴ For instance, in the late 19th and the early 20th century German legislation encouraged the creation of cartels; a policy that was later adopted by the Nazis. When the Rome Treaty came into force market integration and the creation of competitive markets therefore became a goal in itself.

Thirdly, the Second World War showed what political influence the German monopolists in the coal and steel industry could achieve, thereby proving the link between private economic power and political power. The competition provisions first enforced in the ECSC Treaty and later in the Rome Treaty can be viewed as the respond to a concern that cartels might challenge the Community's sovereignty.²⁵

The inevitable paradox in protecting the competitive process is that one of the competitors necessarily has to win. Like Whish points out, if one firm is "the most innovative, the most responsive to consumer's wishes and produces goods or services in the most efficient way possible, this firm may succeed in seeing off its rivals".²⁶ When a company then eliminates competitors by way of their superior productivity and efficiency it seems illogical and against the core of competition law to punish them.

1.2: Changing the competition law policy: heading towards economic analysis and consumer welfare:

Today there is a broad consensus that competition is only instrumental for enhancing economic efficiency and consumer welfare.²⁷ The "economic approach" of modern EC competition law focuses on the likely harm practices have on consumers and is centred on an effect-based analysis model.

²² Monti, *supra* note 6 1065

²³ Alberto Pera, *supra* note 5, page 145

²⁴ G. Monti: EC competition law, 2007, Cambridge University Press, p.1

²⁵ Raymond: The Schuman Plan", *American Journal of International Law*, 47, 1953, p. 97

²⁶ R. Whish: Competition law, 5th ed., 2005, Oxford University press, p 17

²⁷ Alberto Pera, *supra* note 5, page. 127

This implies that the EC competition authorities are focusing increasingly on empirical evidence and economic factors in their legal assessment of competition issues. This shift towards an economic approach was first seen in the United States and was the result of a wide intellectual debate about the appropriate relationship between economic analysis and legal rules.

America's anti-trust policy was for several years based on the Harvard School's concept of structuralism, reflected through a wide range of per-se prohibitions. Vertical restraints were, among other practices, considered anti-competitive and thereby per se illegal because they limited companies' autonomous behaviour on the marketplace.²⁸ This period of American anti-trust law is recognized as a period of intense enforcement and characterized by the focus on market structure rather than actual market effects. The approach was, however, widely criticised because it prohibited practices that did not harm competition.²⁹

In the 1970s American anti-trust policy underwent a radical change. Inspired by the Chicago School³⁰ and Richard Posner American anti-trust authorities and the American courts focused increasingly on market effects, economic efficiency and consumer welfare. In accordance with their theory practices should be examined on the basis of their actual effect on competition, namely by employing the rule of reason.

Richard Posner went even further, arguing that certain practices which generally have pro-competitive effects should be considered per se legal.³¹ I will discuss the relationship between a specific and rule-based enforcement system in chapter 3.

Bork argues in "The Antitrust Paradox: A policy at war with itself" that antitrust law should focus on the effect that business behaviour has on consumers and the wealth of the nation. He furthermore argues that consumer welfare is greatest when society's economic resources are allocated in a way that permits consumers to satisfy their wants within the framework of modern technology. Antitrust law's only function is therefore to increase the collective wealth by overseeing that products and services are sold under conditions that are most beneficial to consumers.³² This will be the case where allocative efficiency is improved to the extent that the net effect - considering the possible

²⁸ *Dr Miles Medical Co v John D Park & Sons Co*, 220 US 373 (1911) – prohibited vertical price restraints, *US v Arnold Schwinn and Co*, 388 US 365 (1967) - prohibited exclusive distribution contracts.

²⁹ Alberto Pera, *supra* note 5, page 137

³⁰ Established by Aaron Director in the 1950 – developed by his students Bowman, Bork, McGee and Telson: Rodgier, B.j: The oligopoly problem and the concept of collective dominance; EC development in the light of US trends in antitrust law and policy, *Columbia Journal of European law*, Vol. 2 no. 1 1995/1996 page 29-30

³¹ Richard Posner, The next step in the antitrust treatment of restricted distribution: per se legality, *University of Chicago Law Review*, 6, 1981.

³² R.H. Bork: The antitrust paradox: A policy at war with itself: 1978, pp. 90-91.

impairment of productive efficiency - will not be detrimental for the consumer. Productive efficiency is the definition for the market condition where the producer produces goods at the lowest possible cost, thereby ensuring that society's resources are not unnecessarily exerted in the production process.³³ Allocative efficiency is greatest where products are allocated between consumers according to their willingness to pay and where the price does not exceed the marginal costs.³⁴

Posner who has a similar perspective on antitrust law argues that competition should only be instrumental for achieving economic efficiency and consumer welfare. In "Economic Analysis of Law" he says that law, in general, should be drafted and interpreted solely on the basis of efficiency considerations; adopting the Kaldor – Hicks criterion.³⁵ The Kaldor-Hicks concept of efficiency is based on two truths; business people are rational and every market participant subjectively values products and services. Wealth will be maximized if products and services are sold at a price that falls between the intervals; buyers' valuation of the goods and services versus sellers' valuations of the goods and services, provided that the overall harm for third parties does not exceed the gain from the transaction.

If buyer A values his product at £50 and seller B values the same product at £100, wealth will be maximized if the product is sold somewhere in the price-range of £50-£100, presuming that the loss for third party C does not exceed the gain of B and A. The reason why this transaction maximizes wealth is because B and A could in theory compensate C for his loss. The fact that no compensation actually has found place is irrelevant, since it is theoretically possible that everybody could be better off without making anybody worse off.

The Chicago School challenged many of the assumptions made under the structuralism paradigm. First, they refuted that there was a connection between industry concentrations and anti-competitive effects. Secondly, high profits by companies could be explained by their superior efficiency rather than their position on the market. Lastly, economies of scale and scope outweighed the negative effects of high levels of concentrations on the marketplace.³⁶

The Chicago School also argued that a market place has self-regulatory powers. In their opinion the market place will eliminate inefficient companies because, even in the case of dominance, established firms or new entrants will offer superior productivity, lower prices and better services. Government intervention should, in their view, therefore be limited to preventing the creation of cartels and setting/monitoring certain hardcore restrictions. Some Chicagoans actually argue that

³³ Which, supra note 26, p. 3

³⁴ Marginal cost is the costs incurred of producing an additional unit.

³⁵ Richard Posner: Economic Analysis of Law, 7ed, 2007, pp 10 - 15

³⁶ Monti, Supra note 24, p.63

government intervention leads to inefficient results and thereby decreases consumer and economic welfare.³⁷

The neo-classical view of competition law, which the Chicago School represent, focuses more on preventing “false negatives” than “false positives”. “False positive” is a term which defines the type of enforcement errors that permit conduct that has detrimental consumer effects. A “false negative” is a type of error that prohibits behaviour that has welfare enhancing effect.³⁸

The Post-Chicago paradigm is a further development of the economic approach and a response to the industrial economy presented by the Chicago School. Compared to the traditional Chicago School this competition theory focuses more on market investigation and adopts a different and broader analytic toolset. This paradigm is based on the concept of “market failure”. Market power, defined as the ability to charge above marginal cost, is the main indicator for market failure. The economic theory does not try to prohibit market power as an end in itself; rather it focuses on the strategic behaviour in achieving or exercising market power. The idea is that a company’s conduct in an imperfect competitive market affects the conduct of other companies, and that strategic use of information advantages can exclude companies from the market place or reduce the attractiveness of competitor’s offers.³⁹ The Post-Chicago paradigm thereby challenges the Chicago School belief that the market has self-regulatory powers.

To what extent has EC competition law been influenced by the Chicago school and the competition policy of focusing on efficiencies and consumer welfare?

The bifurcated structure of article 81 does not conform to the neo-classical perspective of competition law. If the pro-competitive effects of an agreement outweigh the negative effects on competition the agreement does not, the Chicagoans will argue, restrain trade. Neither are there any direct references to the policy objective of consumer welfare or economic efficiency in article 81 (1). Phillip Marsden and Peter Whelan are, however, of the opinion that paragraphs (a) to (d) make an indirect reference to a consumer welfare analysis.⁴⁰

One of the cumulative conditions in article 81 (3) is that consumers must get a “fair share of the resulting benefit” from the agreement for it to be exempted from prohibition under article 81 (1). This is seemingly a reference to a consumer welfare analysis, but as Monti points out, the

³⁷ Monti, *Supra* note 24, p. 65

³⁸ A Bundeskartellamt/competition law forum debate on reform of article 82: A “dialectic” on competition approaches, *European Competition Journal* 211, 2006

³⁹ Monti, *supra* note 24, page 69, page 225

⁴⁰ Phillip Marsden and Peter Whelan: “Consumer detriment” and its application in EC and UK law, *ECLR*, 2006, p 569

requirement that consumers get a fair share of the resulting benefits is not necessarily in correspondence with the neo-classical view.⁴¹ The Chicago School concept of efficiency is, according to Monti, unrelated to “distributional equity”; if society benefits from the agreement, wealth transfer is irrelevant.

In the “Guidelines on the application of Article 81 (3)”⁴² the Commission notes that the objective of competition law is protecting the competitive process “as a mean of enhancing consumer welfare and of ensuring an efficient allocation of resources”⁴³. The guidelines are seemingly influenced by the Chicago School, but still do not want to completely distance themselves from the ordoliberal and traditional view of competition law. Similarly, the Director General of the EC Commission, Phillip Lowe stated that “competition is not an objective in itself, but rather an instrument for achieving consumer welfare and efficiency”.⁴⁴

The question therefore emerges whether these two objectives are in conflict with each other. The Bundeskartellamt answer this question negatively.⁴⁵ They are of the opinion that protecting the competitive process will be favourable to consumers in the long run and that the two policies therefore coincide with each other. In his opinion in *British Airways v Commission* in 2006, the General Advocate also said that the competition rules of the treaty were not designed to protect individual competitors or consumers but to protect “the structure of the market and thus competition as such... because where competition as such is damaged, disadvantages to consumers are also to be feared”.⁴⁶

It is, however, clear that at least in two circumstances the two competition policies will be in direct conflict with each other. First, there will be a conflict with the policy goal of enhancing consumer and economic welfare if the competition authorities or the courts intervene in practices that would have lead to economics of scale or scope. Secondly, consumers will not benefit from protecting small, medium enterprises⁴⁷ that are not capable of producing as effectively and productively as larger ones.

⁴¹ Monti, supra note 6, page 1061

⁴² Communication from the commission, notice, “Guidelines on the application of Article 81 (3)” of the Treaty, 2004/C 101/08

⁴³ Guidelines on the application of Article 81 (3), supra 39, paragraph 13

⁴⁴ Phillip Lowe: “Consumer welfare and efficiency – new guiding principle for competition law”, a speech to the Bundeskartellamt in 2007

⁴⁵ Supra 38, page 214-215

⁴⁶ Opinion of Advocate General Kokott in Case C-95/04P: *British Airways v Commission* of the European Community, 2007 ECR I-2331, paragraph 86.

⁴⁷ From now SMEs.

If competition law, on the other hand, only protects businesses' opportunities to compete on *merits* it can be argued that there is not a conflict between the two objectives. First, if companies compete on merits, agreements that lead to economics of scale or scope will not be prohibited under competition law. Companies that are inefficient will have difficulties surviving on the marketplace since more efficient companies will offer better prices, better quality products and a wider range of products and services.

Alberto Pera discusses whether ordoliberalism is compatible with the increasing role of economic analysis in EC competition law. In his opinion the ordoliberal concept of competition has to be separated from the ordoliberal economic analysis model, which he believes is the result of the structuralism paradigm in the United States, the objective of market integration and the risk of geographical segmentation.⁴⁸ He furthermore argues that cases which date back to *Société Technique Minière*⁴⁹ shows that ordoliberalism is in fact compatible with an economic approach.

In *GlaxoSmithKline v Commission*⁵⁰ the CFI arguably took another step towards the Chicago School's vision of competition law. In this case the Commission had found that GSK's agreement with the Spanish retailers that treated parallel trade unfavourably was by "object" restrictive of competition. The CFI concluded that this was not the case. The Commission was meanwhile entitled, in the CFI's view, to conclude that the agreement had the restriction of competition as its effect.

The presiding Judge said in paragraph 40 that the "strengthening of competition existed only in so far as parallel trade gave final customers the advantages of effective competition in terms of supply or price".⁵¹ This statement can be interpreted as a shift towards focusing solely on consumer welfare. The term "effective competition", however, may lead to doubts about whether this is the right interpretation. In fact it seems that the CFI, like the Commission in the guidelines, does not want to completely distance itself from the established objective of protecting the competitive process.

Another way to understand the statement is to see the "competitive process" and "consumer welfare" as interrelated terms, and that the latter dictates the content of the former. The term competitive process thereby loses its original meaning and become a term that is basically governed by the understanding of consumer welfare.

⁴⁸ Alberto Pera, *supra* 5, page 157

⁴⁹ *Société Technique Minière (LTM) v Maschinenbau Ulm GmbH (MBU)*, case 56-65, 1966, ECR 235 (from now *STM*)

⁵⁰ *GlaxoSmithKline Services Unlimed v Commission of the European Communities* (case T-168/01), 2006, 5 C.M.L.R. 29 (from now *GSK*)

⁵¹ *GSK*, *Supra* note 50, paragraph 29

The fact that the CFI is ambiguous in its statement weakens the weight of the precedent. The truth is that the highlighted text can be interpreted in several directions. Similarly, the phrasing in paragraph 39 contradicts the first statement somewhat and thereby raises further questions about the correct understanding of the Courts' reasoning. Before anything certain can be concluded it seems that either the CFI or the ECJ should take a more clear and precise viewpoint on the subject.

Alberto Pera points out in his article "Changing Views of Competition, Economic Analysis and EC Antitrust Law" that applying the Kaldor-Hicks concept of efficiency uncritically will lead to an examination of how practices will affect total welfare and wealth rather than their effects on consumer welfare.⁵² A practice that is cost-efficient will therefore be considered beneficial as long as the savings are larger than the loss to consumers.

By putting economic efficiency and consumer welfare in the centre of competition law there is a risk that competition law loses its core values. If the terms "competitive process" and "business rivalry" lose their substantive content, competition law get a much wider legal framework. Whether there exists a competitive market place becomes almost irrelevant. And in circumstances where measures other than maintaining a competition process increases consumer welfare more rapidly it can be argued that these factors should be given decisive weight.

The reason why the Commission and the European courts are focusing increasingly on economic efficiency and consumer welfare can be explained by several factors and by observing different developments in EC competition law.

The introduction of Merger regulation 4069/89 had a significant effect on competition law in general. In contrast with other types of competitive behaviour the legality of a merger have to be examined from its expected effect on competition. This examination is based on economic criteria' and considers structural and market effects.⁵³ This in turn influenced the application of article 81 and 82.

The ECJ also adopted a more economic approach in its application of article 81 (1) which I will discuss more closely in chapter 2.

During the 1980's competition legislation was given force or modified in several European countries. Even though the provisions were structured according to article 81 and 82, the national competition authorities did not always adopt the formalistic approach.⁵⁴ This subsequently influenced the European approach. The Commission and the European Courts get input from the Member States of

⁵² Alberto Pera, *supra* note 5, page 142

⁵³ Alberto Pera, *supra* note 5, page 150

⁵⁴ Alberto Pera, *supra* note 5, page 150

the Community through legal proceedings and the appointment of new judges. It is understandable that these new viewpoints and experiences will be reflected in new decisions.

The debate about an economic approach versus a formalistic approach has direct consequences for the substantive content of article 81 and the other competition provisions. The proponents of an economic approach are in many ways arguing for the adoption of the American rule of reason doctrine.⁵⁵ Economists and legal scholars that argue for a formalistic and structural approach are often proponents of per se rules. In the following chapter I will discuss what the current EC approach is.

Chapter 2: The existence of a rule of reason analysis in EC competition law and the role of article 81 (3):

2.1. Existence of the rule of reason:

One of the most debated subjects in the field of EC competition law is whether a rule of reason analysis is used in the ECJs and CFIs application of article 81 (1).⁵⁶ The rule of reason doctrine has its origin from American antitrust law. Already in 1911, the rule of reason was declared the standard analyses for the application of Section 1 of the Sherman Act.⁵⁷ However, because of an increased workload and the complexity of many competition issues the Supreme Court declared many practices per se illegal.⁵⁸

The Chicago School, as mentioned earlier, criticized the structuralism-paradigm in the United States and the result could first be seen in *GTE Sylvania*⁵⁹. Here the Supreme Court held that the rule of reason was the applicable testing standard for deciding whether vertical non-price restraints were in conflict with Section 1 of the Sherman Act.

In *NCAA* the Supreme Court blurred the line between per se rules and the rule of reason by opting for “quick look analyses” and by stating that only in the area of hard-core restraints is there room for per-se prohibitions.⁶⁰

⁵⁵ See chapter 2, page 15 and 16

⁵⁶ Nazzini, supra note 21, Mel Marquis: O2 (Germany and the exotic mysteries of article 81 (1) EC, European law review, 2007, Pietro Manzini: The European rule of reason-crossing the sea of doubt, European Competition law review 2002.

⁵⁷ *Standard Oil of New Jersey v United States* 221 U.S.1, 31.S Ct.502, 55, L.Ed.619 (1911)

⁵⁸ Beverly Robertson: What is a restriction of competition? The implications of the CFIs judgment in O2 Germany and the rule of reason, E.C.L.R, 2007

⁵⁹ *Continental T.V., INC v GTE Sylvania INC*, 433 U.S 36 (1977)

⁶⁰ Christiansen, supra note 8, page 218

In the *Leegin* Case the Supreme Court stated that the same standard was to apply on vertical price restraints, thereby reversing a hundred year old precedent.⁶¹ The presiding Judge formulated the rule of reason as a testing standard that “requires the factfinder to weigh ‘all the circumstances’”, including “specific information about the relevant business and the restraints history, nature and effect.”⁶² The presiding Judge further emphasized the distinction between restraints that are anti-competitive and thereby harmful to consumers and pro-competitive restraints that are beneficial to the consumers. The test thereby involves weighing the welfare-enhancing effects with the welfare-reducing effects, and if this results in a positive balance the practice does not restrain competition.

The phrasing of the presiding Judge makes the analysis conducted under the rule of reason doctrine effectively open-ended; it is necessary to undergo a full-scale market investigation and every justification or argument are in principle relevant.⁶³

The American competition provisions are distinctly different from the European ones. Section 1 of the Sherman Act prohibits “agreements, conspiracies or trusts in restraint of trade “and is the American version of article 81 (1). Unlike EC competition law the American anti-trust legislation does not provide for the possibility of exempting an agreement from prohibition. It is therefore logical that the Supreme Court created an analytic toolset to filter out the agreements that are favourable to consumers.

When viewing article 81 as a whole it seems unlikely that the drafters meant to include a “rule of reason analysis” in article 81 (1); the provision has a bifurcated structure where the restraints on trade have to be considered in the context of article 81 (1) and the efficiency enhancing effects have to be examined in the context of article 81 (3). In contrast with Section 1 of the Sherman Act article 81 (1) has a list of practices that are considered anti-competitive. Retail price maintenance is one of these practices. If the EC competition authorities were to come to the same conclusion as the Supreme Court in the *Leegin* Case, just by applying article 81 (1), they would arguably distort its text.⁶⁴

Robertson is of the opinion that these objections to the rule of reason doctrine are not well founded. From her perspective the adoption of the economic approach leads to a legal situation where the objective of article 81 is identical to that of Section 1 of the Sherman Act; namely to prohibit anti-

⁶¹ Vertical price restraints were deemed per se illegal in “*Dr Miles*” (1911), supra note 28

⁶² *Leegin Creative Leather Products, INC., Petitioner v PSKS, INC., DBA KAY’s Kloset...KAY’s Shoes*, no, 06-480, decided June 28, 2007, Syllabus, paragraph (a)

⁶³ Christiansen, supra note 8, page 217

⁶⁴ Manzini, supra note 56, page 3

competitive behaviour.⁶⁵ She furthermore argues that the practices listed in article 81 (1) are not automatically caught by the provision and that they are at most suggestive.

In accordance to the “Guidelines on the application of Article 81(3)” the weighing of pro and anti-competitive effects is to be “conducted exclusively within the framework laid down by article 81 (3).”⁶⁶ The text of article 81 (1) and the guidelines suggests that it does not amount a rule of reason analysis under EC competition law.

Article 81 (1) prohibit agreements that have as their “object or effect” the restriction of competition. The phrasing “object or effect” has created several interpretive difficulties for the Commission and the European courts.⁶⁷ One problem has been whether these are two cumulative or alternative conditions. In *STM* the ECJ held that the conjunction “or” indicated that the phrasing had to be read disjunctively.⁶⁸

In *Anic Partecipazioni* the ECJ stated that once it was established that the agreement had as its object the restriction of competition there was no need for further market enquires or to show any specific anti-competitive effects.⁶⁹ The underlying logic is that agreements that *by object* restrict competition are those that, from experience and the serious nature of the restriction, have negative effects on the market and competition.⁷⁰ This interpretation of “by object” restrictive of competition makes the restrictions very similar to per se prohibitions in the United States.

In *GSK* the CFI blurred the line between the two alternative conditions by stating that both conditions require the decision maker to examine the agreement in the “legal and economic” context in which it has been deployed.⁷¹ The CFI reversed the Commission’s decision, which deemed the agreement by object restrictive of competition, because the Commission was not entitled to rely merely on the fact that the agreement limited parallel trade. The CFI thereby indirectly said that even though practices have been considered per se illegal in the past they have to be evaluated in the framework of an effect-based analysis model. The weight of the precedent can be questioned. This case revolved around the Spanish pharmaceutical industry, where the Spanish government actively regulates the retail prices. This makes it effectively a non-competitive market. Prohibiting the agreement would neither be favourable to consumers since only the traders/middlemen would benefit from parallel

⁶⁵ Robertson, supra note 58, page 7

⁶⁶ Guidelines on the application of Article 81 (3), supra note 42, paragraph 12.

⁶⁷ Kirsty Middleton, Barry J. Rodger & Angus MacCulloch, “Cases & Materials on UK&EC Competition law”, 1th edition, 2003, page 198

⁶⁸ *STM*, see supra 63, page 198

⁶⁹ *Commission of the European Communities v. Anic Partecipazioni SPA*, Case-49/92 (1999), ECR II, note 12

⁷⁰ Guideline on the application of Article 81 (3), supra note 42, paragraph. 21

⁷¹ *GSK*, supra note 50, p 23 - 27

trade. It therefore has to be concluded that the scope of the Court's reasoning is limited to the current facts.

The conflict between the proponents and the opponents of a rule of reason analysis under article 81 (1) is indirectly a consequence of the earlier enforcement system of article 81 EC. Under the old EC regime the Commission had exclusive competence to exempt agreements under article 81 (3).⁷² National competition authorities thereby had to follow the EC precedents relating to article 81 (1), without being able to exempt pro-competitive agreements. The adoption of the rule of reason, which René Joliet among others recommended, would have allowed national competition authorities to take economic realities into account.⁷³

In 2004 the "modernization" regulation⁷⁴ came into force. One of the major changes was that national competition authorities and the national courts can now apply article 81 (3).⁷⁵ The question therefore arises whether it is necessary to continue the debate about the need for a rule of reason analysis under article 81 (1). The bifurcated structure of article 81 is, however, important for the question about the burden of proof. In accordance to article 2 of Regulation 1/2003 the burden is upon the plaintiff to show that the agreement restricts competition within the meaning of article 81 (1). If an agreement is caught by this provision the burden of proof is reversed and the defendant has to prove that the agreement should be exempted from prohibition.

The rules governing the burden of proof can be seen in a broader perspective and reflects whether the competition system is focusing on reducing "false positives" or "false negatives". The focus on reducing "false positives" can be viewed as a direct consequence of the ordoliberal economic analysis model where protecting the competitive process is significantly more important than market effects and economic efficiency.⁷⁶ The Commission's task of having to show anti-competitive behaviour ensures that the market structure is sufficiently maintained. The fact that the defendant has the burden to prove efficiency enhancing effects reflects the viewpoint that actual market effects are secondary to the preservation of the competitive process.

The debate on whether there exists a rule of reason analysis under article 81 (1) can be dated back to two cases which the ECJ decided in 1966; namely *STM* and *Consten & Grundig v Commission*.

⁷² Council Regulation 17/62, supra note 14, article 9 (1)

⁷³ Manzini, supra note 56, page 3

⁷⁴ Council Regulation (EC) 1/2003: On the implementation of the rules on competition laid down in Article 81 and 82 of the Treaty

⁷⁵ Supra note 74, paragraphs 5 and 6

⁷⁶ See page 6

In *STM* the case revolved around an exclusive distribution agreement containing a non-compete clause. The ECJ began by expressing the view that the conditions set forth in article 81 (1) depended “less on the legal nature of the agreement than on its effect on `trade between member states` and its effect on competition”.⁷⁷

The first issue was whether the agreement by “object” restricted competition. The ECJ stated that this had to be evaluated by determining “the precise purpose of the agreement in the economic context in which it is to be applied”. The Court went on to say that if the agreement did not have as its object the restriction of competition, the “consequences” of the agreement had to be assessed to enable the decision maker to determine whether the agreement restricted competition “to an appreciable extent”.⁷⁸ The Court pointed out that several economic factors had to be taken into account under this analysis; including the nature of the products covered by the agreement, the market position of the parties, the severity of the exclusive agreement and whether the agreement was necessary to penetrate a new market.

The first statement highlighted shows that the ECJ is focusing on the economic effects of the agreement rather than applying formalistic rules. Nazzini is of the opinion that the Court clearly engaged in a balancing exercise in its interpretation of article 81 (1), where the welfare-reducing effects were weighed against the welfare-enhancing effects.⁷⁹ The use of the term “consequences of the agreement” can be interpreted as the establishment of a test where the net competitive effect of the agreement has to be evaluated in the context of article 81 (1).

In *Consten & Grundig v Commission* the ECJ distanced themselves from the economic approach applied in *STM*. The ECJ held that the exclusive distribution agreement, which gave Consten absolute territorial protection, was by “object” restrictive of competition. The case took, as I have mentioned earlier, a formalistic approach on the application of article 81 (1) and the Court has been criticized for not considering the economic effects of the agreement.⁸⁰

Nazzini argues that this case is coherent with the economic approach applied in *STM*: The Court’s conclusion was a result of the effects the agreement would have on the partitioning of the market, which legitimated the strict application of article 81 (1).⁸¹ He points out that the approach must not be generalized and should only be applied in limited circumstances. This interpretation of the case seems influenced by a subjective agenda. Nazzini is clearly a proponent of adopting a rule of reason

⁷⁷ *STM*, supra note 49, 248

⁷⁸ *STM*, supra note 49, 249

⁷⁹ Nazzini, Supra note 21, page 506

⁸⁰ See chapter “Changing policies and the goal of EC competition law” page 7

⁸¹ Nazzini, Supra note 21, page 507

analysis under article 81 (1), and thereby interprets the case from the perspective of proving the existence of the analytic standard rather than interpreting the case objectively.

In *Metro*, the ECJ recognized that selective distribution systems, where resellers are chosen on the basis of objective criteria of a qualitative nature, accord with article 81 (1).⁸² The Court acknowledged the importance of price competition, but stated that it did not constitute the only effective form of competition within the meaning of article 81 (1). Indirectly, the Court is saying that it is necessary to balance the anti-competitive effects of the agreement (the decrease in price-competition) with the pro-competitive effects (the increase in non-price competition). The weight of the precedent can be questioned; the ECJ does not clearly distinguish between its discussions relating to article 81 (1) and 81 (3).⁸³ Basically, it seems that the ECJ applies article 81 as a whole, which give little guidance to which analyses that falls under which section of the provision.

In *Nungesser v Commission*⁸⁴ the plaintiff asked the ECJ to annul the Commission's decision that deemed an exclusive distribution license of breeders rights by "its very nature" restrictive of competition.⁸⁵ The Court held that an open exclusive license agreement, that does not affect third parties, is not "incompatible with article 85 (81) (1) of the Treaty".⁸⁶ In coming to this conclusion the Court focused on the need for protecting agricultural innovations and pointed out that granting an exclusive licensing agreement could be capable of increasing the R&D efforts in this area. The ECJ, furthermore, emphasized that prohibiting such license agreements could lead to a situation where the licensee "might be deterred from accepting the risk of cultivating and marketing that product" and that this "would be damaging to the dissemination of a new technology and would prejudice competition in the Community between the new product and similar existing products"⁸⁷.

The ECJ thereby weighed the harmful intra-brand effects with the enhancing inter-brand effects of the agreement. It can be debated whether this case accepts the rule of reason or whether the precedent is limited to the specific case. The problem with prohibiting licensing agreements is that it is in conflict with the exclusive rights of the intellectual property owner. The Court's solution can therefore be understood as an attempt to converge competition law and intellectual property law.

⁸² *Metro SB-Grossmärkte GmbH & Co m KG v Commission*, case 26-76, 1975 ECR 1875, paragraph 20

⁸³ *Metro*, Supra note 82, paragraph 21

⁸⁴ *L.C. Nungesser and Kurt Eisele v Commission*, case 258/78, 1982, ECR 2015, (1983) 1, CMLR 278

⁸⁵ *Nungesser*, supra note 84, paragraph 44

⁸⁶ *Nungesser*, supra note 84, paragraph 58

⁸⁷ *Nungesser*, supra note 84, paragraph 57

Manzini also argues that the Court's reasoning is "synthetic" and that it is therefore difficult to decide whether such a "thesis has actually been withheld by the case law."⁸⁸

The CFI explicitly considered the issue whether anti-competitive effects can be weighed against pro-competitive effects under article 81 (1) in *Métropole*.⁸⁹ The Court first began by pointing out that earlier practices were ambiguous about the issue and that several cases indicated that "the existence of a rule of reason in Community competition law was doubtful".⁹⁰ Secondly, the CFI found it difficult to interpret article 81 (1) to allow the possibility of a rule of reason analysis, considering the structure and the forming of the provision; article 81 (3) expressly provides for the possibility of exempting agreements that restrict competition. The Court stated that "only in the precise framework of that provision (81 (3)) can pro and anti-competitive aspects of a restriction be weighed".⁹¹ The underlying logic, was according to the Court, that article 81 (3) would lose its effectiveness if a rule of reason examination had to be carried out under article 81 (1).

The CFI went on to clarify the case law that suggested a rule of reason analysis under 81 (1), by stating that "those judgments cannot, however, be interpreted as establishing the existence of a rule of reason in Community competition law. They are, rather, part of a broader trend in case-law according to which it is not necessary to hold, wholly abstractly and without drawing any distinction, that any agreement restricting the freedom of action of one or more of the parties are necessarily caught by the prohibition laid down in article 85 (81) (1) of the treaty".⁹² This ambiguous statement gives little guidance on the correct application of article 81 (1). The fact that the CFI specifies that when assessing the applicability of article 81 (1) "account should be taken of the actual conditions in which it function, in particular the economic context in which the undertakings operate, the product or services covered by the agreement and the actual structure of the market concerned" gives some indications to the content of the test.

Manzini is of the opinion that the Court's statements have to be viewed as the formulation of a testing standard that aims to consider the existence of anti-competitive effects from a broader market perspective.⁹³ Practically it is difficult to perceive how this does not imply balancing pro and anti-competitive effects. When the anti-competitive effects of a practice are determined from a "broader market perspective" it must necessarily entail an evaluation of the net competitive effect the practice will have on the market.

⁸⁸ Manzini Supra note 56, page 4

⁸⁹ *Métropole télévision (M6) v Commission*, Case T-112/99, ECR 2001

⁹⁰ *Métropole*, supra note 89, paragraph 72

⁹¹ *Métropole*, supra note 89, paragraph 74

⁹² *Métropole*, supra note 89, paragraph 76

⁹³ Manzini, supra note 56, page 5

In *O2 (Germany) v Commission*⁹⁴ the German telecommunication companies O2 and T-Mobile operated 2G and 3G mobile telecommunication networks and services in Germany. The two companies agreed to share the infrastructure and the roaming access to their national mobile networks. The Commission found that the national roaming agreement infringed article 81 (1) because it restricted competition on the market for wholesale access to national 3G roaming services. The Commission meanwhile found that the agreement qualified for an exemption under article 81 (3) for a certain time-period.

The CFI first stated that when carrying out the proper examination under 81 (1) it is “necessary to examine the economic and legal context in which the agreement is concluded, its object, its effects, and whether it affects intra-Community trade taking into account in particular the economic context in which the undertakings operate, the products and services covered by the agreement, and the structure of the market concerned and the actual conditions in which it functions”.⁹⁵

Secondly, the CFI made it clear that if the agreement did not have as its object the restriction competition, the effects of the agreement had to be assessed within “the actual context in which competition would occur in its absence.”⁹⁶ The CFI, however, emphasized that this did not imply “carrying out an assessment of the pro and anti-competitive effects of the agreement”⁹⁷. These two statements are seemingly incompatible: When analyzing the conditions of actual and potential competition in the absence of the agreement and evaluating how the agreement will affect these conditions it seems necessary to consider both the pro and anti-competitive effects; the extent of competition on the market place is the combination of both factors.

The CFIs application of article 81 (1) on the facts in *O2 (Germany) v Commission* also indicates that it is necessary to weigh the pro and anti-competitive effects of an agreement under article 81 (1). The CFI criticized the Commission for failing to consider whether, in the absence of the agreement, O2 would have been able to penetrate the 3G mobile communication market. Actually the CFI was of the opinion that O2s presence on the market “could not be taken for granted” and that it was therefore necessary “not only for the purposes of granting an exemption but, prior to that, for the purposes of the economic analysis of the effects of the agreement on the competitive situation determining the applicability of article 81 (1)”⁹⁸ to carry out a substantive counterfactual analysis. Again the CFI

⁹⁴ *O2(Germany) v Commission*, case T-328/03, 2006

⁹⁵ *O2(Germany) v Commission*, supra note 94, paragraph 66

⁹⁶ *O2(Germany) v Commission*, supra note 94, paragraph 68

⁹⁷ *O2(Germany) v Commission*, supra note 94, paragraph 69

⁹⁸ *O2(Germany) v Commission*, supra note 94, paragraph 79

criticized the Commission for concluding on general grounds and not basing its decision on “any specific evidence”⁹⁹ of the present case.

It is difficult to accept that this does not imply balancing the pro and anti-competitive effects of the agreement. The agreement restricted competition, as the Commission correctly concluded, by impeding wholesale roaming access to the national networks. If anti-competitive effects of an agreement can only be weighed against pro-competitive effects in the framework of article 81 (3), the fact that O2 might not have been able to penetrate the market should have been a question under article 81 (3).

The case-law on the existence of a rule of reason analysis is, as this chapter has shown, ambiguous and contradictory. It is, however, difficult to see how the balancing of pro and anti-competitive effects can be avoided under the economic approach adopted by both the ECJ and CFI: It then has to be sufficient that the agreement produces only one potential or actual anti-competitive effect for it to be caught by article 81 (1). An agreement that has both pro and anti-competitive effects will thereby naturally be caught by the provision. This does not correspond to the case law which relates to the application of article 81 (1) and it therefore has to be concluded that the European courts, to some extent, balances the pro and anti-competitive effects of an agreement under article 81 (1).

2.2: Can all factors and circumstances be taken into account under article 81 (1) and what is the role of article 81 (3)?

It is clear that the ECJ and CFI weigh pro and anti-competitive effects of an agreement in their application of article 81 (1). This does not, however, necessarily imply an adoption of the American rule of reason doctrine. In accordance to the *Leegin* Case the rule of reason is a standard which requires the factfinder to consider “all the circumstances”.¹⁰⁰ It can be argued that the ECJ and CFI instead have adopted an approach where some pro-competitive effects are relevant under article 81 (1), while other pro-competitive effects have to be weighed in the context of article 81 (3).

Odudu argues that the distinction in the analysis conducted under article 81 (1) and 81 (3) is that under article 81 (1) the analysis relates to allocative efficiency, while article 81 (3) is concerned with productive and dynamic efficiency.¹⁰¹ He argues that practices that “restrict” competition within the meaning of article 81 (1) are synonymous with practices that affect allocative inefficiency. The productive efficiency assessment under article 81 (3), on the other hand, allows the courts to consider the effects of cost-reducing agreements, such as agreements that results in economics of

⁹⁹ *O2(Germany) v Commission*, supra note 94, paragraph 86

¹⁰⁰ See above, page 15-16

¹⁰¹ O. Odudu: A New economic approach to article 81 (1)? E.L.Rev.27 2002, page 104

scale and scope, and technology transfer agreement that enhances the incentive to innovate and leads to new and improved products and services on the market place.

Nazzini adopts a similar approach. He believes that consumer-enhancing effects should be weighed against consumer-detrimental effects under article 81 (1), and if the net effect of the agreement is likely to increase consumer welfare the agreement should not be caught by article 81 (1).¹⁰² In his opinion article 81 (3) should be concerned with the other form of pro-competitive effects; namely “agreement-specific productive efficiency”, and only if the agreement reduces consumer welfare should these types of efficiencies be weighed against the restrictions of competition.

Thirdly, the “Guidelines on the application of Article 81 (3)” can be interpreted as the adoption of a balancing exercise where only certain types of factors are weighed under article 81 (1). In paragraph 24, the guidelines say that for an agreement to restrict competition by effect “the actual or potential” affect on competition must extend to such a degree that “negative effects on prices, output, innovation or the variety or quality of goods and services” on the relevant market are the probable result. This does necessarily entail balancing the pro and anti competitive effects of the agreement. If the net effect of the agreement leads to lower prices and better products they are, if this paragraph of the guidelines is read literally, not caught by article 81 (1). This is in direct conflict with paragraph 12 of the guidelines that states that pro and anti-competitive effects can only be weighed in the framework of article 81 (3). A way to converge these two conflicting statements is to say that an agreement is not anti-competitive unless it affects prices, quality of products etc. in a negative manner and that the pro-competitive effects referred to in paragraph 12 are only a reference to non-competition concerns.

In *Wouters* the Dutch court sought advice from the ECJ on the question of whether the 1993 Regulation, that adopted universally binding rules governing the formation of multi-disciplinary partnerships between lawyers and other professions, had as its ‘object or effect’ the restriction of competition within the meaning of 81 (1). The appellant in the case argued that a professional partnership between members of the Bar and accountants should be deemed legal. The Luxembourg Government claimed in the hearing that the prohibition would actually have pro-competitive effects because it prevented the market from being concentrated by few international firms, and that the prohibition thereby protected the competitive process.¹⁰³

¹⁰² Nazzini, *supra* note 21, page. 504

¹⁰³ *Wouters v. Algeme Raad van de Nederlandse Order van Advocaten*, case C-303/99, 2002, ECR 611, paragraph 85

The ECJ found that permitting multidisciplinary partnerships between companies that provided legal services and companies that provided accounting services would have welfare-enhancing effects. Particularly considering the increasing link between these services, legalizing partnership agreements between law and business would result in a wider range of products and would even possibly lead to the introduction of new products on the market place.¹⁰⁴ Furthermore, a prohibition of this kind of multi-disciplinary partnership would prevent law-firms from benefiting from economics of scale and scope.¹⁰⁵ The Court even acknowledged the dangers of concentrated markets, but found that there were less restrictive ways to guarantee a competitive market for legal services.¹⁰⁶

Having concluded that the prohibition of multi-disciplinary partnerships between members of the Bar and accountants restricted competition the Court went on to say that not every agreement that restricts “the freedom of action” of the parties is caught by article 81 (1). The Court stated that it was necessary to consider the objectives of the 1993 Regulation, which in their view were connected with the need to make rules “relating to the organization, qualification, professional ethics, supervision and liability” in the legal profession in order to provide the best and most reliable service for the ultimate consumer.¹⁰⁷ The Court went on to consider “whether the consequential effects restrictive of competition were inherent to the pursuit of those objectives”.¹⁰⁸ The Court thereby asked whether the anti-competitive effects of the prohibition were proportional to the objective of ensuring a proper practice in the legal profession. The Court answered this positively and concluded that the 1993 regulation did not infringe article 81 (1).

The underlying logic and the consequences of the ECJs reasoning are much debated subjects in academic circles. The debate is divided between those who argue that the ECJ is only weighing up economic factors and those who argue that the ECJ is carrying out a balancing exercise where anti-competitive effects are weighed against non-competitive concerns.¹⁰⁹

Monti is of the opinion that this case is the convergence of the principles governing competition law and free movement law, and that his case adopts the *Cassis de Dijon* doctrine. In accordance with this doctrine domestic rules that impede or act as an obstacle to free movement are not prohibited under article 28 if they are necessary to achieve a mandatory requirement of commercial fairness or are necessary to protect consumers.¹¹⁰ Monti describes the approach as the “European rule of

¹⁰⁴ *Wouters*, supra note 103, paragraph 87

¹⁰⁵ *Wouters*, supra note 103, paragraph 92

¹⁰⁶ *Wouters*, supra note 103, paragraph 93

¹⁰⁷ *Wouters*, supra note 103, paragraph 97

¹⁰⁸ *Wouters*, supra note 103, paragraph 97

¹⁰⁹ *Nazzini*, supra note 21, page 522

¹¹⁰ *Monti*, supra note 6, page 1087

reason” which implies weighing the restraints on competition with other legitimate policy aims. He defends the decision by stating that the case has links to both competition law and free movement law and that it was arbitrary which jurisdiction the case fell under. Depending on whether the Bar Council Regulation was governed by a Member State or by a private body empowered by the state the public policy aims would be treated differently if it were not for the adoption of the *Cassis de Dijon* doctrine.

Nazzini criticizes Monti for not appreciating the balancing of anti-competitive effect with both pro-competitive effects and public policy objectives which he believes the ECJ is carrying out.¹¹¹ He, furthermore, argues that the *Cassis de Dijon* doctrine changed its nature once the analytical test was transported to competition law. As opposed to free movement law which is concerned with State measures, competition law is based on economic considerations. Terms like “consumer protection” and “commercial fairness” therefore have a different meaning depending on whether one faces a competition issue or a free movement issue. Nazzini is therefore of the opinion that Monti’s understanding of *Wouters* differs from the correct interpretation of the case.

R. Whish interprets this case as the introduction of a “regulatory ancillary”: A practice that is restrictive of competition does not infringe article 81 (1) because it is ancillary to the achievement of securing other legitimate objectives.¹¹² He, furthermore, argues that the precedent does not limit itself to the specific facts, but that the Court’s reasoning has a general tone, and that the “regulatory ancillary” can be applied to any regulatory rule that protects consumers. The Commission’s dismissal of ENIC’s claim that UEFAs rule, which prohibited ownership in more than one football club, restricted competition can be viewed as the application of the “regulatory ancillary” test. The rule was necessary to ensure the integrity of the game and to ensure fair and genuine results.¹¹³

R. Whish is of the opinion that the “regulatory ancillary” test has limited relevance after the enforcement of the Modernization regulation.¹¹⁴ This regulation removed the procedural complications which national competition authorities faced under Regulation 17/62; they can now exempt agreements under article 81 (3). Secondly, the burden of proof for the ancillary test is the same as under article 81 (3). It is the person defending the practice/regulation that has to prove that it is ancillary to the public policy objective.

A third interpretation of the case is that the ECJ adopts the American rule of reason doctrine, and that the ECJ balances the anti-competitive effects of the agreement with *both* pro-competitive

¹¹¹ Nazzini, *supra* note 21, page 523

¹¹² R. Whish, *supra* note 26, page 121-123

¹¹³ Commission Press Release IP/02/942, 27 June 2002

¹¹⁴ R. Whish, *supra* note 26, page 123

effects and non-competition concerns in a bidimensional test.¹¹⁵ Nazzini interprets the statement; “in order to ensure that the ultimate consumer of legal services and the sound administration of justice are provided with the necessary guarantee in relation to integrity and experience” as the pursuit of two different objectives; namely increasing the quality of the service and pursuing the public policy objective of protecting the integrity in the legal profession. This proves, in his opinion, that the Court is focusing on both economic and public concerns in the second step of the bidimensional test and that the result is a weighing of both. In fact he argues that only public policy objectives that result in identifiable welfare enhancing effects can be weighed under article 81 (1)¹¹⁶.

This scope of interpretation alternatives weakens the weight of the precedent of the *Wouters* case. It is difficult to grasp how the Court’s application of the second step of the bidimensional test under article 81 (1) involves a balancing exercise where anti-competitive effects are weighed against both pro-competitive effects and non-competition concerns. In the first part of the case the ECJ balances the pro and anti-competitive effects of the agreement by weighing the possible introduction of new and improved products on the market place with the likely effect of a more concentrated market. In the second part of the judgment the ECJ balances this net competitive effect of the agreement with non-competition concerns. Nazzini’s interpretation of the case is illogical and would imply that the Court weighs the same factors twice in its application of article 81 (1).

Whish’s interpretation of the case is more in line with the structure of the ECJ’s reasoning. His argument also puts the case in a broader perspective by generalizing the Court’s arguments and is therefore academically very persuasive. The suggested interpretation forwarded by Monti is also very well-founded and gives the case a broader contextual meaning. In the authors view the case is merely a result of the facts of the case and the ECJ’s application of article 81 (1) cannot be generalized. The ECJ’s principle task is to resolve disputes on a case-by-case basis. The bi-product of this principle task is the significance the ECJ’s reasoning has for future cases. The *Wouters* case seems more focused on coming to a fair result than creating a strong precedent. The outcome depended solely on the structure and organization of the government – they delegated their competence to a private party – and that was the only reason why competition law was applicable. Under those circumstances it was understandable that the ECJ transported arguments from free movement cases.

The *Wouters* case was delivered straight after the collapse of Enron in the United States, which was partly explained by ineffective regulations for accounting firms.¹¹⁷ This strengthens the presumption that the precedent is limited to the specific case. The Commission’s decision in the afore-mentioned

¹¹⁵ Nazzini, supra note 21, page 525

¹¹⁶ Nazzini, supra note 21, page 527

¹¹⁷ Whish, supra note 26, p 121

ENIC dismissal was based on different facts than in the *Wouters* case. In that case the regulatory rules were adopted voluntarily by UEFA and were not a result of government delegation or legislation. The close relationship between competition law and free movement was therefore not a decisive factor in that case. A dismissal, will in addition, have less weight than other types of decisions.

The cases discussed above relating to the correct interpretation of article 81 (1) are also confined to purely competition related issues. In *Metro*, the decrease in price competition was weighed against the increase in non-price competition. Similarly, in *Nungesser* the deciding factor was that the agreement resulted in an increase in inter-brand competition, and that this outweighed the restraints on intra-brand competition. In *O2 (Germany) v Commission* the deciding factor was that in the absence of the agreement O2's presence on the market was not guaranteed and that this outweighed any impediments on wholesale roaming access to the national networks.

The question whether the agreement should be exempted because of non-competition concerns has generally been considered explicitly in the context of article 81 (3). In *Metro* the ECJ considered employment issues relevant under this provision¹¹⁸ and in *CECED* the Commission concluded that the decreases in pollution constituted an economic gain and efficiency within the meaning of article 81 (3).¹¹⁹

The analytic test conducted by the ECJ in *Wouters* seems therefore limited to the specific case and cannot be read as the adoption of the American rule of reason. The question therefore emerges what kind of factors that are relevant under the weighing of pro and anti-competitive effects under article 81 (1). Odudu's distinction between allocative and productive efficiency seems overly complicated and it is difficult to detect such a distinction in the examined case law. In *Nungesser* the ECJ clearly considered the effects the agreement would have on the incentives to innovate when deciding whether article 81 (1) was applicable. Under Odudu's model this evaluation should have been carried out under article 81 (3).

The Nazzini approach, where a *consumer welfare* balancing exercise is conducted under article 81 (1) and where other pro-competitive effects are considered under article 81 (3), has some supporting arguments. This type of distinction might be necessary for implementing the objective of consumer welfare and economic efficiency in EC competition law. Article 81 (3) has a reference to consumer welfare, but only to the extent that it does not lead to the elimination of competition. It can therefore be argued that the broad wording of article 81 (1) makes the provision the only acceptable testing standard for contemplating the effect an agreement will have on the end-consumer. Nazzini,

¹¹⁸ *Metro*, supra note 82, paragraph 43

¹¹⁹ *CeCed*, O.J. 2000, L 187/47

however, fails to explain specifically what types of factors fall under article 81 (3). The consumer-welfare analysis applied under article 81 (1) would also give the competition authorities and the courts a very broad scope of analytic freedom and it is questionable whether this approach can justifiably be maintained against the bifurcated structure of article 81.

It can also be questioned whether it is beneficial for the business society to adopt an analytic model that occurs with Odudu's and Nazzini's suggestions. In their attempt to structure the application of article 81 it can be argued that their approaches have actually the opposite result of the desired effect. Neither of the scholars separate, to an acceptable degree, which factors fall under which phase of article 81. Such a model would create a lot of legal uncertainty, and it would be difficult for the business society to predict their legal position and future outcomes.

Balancing competition issues under article 81 (1) and weighing this net competitive effect with non-competition concerns under article 81 (3), which the "Guidelines on the application of Article 81 (3)" indirectly suggests, is the analysis standard that is most coherent with the case-law examined above.¹²⁰ However, in the ECJ's and the CFI's application of article 81 (3) purely non-competition factors have rarely been considered enough to exempt an agreement from prohibition. In *Metro* and *Métropole* the public policy aims were supplementing factors in an efficiency assessment. This can be explained by the ECJ's and CFI's attempt to uphold the bifurcated structure of article 81 and to be loyal to the wording of article 81 (3). The problem is that, considering the Courts' interpretation of article 81 (1), weighing competition issues under article 81 (3) will often imply a double-treatment of the same issues.

2.3: Should the Commission and the European Courts give non-competition concerns relevance in their application of article 81 (3)?

If the Commission and the European courts should not take non-competition concerns under article 81 (3) and considering that weighing competition issues in this context would imply weighing the same issues twice, the EC should abandon article 81 (3).

Legally it is justifiable that the Commission and the European courts take non-competition concerns in their application of article 81. First, the ECJ has held on numerous occasions that article 81 has to be read in conjunction with the other objectives of the Community, set out in article 2 and 3.¹²¹ The condition set in article 81 (3), that states that the agreement must lead to an improvement in "production or distribution of goods" or lead to the promotion of "technical and economic process"

¹²⁰ See *Metro*, supra note 82, *O2 (Germany) v Commission*, supra note 94 etc.

¹²¹ *Walt Wilhelm v Bundeskartellamt*, case 14/68 (1968), ECR 1, 14, *Europemballage Corporation and Continental Can Company Inc v, Commission*, case 6/72 (1973) ECR 215, 244-245

is textually open enough, from an interpretive perspective, to justify the examination of non-competition factors.

The Treaty is also designed to allow the Commission and the European Courts to consider other policy aims by the inclusion of “cross-sectional clauses”.¹²² Article 127 (2) EC says that the “objective of employment shall be taken into consideration in the formulation and implementation of Community policies and initiatives.” The term “shall be taken into consideration” can be interpreted as a duty for the Commission and the European courts to consider the consequences competition issues will have on employment. Similar cross-sectional clauses can be found for the promotion of environmental, industrial and consumer protection policies.¹²³

In *Metro* and *Métropole* the public policy aims were only supplementing factors for exempting an agreement. In *CeCed* the Commission arguably gave non-competition concerns increased weight under article 81 (3). The majority of washing machines producers in the Community entered into an agreement which was designed to eliminate washing machines that consumed high quantities of electricity. The agreement reduced consumer choice and was harmful to manufacturer that lacked the necessary technical expertise to produce such machines and was therefore anti-competitive. The Commission equated the aim of reducing pollution with economic efficiency, thereby allowing them to exempt the agreement from prohibition.

It is questionable whether this decision is coherent with the wording of article 81 (3). The first positive cumulative condition in article 81 (3) is, as mentioned above, textually open enough to justify the Commission’s decision. The question is whether this decision is in conflict with the requirement that states that consumers must receive a fair share of the resulting benefits.

Environmental benefits relate to social welfare and cannot be linked with any specific group of consumers.¹²⁴ In *CeCed* the Commission stated that such “environmental results would adequately allow consumers a fair share of the benefit even if no benefits accrued to individual purchasers of machines.”¹²⁵ The term “consumers” is thereby given a broad definition, where the underlying idea is that consumers are part of society and will thereby benefit from social welfare. By interpreting the consumer concept in such a broad manner the Commission risks several contextual problems. “Consumers” is a term that is often used in EC competition law. The term is, for instance, directly

¹²² Monti, *supra* note 6, page 1069

¹²³ Industrial policy: Article 157 (3), Environmental policy: Article 6 and Consumer Protection, Article 153 (2)

¹²⁴ Halil Rahman Basaran: How should Article 81 EC address agreements that yield environmental benefits, *European Competition Law Review*, 2006, page 480

¹²⁵ *CeCed*, *supra*, paragraph 56

considered when defining the relevant market or when determining dominance.¹²⁶ Especially after the enforcement of the “modernization” regulation it is important that concepts and expressions will be given the same meaning throughout EC competition law to create legal certainty and an equal legal treatment of competition issues in the Community.

To avoid these potential interpretive difficulties the “consumer” term should be given a more narrow scope and the decision in *CeCed* should be viewed as a single incident. Because of the wording of article 81 (3), non-competition concerns can therefore only be supplementing factors in an efficiency assessment. This questions the role of article 81 (3). Carrying out a balancing exercise where pro-competitive effects are weighed against anti-competitive effects under article 81 (3) will imply a double-treatment the same issues. This is time-consuming, expensive and leads to legal uncertainty and cannot be justified. A very limited scope of factors should therefore be relevant under article 81 (3).

In the Commission’s “White Paper on Modernization” it was suggested that the Commission and the European Courts should withdraw from taking non-competition concerns in their application of article 81 (3). The underlying thought was that article 81 (3)’s function is to provide a “legal framework” for the “economic assessment” of agreements.¹²⁷ Permitting the evaluation of other public policy aims in this context would possibly lead to a situation where competition rules were set aside because of political factors.

The fact that national competition authorities and national courts are permitted to exempt agreements from prohibition, following the implementation of the “modernization” regulation, increases the need for a single and unified interpretation of article 81. The simpler the rule is the more consistent the interpretation of the provision will be. Allowing the examination of non-competition concern has the potential of creating a lot of legal uncertainty. On the other hand, limiting the competition authorities’ and the courts’ competence to balancing purely competition issues can be unpractical and lead to unfair results.

It is debatable whether non-competition concerns should be taken into account in the application of article 81. The one thing that is certain is that weighing non-competition concerns under the CFI’s and the ECJ’s current approach of article 81 (1) and 81 (3) is problematic. To give other public policy aims relevance under the current enforcement system it seems necessary that they are weighed in the context of article 81 (1). The case-law examined above has shown that they are only

¹²⁶ Commission Notice on the definition of relevant market for the purposes of Community competition law, (OJ 1997, No. C372/5, paragraphs 7 and 10

¹²⁷ Monti, *supra* note 6, page 190

supplementing factors and to avoid a double treatment of competition issues they should be balanced under this provision.

Overall it must be concluded that article 81 (3) has lost much of its function under the current enforcement system. It is difficult to pinpoint exactly what the role of the provision is. The various block exemptions have created a lot of legal certainty for the market participants. This alone is, however, not enough to justify to maintaining of the bifurcated structure of article 81.

Chapter 3: How should article 81 be formulated: high precision rules versus specific intervention?

The last chapters considered the role of article 81 (3) under the current enforcement system in EC competition law and whether the Commission's and European courts' application of article 81 (1) make the provision ineffective and whether it therefore should be abandoned. This chapter examines, from a normative perspective, how competition law should be shaped and formed. This examination will focus around the relationship between a specific and rule-based enforcement system, how detailed competition rules should be and whether article 81 should be modified or renewed all together.

This paper has shown that EC competition authorities are focusing increasingly on economic analyses and have developed a broad application of the rule of reason. The question this chapter asks is whether this is a positive development and whether the application of per se rules is preferable.

The economic and legal justification behind a case-by-case analysis on competition issues are that it leads to reasonable and objective results. Some economist will even argue that high precision rules lead to allocative *inefficiency*.¹²⁸ The inherent ambiguity of legal phrases, human incompetence and limited foresight creates loopholes between the predicted coverage and the conduct sought to be regulated.¹²⁹ The result is that general standards lead to both over – and under enforcement.

Specific intervention also enables competition authorities to respond to market changes and economic developments and to adjust the law accordingly. Competition law is a dynamic field where economic theories and policies change consistently. The need for judicial rulemaking is therefore prominent. The ECJ has stated that a teleological interpretation principle applies in EC law.¹³⁰ This implies that the decision maker must seek to find the spirit of the text rather than interpret the text literally. This interpretive principle reflects competition law's dynamic and evolutionary aspect.

¹²⁸ See chapter 1: page 9-11

¹²⁹ Isaac Ehrlich and Richard Posner: An economic analysis of legal rulemaking. *Journal of Legal Studies* 257 (1974), page 268

¹³⁰ *Srl CILFIT and Lanificio di Gavardo SpA v Ministry of Health*, Case 283/81, paragraph 20

The complete opposite of the “rule of reason” is the application of per se rules. These rules can again be divided in rules that are per se illegal and per se legal. Per se rules require the decision-maker to generalize a class of cases and are justifiable where few common or important cases lead to the opposite result.¹³¹

The rule-bound approach is supported by several arguments. First, clear and general rules lead to legal certainty. A case-by-case analysis gives the market participants little predictability and specific interventions can lead firms to adopt welfare reducing policies.¹³² Companies may be deterred from adopting the most efficient and productive distribution system or from entering into pro-competitive agreements because of the fear of infringing competition law. In other circumstances firms may engage in anti-competitive behaviour or test the scope of competition law, since the possible gain may outweigh the risk of prosecution.¹³³ Specific intervention can therefore have the opposite effect of the envisaged result.

According to economic studies increased predictability results in a higher settlement rate.¹³⁴ This in turn will have a positive outcome for the allocation of society’s resources, since settling a dispute outside the courtroom reduces the total cost of dispute resolutions. The expenditures in settling a dispute can also be reduced since it is easier to come to a common understanding if the rules are clear.

Secondly, clear and general rules reduce the possibility for judicial abuse. The side-effect of a high degree of discretionary rules is arbitrariness, political favoritism and other forms of third-party interference.¹³⁵ Political pressure and other types of rent-seeking activities can occur in three different phases.¹³⁶ First, legislators may favour certain groups in the rule-making process. It can be argued that there is less latitude to abuse their legislative power if the rules are simple and clear; arbitrariness and political favoritism are more easily detected. On the other hand, the lack of judicial discretion prevents the courts from adjusting the law when “abuse” has occurred.

In EC competition law there is a further risk that guidelines and notices will be targeted and altered by the interests of strong and well established political or economical lobby groups.¹³⁷ Even though the guidelines are not binding for the European courts¹³⁸ it is likely that their interpretation and

¹³¹ *GTE Sylvania*, supra note 59, 50

¹³² Christiansen, supra note 8, page 219

¹³³ Christiansen, supra note 8, page 232

¹³⁴ Isaac Ehrlich supra note 129, page 265

¹³⁵ Isaac Ehrlich supra note 129, page 260

¹³⁶ Christensen, supra note 8, page 233

¹³⁷ Christensen, supra note 8, page 233

¹³⁸ Guidelines on vertical restraints, supra note 17, paragraph 4, Guidelines on the application of article 81 (3), supra note 42, paragraph 7, etc.

understanding of EC competition concepts and rules will be given weight in dispute proceedings. The consequences of abuse in this phase can therefore have a significant impact on competition law.

Lastly there is a risk that the competition authorities may be influenced in individual cases. This influence can either come directly from the evolving firms or indirectly from political pressure.¹³⁹ The less degree of discretionary power, the less chance there is for judicial abuse in this phase. If the courts can exempt an agreement for various reasons or if the analysis carried out by the courts is effectively open-ended it becomes significantly more difficult to detect abusive behaviour.

Thirdly, a case-by-case analysis will necessarily involve wide market investigations, the delimiting of the market place and other economic enquires that require the decision maker to have firsthand and reliable information available. Companies will often try to strategically withhold important information and the courts will often have serious knowledge problems.¹⁴⁰ Clear and general rules might therefore lead to fewer wrong decisions compared to optimized case-by-case interventions.

After the publication of the *GTE Sylvania* case Posner questioned whether the rule of reason was the preferable testing standard for anti-trust cases in the United States. In his view, the Supreme Court's reasoning opened too broad a legal framework.¹⁴¹ The formulation of the rule of reason in that case is similar to the standard analysis applied in the U.S. today and his criticism is therefore still justifiable. The reason why he felt the rule of reason was not the appropriate testing standard in anti-trust cases was because of incompetence by the decision makers combined with a poorly articulated test. In his opinion the juries, the Federal Trade Commission and inexperienced federate district judges would find it difficult to understand antitrust standards and weigh expert testimonies that contradicted each other.¹⁴²

In EC competition law the EC commission and the European courts have to be characterized as competition law specialists and the arguments of Posner do not therefore apply to the same extent. The competition authorities are, however, not economists and must often rely on expert testimonies. National courts, on the other hand, have generally limited experience with competition related issues and are therefore often worse equipped to carry out complex economic analyses. The fact that national competition authorities have to apply article 81 in a similar way to the EC competition authorities is a strong argument for clear and general rules.

¹³⁹ Christiansen, supra note 8, page. 233

¹⁴⁰ Christiansen, supra note 8, page. 233

¹⁴¹ Posner, supra note 31, page 15

¹⁴² Posner, supra note 31, page 16

Of course the available options are not merely diametrically opposed case-by-case economics approach and the per se rule approach. Indeed several academics suggest analysis standards that have aspects from both a rule-bound approach and specific intervention. Christiansen, for instance, supports the increased input of economics in competition law issues, but emphasizes that focusing on a case-specific enforcement system can have negative welfare effects. These negative effects are a direct result of the rising enforcement costs, rent-seeking problems and legal uncertainty.¹⁴³ In his opinion EC competition rules should be formed with the view of achieving the optimal complexity of rules. This will be the case where the marginal benefit of additional differentiated rules exceeds the marginal costs.¹⁴⁴ The desired effect is that the application of rules will reduce decisional errors of type I (false positives) and type II (false negatives).

Christiansen's analysis of optimally differentiated rules is examined from the view of maximizing consumer welfare. Consumer welfare will in accordance with this model be highest when error costs are in equilibrium with regulation costs and rent seeking costs. Decision errors are an inevitable consequence for various reasons. First, the competition rules are often imperfect. Since the legislator cannot predict every possible scenario the rules often prohibit beneficial practices or allow for harmful conduct. The rules can also be too formalistic and not take into account economic factors. This was the case under the structuralism-paradigm in the United States and Europe where vertical restraints were considered per se illegal.

In other cases the assessment that has to be carried out by the courts is based on ambiguous and complex conditions and economic factors. Before deciding whether an agreement restricts competition the courts must, for instance, delimit the market. This is a complex economic assessment that can lead to wrong decisions. The delimiting of the market enables the court to determine the competitive constraints companies' faces on the market place.¹⁴⁵ If the parties to an agreement face sufficient competition it is unnecessary to intervene because the market will eliminate the anti-competitive behaviour. Wrong estimations from the courts or lack of information about available substitutes can have a major impact on the final decision.

The increased complexity and differentiation of rules will necessarily lead to a more efficient separation between pro and anti-competitive behaviour. This will in principle decrease type I and type II decisional errors. The problem is that differentiated rules do not always separate perfectly between the two types of behaviour. Christiansen therefore argues that the question about the optimal complexity of rules should be evaluated from the perspective of "separation effectiveness":

¹⁴³ Christiansen, supra note 8, page 224 -.

¹⁴⁴ Christiansen, supra note 8, page 237

¹⁴⁵ Commission Notice on the definition of the relevant market, supra note 126, paragraph 2

Only in circumstances where the *complex* provision can effectively separate between pro and anti-competitive behaviour is it justifiable to have a high degree of differentiated rules.¹⁴⁶

Regulation costs are the definition for every direct or indirect cost for the formulation and application of competition rules. These can basically be divided in set-up costs, monitoring costs, information and administration costs, compliance costs and indirect costs due to legal uncertainty.¹⁴⁷ Regulation cost can be expected to rise somewhat proportionally with the higher degree of differentiated rules. With the higher degree of complexity of competition rules the more criteria' have to be evaluated and more advanced market investigations have to be carried out.¹⁴⁸

Set up costs are a fixed costs and can be expected to rise with the higher degree of differentiated rules. The costs of formulating a rule are highest when the object and wording of the provision are subject to political controversy; negotiations become necessary which are time-consuming and expensive.¹⁴⁹ In EC competition law it is in addition costly to formulate the different guidelines. The more differentiated the rules are the more complex the guidelines must necessarily be. Gifford therefore argues that complex rules should be limited to areas where the number of enforcement proceedings is high.¹⁵⁰

The next major group of regulation costs is the expenses spent on gathering information and having dispute proceedings. The more differentiated the rules are the more information will have to be gathered and the lengthier the proceedings will necessarily be. The costs are variable and depend on the depth of analysis that has to be carried out, the range of relevant factors and whether there are a lot of objective justifications.¹⁵¹

Firms and the competition authorities incur costs outside the dispute resolution as well. First, firms have to adapt their behaviour to the competition rules. In this phase they might incur costs by having to change established practices and reconsider certain agreements. There are also expenses in the form of legal advice and other types of consultation services. The Commission, on the other hand, has to spend resources on monitoring the market on a regular basis. These expenses can be categorized as partly fixed and partly variable costs.¹⁵² The costs of compliance and the monitoring

¹⁴⁶ Christiansen, supra note 8, page 231

¹⁴⁷ Christiansen, supra note 8, page 231

¹⁴⁸ Christiansen, supra note 8, page 231

¹⁴⁹ Isaac Ehrlich, supra note 129, page 267

¹⁵⁰ Gifford: Discretionary decisionmaking in Regulatory Agencies: A Conceptual framework, published in; Making Regulatory Policy, Hawkins, Thomas

¹⁵¹ Christiansen supra note 8, 232

¹⁵² Christensen supra note 8, 232

costs are likely to rise with a higher degree of differentiated rules: Anti-competitive behaviour becomes more difficult to detect and the legal expenses increase.

The costs incurred by legal uncertainty and lack of predictability are difficult to measure. It is, however, likely that the indirect costs due to legal uncertainty will rise with a higher degree of differentiated rules. The market participants will, as mentioned earlier, have difficulties knowing in advance which practices will be deemed legal or illegal. The fact that firms may be deterred from adopting welfare enhancing practices or inclined to adopting welfare reducing policies with the hope of escaping prosecution can amount to significant costs for the society.

The third important group of expenses in Christiansen's model of optimal differentiated rules is rent seeking costs. This will be the costs society and firms have to incur because of the type of judicial and political abuse mentioned earlier in this chapter.¹⁵³

Put simply Christiansen's model asks four simple questions when evaluating what the optimal differentiated rules are for a specific practice.¹⁵⁴ First, what percentage of cases has welfare enhancing effects and how many have welfare reducing effects? Secondly, how large is the separation effectiveness? Thirdly, what are the possible dangers for wrong decisions due to judicial abuse and corruption? Lastly, what are the additional regulation costs?

The vertical block exemptions can be viewed as an attempt on applying the model of optimal differentiated rules. In accordance with article 3 the block exemption set in article 2 only applies as far as the market share of the supplier does not exceed 30%. The error costs under this market share threshold are likely to be low: When firms have such a low market share the market will eliminate any anti-competitive behaviour on its own. It is therefore unnecessary and maybe even harmful for competition and the market if the competition authorities or courts intervene. When the market share of the supplier exceeds 30% the error costs are likely to rise and it is therefore justifiable to carry out a more case-oriented evaluation.

After the publication of the *Leegin* case there has been a debate about whether vertical price restraints should continue to be deemed per se illegal.¹⁵⁵ Viewed from the perspective of achieving optimal differentiated rules it can be questioned whether this debate should continue. The dissenting Judge in *Leegin* emphasized that the separation effectiveness on these sorts of practices

¹⁵³ See pages 33-34

¹⁵⁴ Christiansen, supra note 8, 238

¹⁵⁵ Mart Kneepkens: Retail price Maintenance, economics calls for a more balanced approach, *European Competition Law Review*, 2007, Femi Alese: Unmasking the masquerade of vertical price fixing, *European Competition Law Review*, 2007

are low.¹⁵⁶ He furthermore pointed out that the regulation costs were high and that fewer cases would be prosecuted before the courts which could lead firms to adopting welfare reducing practices with the hope of escaping prosecution. The marginal costs of permitting retail price maintenance are therefore likely to be inversely proportional to the benefits of additional differentiated rules.

From an overall viewpoint Christiansen supports the adoption of a more “economic approach” in EC competition law, but believes economic analysis should be used as a tool for the formulation of optimal differentiated rules. There are some flaws in Christiansen’s model. First, the model is not well equipped to deal with changes in competition law. Secondly, a class of cases can have been under-prioritized by the competition authorities and the courts in certain enforcement-periods. In those circumstances there will be little available data about the practice’s pro- and anti competitive effects. This does not imply that the practice in question should be deemed per se legal or per se illegal. In fact the nature of the practice could suggest that a full-scale evaluation is the preferable testing standard. The decision on what degree of differentiated rules is optimal can therefore often be made on a limited and wrong foundation.

The cost-measurements will also necessarily be suggestive and diffuse. Particularly when it comes to indirect costs are there difficulties making correct estimations. The costs incurred with an additional degree of differentiated rules can therefore be significantly higher than first assumed. Lastly, it can be questioned whether it is justifiable to consider the regulation costs in the formulation of competition rules. Certain practices are better suited for one industry and vice-versa. It can therefore be viewed as unfair and even arbitrary to prohibit a certain practice solely because of the likely costs.

Beckner has a similar perspective on competition law. However, instead of focusing on competition rules his model is centered on legal proceedings. In his view the estimation of optimal differentiated rules should be carried out by studying two equally important factors; the cost of gathering more information and the benefits of gathering that additional information. Beckner’s model is based on a multi-stage decision process divided in seven stages.¹⁵⁷ In each stage the court must decide whether to conclude on the subject with limited information or gather additional information.

In the first phase of Beckner’s model the court bases its initial decision on general and case-specific presumptions. If the court concludes on the subject the decision will in many ways equal the application of per se rules. If the court finds that it does not have the foundation to come to a fair and correct decision it must gather and examine more information. According to Beckner’s theory additional information reduces the chances for judicial and factual errors. In each stage the court

¹⁵⁶ *Leegin*, supra note 62, page 68-73

¹⁵⁷ Beckner and Salop, Decision theory and antitrust rules, *Antitrust law journal* 67, 1999-2000, page 55

must carry out the same considerations. The seventh and final step in this model equals the application of the rule of reason.¹⁵⁸

This model can also be criticized. First, it requires the court to have a certain degree of knowledge of general presumptions, costs and possible benefits. Particularly when it comes to the national courts it is likely that their limited experience makes this model overly-complicated. There is also a risk that if this model was adopted it would lead to different enforcement-practices throughout the Community.

An argument that is closely related to this subject is that the model attributes too much power to the decision makers. This will necessarily increase the dangers of judicial abuse. From a democratic point of view the European Parliament should also be a part of the legislation process. They are the only EC organization that is chosen directly by the people of the Member States which is a strong argument for limiting judicial discretion.

How article 81 should be shaped and formed is a complex and difficult question to answer. Several factors point in different directions. Per se rules lead to legal certainty, but can lead to unfair results. A case-by-case analysis gives decisions a more objective foundation. However, the proceedings are often time-consuming, expensive and it is often difficult for the business society to predict their legal future and adopt their behaviour accordingly. Christiansen's and Beckner's models are theoretically very persuasive, but it is difficult to anticipate how the models would function in practice. The two models meanwhile represent in many ways the standards by which the EC should base the formulation of rules according to.

Chapter 4: Conclusion:

In this thesis I first examined the role of article 81 (3) under the current EC enforcement system. This analysis has shown that the European Courts have adopted something similar to the American rule of reason doctrine in their application of article 81 (1). This does not, however, imply a full-scale adoption of the American standard analysis test. In fact the Community case-law suggests that only competition issues can be balanced in the context of article 81 (1).

This has left a vacuum in the application of article 81 (3). The four conditions set in the provision suggest that only efficiency enhancing effects can result in an exemption from prohibition. The problem is that this will necessarily imply carrying out a very similar "pro vs. con" analysis twice in the application of article 81. This cannot be economically or legally justified; it entails an unnecessary

¹⁵⁸ Beckner, supra note 157, page 56-58

use of resources and creates legal uncertainty.

The paradox in not carrying out an economic assessment under article 81 (3), is that the case-law relating to the achievement of other public policy aims loses its weight. Public policy concerns have only been given supporting weight in an efficiency assessment. Another approach will also arguably be in conflict with the text of article 81 (3). Meanwhile allowing the national courts and the national competition authorities to consider non-competition concerns in their application of article 81 (1) has the potential of giving them an uncontrollable degree of discretion, which can lead to a heterogeneous legal treatment of competition issues in the Community.

Under the current enforcement system there seems to be few acceptable solutions to this dilemma. The standard article 81 (1)' analysis applied by the CFI and the ECJ does not conform to the bifurcated structure of article 81. The end-result is that the EC should either adopt an approach that is coherent with the text and structure of article 81 or narrow the provision's scope to purely competition related issues and abandon article 81 (3).

The next step in my thesis was to consider whether article 81 should be modified from a normative perspective. The fact is that there are several contradicting arguments for per se rules, the rule of reason and an intermediate solution. From an economic perspective the intermediate solution is the preferable one. Applied properly the overall costs are proportional to the benefits of a higher degree of differentiated rules.

To enable the business society to compete globally the competition rules should not differ or be stricter than similar rules in other countries. This is a strong argument for adopting the American rule of reason doctrine. On the other hand it can be argued that the business society will benefit from clear and precise rules in the long run. This will enable them to map out their future and adopt long-term practices.

Overall it has to be concluded that every alternative has positive and negative aspects. The unacceptable solution is the one that exists today. The European Courts and the European legislators should either be faithful to the bi-furcated structure of article 81, abandon article 81 (3) or modify the provision completely. The current EC approach only has the potential to create more debates and legal uncertainty.

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