European Competition Law

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ARTICLE 101(3)

ARTICLE 101(1) may be declared inapplicable to any agreement/decision/concerted practice which:

- provides specified benefits (i.e. improves production or distribution of good/services or promotes technical or economic progress);
- allows consumers a fair share of the benefit;
- doesn’t contain any indispensable restrictions;
- doesn’t eliminate competition in a substantial part of the products in question.
OECD point of view

• The approach to anti-competitive practices should be:
  • **accurate** – based on widely accepted economic principles and yielding minimal costs from false positives and false negatives;
  • **administrable** – relatively easy to apply;
  • **applicable** – the wider the scope of conduct the approach can cover well, the better;
  • **consistent** – it should yield predictable results;
  • **objective** – it should leave no room for subjective input from the decision-maker;
  • **transparent** – the approach and its objectives should be understandable.
POSSIBLE WAYS OF RECONCILING ARTICLE 101(1) AND 101(3)

- To adopt a literal or broad interpretation of Article 101(1), bringing many agreements within its net and conducting a more detailed analysis of the anti-competitive, pro-competitive and other aspects of the agreement within the more structured framework of Article 101(3).

- To conduct a more detailed analysis when determining whether an agreement has as its object or effect the “restriction” of competition (Article 101(1)) and to thereby confine the role of Article 101(3).

- To divide the substantive appraisal more evenly between the two parts: to use Article 101(1) to identify presumed, actual or likely anti-competitive effects and Article 101(3) to enable the parties to establish that the agreement achieves offsetting efficiencies or pro-competitive effects.

- [Neither the Commission nor the Court’s approach equates exactly to any of those above].
THE INTERPRETATION OF “OBJECT OR EFFECT IS THE PREVENTION, RESTRICTION, OR DISTORTION OF COMPETITION” – THE BROAD APPROACH

• The Commission found that many agreements were caught within the widely cast net of Article 101(1) but subsequently completed its analysis and authorized many agreements, using Article 101(3), motivating this approach by ideology and practicalities:
  – the Commission utilized Article 101 to limit restrictions on conduct, to promote rivalry between undertakings operating on a market and to prevent interferences with the single market project.

• A broad jurisdictional interpretation of Article 101(1) cemented the Commission’s central role in the development of EU competition policy since it had the exclusive right to apply Article 101(3) through the system of “notification and exemption”.
What if the Commission had adopted a narrower approach of Article 101(1)…

- Greater enforcement of agreement would have been delegated to the national level;
- The national competition authorities together with the national and EU courts would have played a greater role in the development of competition policy;
- The interpretation of Article 101 might have evolved differently and the uniform interpretation of the competition rules might have been compromised.
- National courts may have adopted divergent views on the restriction of competition [although Article 267 TFEU sets out a procedure for national courts to refer questions relating to the interpretation of EU law, only courts from which there is no appeal are obliged to make sure such a reference].
ARGUMENTS IN SUPPORT OF THE NEED FOR A MORE SOPHISTICATED ECONOMIC APPROACH

- The broad approach failed to provide transparent, predictable and operable criteria for businesses to apply;
- It wrongly favoured the freedom of individual traders and competitors over consumer welfare;
- That approach led to the condemnation under Article 101(1) of innocuous agreements which didn’t in fact restrict competition through anti-competitive effects;
- If a weighing of anti-and pro-competitive effects was conducted under Article 101(1), many of the procedural problems experienced in the application of Article 101 would fall away. Fewer agreements would need either to be notified and subjected to the interminable delay involved in gaining Commission authorization or drafted to comply with rigid block exemptions;
- The Commission’s resources would be freed to deal with the more serious violations of the competition rules and the rarer cases which would demand scrutiny under Article 101(3);
- An economic approach was needed by the case law of the ECJ which had not interpreted the restriction of competition so broadly as the Commission.
SECTION I OF THE SHERMAN ACT 1890 (USA)

• “Every contract, combination in the form of a trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal”. No legal exception to the prohibition are provided.

• 1960’s – for the sake of business certainty and litigation efficiency the courts were prepared to tolerate the invalidation of some agreements that a full-blown rule of reason inquiry might have proved to be reasonable.

• 1970’s – the Supreme Court began to retreat from its formal position, embracing rule of reason analysis.

• Since 1977 the presumptive and prevailing standard has been the “rule of reason”:
  – Agreements are not assumed to be illegal, but are assessed in their legal and economic context to determine “whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition.
  – The anti- and pro-competitive aspects of the agreement are weighed before it is condemned as illegal.

• Regardless of the fact that the borrowing of terms from a different system might confuse more than clarify, the core message was simple: a less formalistic and more economic approach was required under Article 101 on the wake of the US rules.
On 1 May 2004, Regulation 1/2003 abolished the Commission’s exclusive right to rule on the compatibility of an agreement with Article 101(3), rendering it directly applicable as a legal exception to Article 101(1) also by national competition authorities and national courts:

– Art.1 Reg.1/2003: Agreements which are caught by Art.101(1) and which do not satisfy the conditions of Art.101(3) are prohibited, no prior decision to that effect being required. Agreements which are caught by Art.101(1), but which satisfy the conditions of Art.101(3), are not prohibited, no prior decision to that effect being required.

The Commission has gradually detached itself from its earlier interventionist policy, moving towards an acceptance that consumer welfare should be the benchmark against which agreements are tested.

Article 101(3) provides the appropriate forum for weighing the restrictive effects of the agreement, identified at Article 101(1) stage, against the economic benefits and efficiencies created by the agreement [White Paper on Modernization 1999]
The General Court’s judgment in *Métropole*

- **Métropole (2001):** the General Court echoing the view of the Commission stated that Article 101(3) provided the correct forum for weighing the pro-and anti-competitive aspects of the agreement.

- The Court recognized that some EU cases had favoured a “more flexible” interpretation of the Article 101(1) prohibition (STM-1966), but they didn’t establish the existence of a *rule of reason*. They simply formed part of a broader trend in the case law according to which it is not necessary to hold that any agreement restricting the freedom of action of one or more of the parties is necessarily caught by Article 101(1).

- The Court indicated that the Article 101 appraisal should be divided into five parts:
  - The Commission must establish that the agreement restricts competition;
  - The parties must establish that the agreement achieves pro-competitive objectives;
  - Consumers attain a fair share of those benefits;
  - The agreement is indispensable to the attainment of the benefits;
  - There is no possibility of an elimination of competition.
OBJECT OR EFFETC

• Since the judgment in LTM (1966) the ECJ has held that the words “object or effect” are to be read **disjunctively**:  
  – Where the object of the agreement is said to restrict competition, there’s no need to look further and to prove its restrictive effects.  
  – Where the object cannot be said to restrict competition, an agreement will not infringe Article 101(1) unless its effect can show to be the restriction of competition.  

• **Burden of proof:**  
  – In the former case a violation of Article 101 is proved unless it can be demonstrated that the agreement satisfies the Article 101(3) criteria  
  – In the latter case the burden of proving the restrictive effect is on the person alleging the breach. Only once established that the burden shifts onto the parties to defend the agreement under Article 101(3).

• *Restrictions of competition by object* are those that “by their very nature” have such a high potential of negative effects on competition that it is unnecessary for the purposes of applying Article 101(1) to demonstrate any actual effect on the market. This presumption is based on the serious nature of the restriction and on experience showing that restrictions of competition by object are likely to produce negative effects on the market and to jeopardize the objectives pursued by EU competition rules.
Horizontal agreements restrictive by object

- **GalaxoSmithKline Unlimited (2009) ECJ**: to determine whether conduct is “by its very nature” injurious to competition regard must be had inter alia to the content of its provisions, the objectives it seeks to ascertain and the economic and legal context of which it forms part.

- **European Night Services (1998) General Court**: provisions in agreements between competitors fixing prices or sharing markets will automatically be held to restrict competition.

- **Competition Authority v. BIDS (2008) ECJ**: an agreement between beef and veal processors designed to reduce processing capacity had as its object the restriction of competition.

- **T-Mobile Netherlands (2009) ECJ**: an exchange of information designed, directly or indirectly, to fix purchase or selling prices might have an anti-competitive object.
Vertical agreements restrictive by object

• **Consten and Grundig (1966):** is one of the most important judgment in EU competition law. The ECJ not only established that Article 101(1) applies to:
  – horizontal and vertical price fixing agreements,
  – all agreements which affect trade between Member States even if the effect on trade is not a prejudicial one, and
  – potentially to agreements relating to the licensing of intellectual property rights,

The ECJ also held that Article 101(1) applied to an agreement which had as its object the restriction of competition **irrespective of its alleged effects** (although the parties have been able to show that the agreement was *necessary to ensure that the supplier found an outlet for its products*).
Consten and Grundig Case from the single market perspective

• Apart from the economic justifications
  – the need to stimulate competition between dealers;
  – the need to maintain intra-brand (between distributors) as inter-brand (between producers) competition;
  – the fact that restrictions on intra-brand competition may facilitate brand differentiation and diminish competition between producers;

• The affront to the single market goal was in this case too severe:
  – The object of the agreement was designedly to grant absolute territorial protection and to eliminate competition at a wholesale level in Grundig products in the French territory, with the consequent isolation of the French market and the exclusion of the French distributors from all effective competition.

• The ECJ firmly asserted that agreements which divide up the common market and preclude all cross-border trade in the contract product will not be tolerated.
THE SUBJECTIVE INTENTION OF THE PARTIES

• BIDS (2008) ECJ: Closer regard is paid to the wording of the agreement provision and to the objective which is intended to attain, than the subjective intention of the parties.

• The parties had argued that by acting to reduce capacity they had not acted with an anti-competitive purpose or an intention to injure competition and the welfare of consumers. They alleged that they had sought to rationalize the beef industry and so make it more competitive by reducing, but not eliminating, production overcapacity.

• The Court rejected this argument and replied that an agreement may be regarded as having a restrictive object even if it doesn’t have the restriction of competition as its sole aim but also pursues other legitimate objectives.
THE ECONOMIC AND LEGAL CONTEXT

• In some unusual horizontal cases involving price-fixing which was not “naked”, the Commission seemed prepared to accept that the arrangements should not be found to have as their object the restriction of competition where the price fixing might be ancillary to an efficiency enhancing joint venture (Visa International-Multilateral Interchange Fee 2002).

• In subsequent cases, the Commission retreated from this approach (Reims II 2004, MasterCard 2007), gaining some support from the judgment of the ECJ in Coop de France bétail et viande (2008):
  – The General Court had taken the economic context into account when making its determination that the purpose of the agreement was to restrict competition in the single market and to distort the setting of prices. There was no need to take account of the actual effects of an agreement once it appears that its object is to restrict competition.
AGREEMENTS THAT RESTRICT COMPETITION BY EFFECT

• Article 101(3) Guidelines – Commission: in Article 101(1) “effects” cases there’s no presumption of anti-competitive effects: it’s necessary to prove that the agreement
  – either affects actual or potential competition to such an extent that on the relevant market negative effects on prices, output, innovation or the variety or quality of goods and services can be expected with a reasonable degree of probability (inter-brand competition);
  – or restricts a supplier’s distributors from competing with each other since potential competition that could have existed between the distributors absent the restraint is restricted (intra-brand competition).

• If the transaction proves to be not restrictive, the restraints “ancillary” to the main non-restrictive transaction also fall outside Article 101(1).
Restraints on Inter-Brand Competition

- **Delimitis v. Henninger Bräu (1991)** ECJ: in determining the effect of the agreement
  - It’s first necessary to define the relevant market;
  - It must then be ascertained whether there is a concrete possibility for new competitors to penetrate the market or existing competitors to expand, taking into account of the number and size of producers operating on the market, the existence of networks of agreements, the saturation of the market, the brand loyalty, etc.
  - If analysis shows that access to the market is inhibited it must be assessed whether the agreement in question contributes appreciably to that situation, looking at the contractual restraint in the context in which it operates before its effect can be determined
Restraints on Inter-Brand Competition

• **European Night Services (1998):** the General Court held that account has to be taken of:
  – the economic context in which the undertakings operate,
  – the products or services covered by the agreement and
  – the actual structure of the market concerned.

• It’s important to examine the conditions of competition, including existing and *potential competition*, in order to ascertain whether there are real concrete possibilities for the undertakings concerned to compete among themselves or for a new competitor to penetrate the relevant market and compete with the undertakings already established.

• **O2 GmbH & Co OHG v. Commission (2006):** the General Court stressed that the examination required in the light of Article 101(1) consists in taking account of:
  – the impact of the agreement on existing and potential competition and
  – the competition situation in the absence of the agreement.
Restraints on Intra-Brand Competition

- **STM (1966):** the ECJ indicated that an exclusive distribution agreement would not restrict competition if the appointment of an exclusive distributor was *necessary* in order to enable a manufacturer to penetrate a new market.

- The agreement should be examined in the light of the competition which would occur *if it was not or had not been made*. In this case it seemed that the economic justifications for the agreement might outweigh the territorial restrictions inherent in the agreement.
Ancillary restraints

• Article 101(3) Guidelines: the Commission states that if a main transaction doesn’t restrict inter-or intra-brand competition, individual restraints in the agreement ancillary to it (i.e. directly related and necessary to its implementation and proportionate to the main non-restrictive distribution or joint venture agreement) will also be compatible with Article 101(1).

• The Commission relies on the ECJ’s rulings in:
  – Remia and Nutricia (1985) that a reasonable non-compete clause in an agreement for the sale of a business would ensure that the transfer had the intended effect and didn’t restrict competition;
  – Pronuptia (1986) that restrictions on a party’s conduct necessary for the successful operation of a franchising distribution agreement did not infringe Article 101(1);
  – Gøttrup-Klim (1994) that the restraints necessary to enable the parties to set up an effective group purchasing association didn’t infringe Article 101(1)

as examples of cases where restraints ancillary to a pro-competitive agreement have also been held to be compatible with Article 101(1).
ARTICLE 101(3)

- The burden imposed by Article 101(3) requires demonstration
  1. that the agreement achieves benefits;
  2. that a fair share of those benefits are passed on to consumers;
  3. that the agreement doesn’t contain any indispensable restraint;
  4. that it doesn’t eliminate competition in respect of a substantial part of the products in question.
- The exception rule applies only for as long as the four conditions are met.
Criterion 1. Benefits

- The Commission authorizes agreements which:
  - lead to an improvement in the production or distribution of good or services;
  - promote technical or economic progress.
- The improvement must show *appreciable objective advantages* of such a character as to compensate for the disadvantages which they cause in the field of competition.
  - Parties have to show the nature of the claimed efficiencies, the link between the agreement and the efficiencies, the likelihood and magnitude of each claimed efficiency and how and when each of them would be achieved.
  - Benefits may result from cost reduction, and/or improvement in the quality and choice of goods and services.
- Many joint venture agreements have succeeded on the ground that the cooperation permitted the parties to produce new or better products more quickly or cheaply and/or through the sharing of risk or cost, through the pooling of technical expertise and/or by making the venture financially viable.
Criterion 2. Consumers sharing part of the benefits

• The Article 101(3) Guidelines indicate that this condition should be considered only once determined that the restrictions incorporated in the agreement are indispensable (criterion 3).

• This requirement implies a balancing exercise of pro-competitive and anti-competitive effects, that shouldn’t include restrictions unnecessary to achieve the efficiencies.

• Broad interpretation of the category of “consumers”: not only final consumers but also intermediate, included wholesalers and retailers. It has to be taken into account of the beneficial effect on all consumers in the relevant markets.

• “Fair share”: the pass-on of benefits must at least compensate consumers for any actual or likely negative impact caused by the restriction of competition.
Criterion 3. Indispensable restrictions

- Restrictions will not be indispensable if the efficiencies claimed can be achieved by other practicable and less restrictive means, or if individual restrictions are not reasonably necessary to produce such efficiencies.
- A restriction will be indispensable if its absence would eliminate or significantly reduce the efficiencies following from the agreement.
- The assessment of indispensability must be made within the actual context in which the agreement operates.
Criterion 4. The agreement must not lead to the elimination of competition

- The protection of rivalry and the competitive process is given priority over potentially pro-competitive efficiency gains which could result from restrictive agreements.

- The Commission considers in its assessment:
  - the market shares of the parties;
  - the incentives for actual competitors to compete;
  - the impact of the agreement on the various parameters of competition;
  - the actual market conduct of the parties;
  - past competitive interaction;
  - the closeness of competition previously existing between the competitors;
  - the scope of potential competition.
APPLICATION IN INDIVIDUAL CASES

• Commission may apply Article 101(3) in individual cases in a variety of ways:
  – infringement proceedings where it is raised by persons seeking to rely on it;
  – when adopting commitment or non-infringement decisions;
  – when providing “informal guidance”.

• National competition authorities and national courts may apply it when considering the compatibility of an agreement with Article 101.
BLOCK EXEMPTIONS

• Council Regulation: Reg.1017/68 granting exemption to agreements in road and inland waterway sectors.
• Commission Regulation: a number of block exemption applied to vertical, horizontal, technology transfer, and other particular agreements.
• Art.288 TFEU provides that regulations are directly applicable.
• In the block exemption applying to vertical and technology transfer agreements, the Regulations distinguish between:
  – provisions which mean that the block exemption doesn’t apply;
  – provisions which are not covered by the block exemption but which don’t prevent the remaining provisions of the agreement benefiting from the Regulation.
• Where the conditions of a block exemption are not met, the national court will be bound to determine whether or not the agreement infringes Article 101(1) and, if so, whether it individually meets the Article 101(3) criteria.
MARKET SHARE THRESHOLDS and HARDCORE RESTRAINTS

• According to the new economic approach, the new block exemptions provide a rule of thumb that agreements concluded by undertakings which meet specified market share thresholds, satisfy specified conditions and don’t contain hardcore restraints are unlikely to raise competition problems.

• There are listed only the restrictions which may not be included within an agreement.

• Most block exemption contain a list of hardcore restraints which preclude the application of the exemption if included in the agreement, therefore presumed to violate Article 101. They must be scrutinized individually to determine their compatibility with Article 101(3).
WIThe Regulation 1/2003 provides that the Commission may withdraw the benefit of any Commission block exemption when an agreement, decision or concerted practice to which the Regulation applies has effect which are incompatible with Article 101(3).

• Regulation 1/2003 also provides that national competition authorities may withdraw the benefit of any Commission block exemption where the agreement, to which the regulation applies has effects incompatible with Article 101(1) in the territory of a Member State, or in a part thereof, which has all the characteristics of a distinct geographic market.