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The American
Antitrust Institute

RESPONSE TO PUBLIC CONSULTATION

ON THE

EUROPEAN COMMISSION

DIRECTORATE-GENERAL FOR COMPETITION

DISCUSSION PAPER ON THE APPLICATION

OF ARTICLE 82 OF THE TREATY TO ECLUSIONARY ABUSES

SUBMITTED BY

THE AMERICAN ANTITRUST INSTITUTE

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INTRODUCTION

The American Antitrust Institute ("AAI") is a Washington, D.C.-based independent non-profit education, research, and advocacy organization dedicated to the continued vitality of the antitrust laws in the United States and around the world. The AAI's advisory board includes scholars, attorneys, former enforcement officials, and business professionals. The Institute's homepage, at www.antitrustinstitute.org, describes the AAI's activities in detail.

The AAI welcomes this opportunity to consult with the Directorate-General for Competition on the December 2005 discussion paper on the application of Article 82 of the Treaty to exclusionary abuses ("discussion paper"). The leadership and staff of D-G Comp are to be complimented for a thoughtful analysis of a topic of concern to a significant part of the antitrust community. In many ways, the appropriate antitrust treatment of exclusionary abuses presents a greater challenge than any other area of competition policy. The reasons for this are recognized in the discussion paper's acknowledgement that not only low prices and high quality but also variety and innovation are legitimate values worthy of protection and promotion under the competition laws.[1] Recent economic research recognizes that dynamic competition along variety and innovation dimensions can be as important—or perhaps even more so—than static competition on the plane of prices and output. However, anticompetitive conduct that impairs dynamic economic processes affecting product variety and the pace and depth of innovation is considerably more difficult to detect and deter. Nonetheless, the AAI is greatly encouraged by the willingness of D-G Comp to tackle such issues, and in particular to examine the appropriate role of competition policy with respect to dynamic exclusionary strategies affecting potential entrants, rivals with lesser scale or scope, and participants in complementary lines of commerce and "aftermarkets."

The discussion paper and follow-on public consultation are occurring at a propitious time. In the U.S., the Presidentially-appointed Antitrust Modernization Commission is completing a series of hearings in preparation for a report on all facets of the U.S. antitrust laws. In addition, the U.S. enforcement agencies, the Antitrust Division of the Department of Justice and the Federal Trade Commission, are expected to announce joint hearings in the near future that focus on Section 2 of the Sherman Antitrust Act, the provision directed at monopolization and single-firm conduct. It is vital that these reexaminations aimed at clarifying the objectives and the mission of competition law occur with an adequate institutional understanding of the trends and proclivities of enforcement officials in the European Union. Undoubtedly, D-G Comp's discussion paper and public consultation will shed substantial light on the modern development and direction of EU competition law in the area of exclusionary abuses and in so doing highlight the extent of global harmonization or the divergence of perspectives in this commercially vital area.

The timing of the release of the discussion paper and this public consultation is also significant because it occurs after several decades during which U.S. antitrust doctrine has been moving toward a far less interventionist approach to the practices of dominant firms. Although as early as 1911 the U.S. Supreme Court in *Standard Oil Co. v. United States*[2] characterized certain

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[1] Discussion Paper at para. 4 (references to the discussion paper appear henceforth as "D.P.").
[2] 221 U.S. 1 (1911).

conduct as exclusionary, it was not until the middle of the Twentieth Century that interventionism in response to exclusionary conduct began its ascent. By the 1960s that activism had reached its zenith.[3] During this period, little or no weight was placed on efficiency justifications for practices of dominant firms with exclusionary effects.

The approach to exclusionary conduct in American doctrine changed dramatically, however, in the 1970s, when the influence of the "Chicago school" of economics gained traction, forcefully entering U.S antitrust jurisprudence in the Supreme Court's decision in *Continental T.V. Inc. v. GTE Sylvania Inc.*,[4] which held that vertically imposed dealer territories should not be condemned as *per se* unlawful. Since then the clear trend in the courts and enforcement agencies has been toward less intervention and in favor of a wider scope within which large enterprises may determine their business practices. The judicial decisions that marked the ascendancy of modern activism have lost their persuasiveness for with an increasingly conservative judiciary.

Nearly thirty years after the decision in *GTE Sylvania*, however, it is now legitimate to question whether the non-interventionist trend in U.S. antitrust policy inspired by Chicago school economics has gone too far. One fundamental tenant of the Chicago school of antitrust analysis is that, most of the time and in most industries, "one may treat observed prices and quantities as good approximations to their long-run competitive equilibrium values."[5] However, the current consensus among economists rejects this view, both as a premise for the analysis of market performance and as the basis of antitrust and competition policy. The evolution of economic thinking, in turn, leads to a series of practical questions about how U.S. antitrust policy is implemented. For example, has too much weight been placed on the claimed efficiencies put forward to justify conduct that has or is likely to have exclusionary effects? Does the current view exaggerate the danger of false-positives in antitrust prosecutions or the likelihood that greater activism may squelch competition and innovation? Does current policy undervalue the competence of antitrust courts and enforcement institutions to meet the sometimes difficult challenges of fashioning and administrating efficient remedies? Many well-recognized antitrust scholars, commentators, and enforcement officials are increasingly concerned that American non-interventionism has reached beyond the point at which non-interventionist antitrust doctrine and enforcement policies are optimal.

To be sure, in important respects, the U.S. antitrust laws still circumscribe exclusionary conduct by dominant firms. But the circumscription that now exists has been limited and is under continuing assault. The timing of the Article 82 discussion paper and this public consultation, therefore, is propitious because this process can contribute meaningfully to the development of the economic case in favor of a global competition policy regime that achieves a better balance

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[3] *See* William E. Kovacic and Carl Shapiro, "Antitrust Policy: A Century of Economic and Legal Thinking," 14 J.ECON.PERS. 43 (2000), identifying the trajectory of the ascendancy of the interventionist approach to exclusionary conduct through U.S. v. Aluminum Co. of America, 148 F.2d 416 (2nd Cir., 1945) (preemptive addition of capacity unlawfully exclusionary), U.S. v. United Shoe Machinery, 110 F. Supp 295 (D. Mass, 1953) *aff'd per curiam*, 330 U.S. 806 (1954) (leasing-only policy for shoe-making machinery unlawfully exclusionary), and Utah Pie Co. v. Continental Baking Co., 386 U.S. 685 (1967) (localized price cutting to challenge the leading local rivals unlawful).
[4] 433 U.S. 36 (1977).
[5] Melvin W. Reder, "Chicago Economics: Permanence and Change," 20 J.ECON.PERS. 1, 12 (1982).

between the concern for efficiency and the mitigation of anticompetitive conduct by firms with significant market power.

Before proceeding to comments directed at principal sections of the discussion paper, it bears mentioning that the AAI is encouraged by the increased emphasis on economic effects rather than particular forms of conduct that is reflected in the discussion paper. While both formalistic and effects-based analysis can and do rely on underlying economic policies, the latter can be significantly more productive in the area of exclusionary abuses. This is both because of the innumerably many varieties of conduct that can lead to potentially exclusionary effects and also because of the critical role of market context in determining whether a particular strategy is likely to have anticompetitive effects. Over-reliance on forms of conduct can degenerate into what one former U.S. enforcement official has called the search for a holy grail that never will be found and may inappropriately de-emphasize the all-important industrial context in which a particular strategy is attempted.

These themes—the unique analytical challenges presented by exclusionary abuses, the timing of this exercise as it relates to developments in the U.S. and elsewhere, and the appropriate emphasis of competition policy in this area on market effects, economic analysis, and the commercial context of particular cases—are reflected throughout the following comments.

1. MARKET DEFINITION

With respect to defining the relevant markets in the context of evaluating a suspected exclusionary abuse, the discussion paper ventures beyond the Commission Notice on the definition of the relevant market[6] only with regard to the application of the SSNIP test. As the discussion paper recognizes, applying the SSNIP test in a market in which prices may have already reached supra-competitive levels can lead to an overly broad market definition, *i.e.*, the so-called "cellophane fallacy." As a result, the SSNIP test is significantly more useful in connection with the evaluation of the likely competitive effects of a proposed merger than it is in arriving at the appropriate market definition for an investigation of an exclusionary abuse the effects of which may have already occurred.[7] This is principally because merger analysis requires a *prospective* analysis as compared to the usually *retrospective* analysis in cases of suspected exclusionary abuse. However, this need not be the case, as where attempted monopolization is involved, in which case the prevailing price level may provide an appropriate baseline. As recognized in the discussion paper, this corresponds to the Article 82 case in which no dominant firm has yet emerged, in which case "there may be no reason to suspect that the prices in that market are already above competitive levels."[8]

The central issue is whether the investigator knows whether the effect of the suspected exclusion has already manifested itself in the price-quantity dimension. However, such knowledge is not likely to be verifiable at the initial stages of an investigation. In the merger context the fact that the transaction is executory at the time of the analysis may recommend the

[6] OJ 1997 C372/5.
[7] D.P. at para. 15.
[8] D.P. at para. 17.

SSNIP test as a suitable criterion by which to define the relevant market. However, unless it is known with certainty that suspected exclusionary conduct has *not* affected prevailing prices, the SSNIP test is likely to be misleading. Accordingly, in exclusionary abuse cases alternative evidence of market definition should be relied upon.

A slightly more subtle inadequacy of the SSNIP test is pointed out by Krattenmaker, Lande & Salop,[9] who stress the distinction between market power exercised by a firm for the purpose of controlling price by limiting its own output and market power exercised by a firm for the purpose of excluding competition and thereby restraining market output. The SSNIP test is narrowly focused on market power exercised in the former, price-control sense rather than in the latter, competition-excluding sense. As Krattenmaker *et al*. point out, even if a firm's pricing is constrained by producers of substitutes, it may still be able to exercise exclusionary market power.

Two modifications have been suggested to adapt the SSNIP to cases of suspected exclusionary abuse.[10] The first is to enlarge the test to include an evaluation of the effects of the suspect conduct on rivals' input costs in addition to the effects of these costs on output prices in the market in which the firms compete. So modified, the analysis comprises much more than an initial task of defining the relevant market. It becomes central to the substantive merits of the claim itself. This is not surprising because it is characteristic of exclusionary conduct that its effects can alter the definition of the relevant market.

A second proposed modification applies when firms can be identified that have exited the market as a result of the claimed exclusion. An SSN*D*P test asks whether the preservation of the excluded competitors would have contributed sufficient additional output to lead to a small but significant nontransitory *decrease* in prices.[11] If so, the defendant can be said to have market power that it exercised with exclusionary effect.

2. DOMINANCE

Much has been made of the difference in terminology between the prohibition against the abuse of a dominant position contained in Article 82 and the rule against monopolization, or attempts to monopolize, found in Section 2 of the Sherman Act of 1890. Some commentators suggest that the concept of dominance—the power of a firm to behave independently of its competitors to an appreciable extent—involves meaningfully less market power than does monopoly—defined in U.S. jurisprudence as the power to raise price or exclude competition.[12] For example, while a market share of 50% or more would permit a presumption of dominance under Article 82, according to a recent statement of one U.S. enforcement official, the market

[9] Thomas G. Krattenmaker, Robert H. Lande, and Steven C. Salop, "Monopoly Power and market Power in Antitrust Law, 76 GEO.L.J. 241 (1987).
[10] *See id.*
[11] *See* Philip B. Nelson and Lawrence J. White, "Market Definition and the Identification of Market Power in Monopolization Cases: A Critique and a Proposal," NYU Center for Law & Business Working Paper No. CLB-03-022 (November 2003), available at: http://w4.stern.nyu.edu/emplibrary/03-022.pdf.
[12] United States v. E.I. duPont de Nemours & Co., 351 U.S. 377, 391 (1956).

share required to support a presumption of monopoly power might be as high as 70%.[13] However, as the discussion paper correctly recognizes, market share does not constitute direct evidence of market power, but a proxy, or circumstantial evidence.[14] Accordingly, the distinction between dominance and monopoly in the context of exclusionary conduct cases easily may be overstated.

Moreover, although the anticompetitive effect of the exclusionary conduct may be to raise prices above the competitive level, other potential anticompetitive effects are at least as important, such as the maintenance of a price level which, in the absence of the exclusionary conduct, would have fallen, the restriction of product variety and consumer choice, or the impairment of the process of innovation. The nexus between these other effects and dominance or monopoly power as measured by market share is less direct. That is, the relationship between concentration and the kind of market power needed to induce an exclusionary distortion in a market is less clear than with other types of abuse of dominance.

Moreover, in contrast to excessive pricing (which contrary to Article 82 is actionable under U.S. law only upon proof of collusion by separate firms, under Section 1 of the Sherman Act), exclusionary abuse ordinarily involves a dynamic strategy. As a result, the competitive harm resulting from exclusionary abuse is unlikely adequately to be demonstrable with the tools of comparative statics. The considerations in the discussion paper, therefore, of the extent and nature of barriers to entry, the capacity of firms to mount strategic responses to entry or expansion, or to invest in reputation-building, are central to the analysis of dominance in the context of suspected exclusionary abuse.[15]

Excessive pricing, however, should not be artificially de-coupled from the analysis of dominance as a pre-condition to exclusionary abuse. Examining profits or price-cost margins to determine whether pricing is excessive may be necessary to corroborate indicia of dominance and to make sense of current market conditions. Moreover, where an exclusionary abuse consists of product bundling, calculating a reasonable price for unbundled products may be necessary in connection with fashioning an appropriate remedy. Competition policy should not fail to consider excessive prices where doing so is a necessary element of the analysis.[16]

It is noteworthy that the discussion paper considers as potentially significant for the evaluation of dominance the position of buyers, an element not routinely emphasized in U.S. doctrine.[17] However, the discussion paper does not broach the issue of buyer power itself as a form of dominance. Because a much smaller share of total market purchases are required to produce substantial market power, an inquiry into the ways in which exclusionary abuses may be enabled and dealt with under Article 82 may be warranted.[18]

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[13] J. Bruce McDonald, Deputy Assistant Attorney General, Department of Justice Antitrust Division, "Section 2 and Article 82: Cowboys and Gentlemen," Speech before the College of Europe, Brussels, June 16-17, 2005, available at: http://www.usdoj.gov/atr/public/speeches/210873.htm.
[14] D.P. at para. 33.
[15] D.P. at paras. 39-40.
[16] *See* Eleanor M. Fox, "Monopolization and Dominance in the United States and the European Community, " 61 NOTRE DAME L. REV. 990 (1986).
[17] D.P. at paras. 41-42.
[18] *See generally* "AAI Symposium: Buyer Power and Antitrust," 72 ANTITRUST L. J. 505 (2005).

3. FRAMEWORK FOR THE ANALYSIS OF EXCLUSIONARY ABUSES

Aside from the express acknowledgement that the overall purpose of the competition laws is to protect "competition, and not competitors as such,"[19] which is also a fundamental tenant of U.S. competition law,[20] and the exclusion of "genuine competition" from the type of conduct proscribed by Article 82, the analytical framework presented in the discussion paper departs both in emphasis and in particulars from the current U.S. approach.

With respect to emphasis, the framework concerns itself with both short term as well as medium and long term harm from suspected exclusionary abuse.[21] This is significant and appears to account for the centrality of "foreclosure" as the essential element of competitive harm from the perspective of EU jurisprudence, whereas U.S. doctrine is more likely to require a showing of an actual or probable effect on price or output. Insofar as the U.S. approach may be overly lenient on exclusionary conduct with dynamic effects that may take some time to play themselves out, the broader concept of conduct that influences the structure of the market, particularly with "the capability, by its nature, to foreclose competitors from the market," appears to address a wider range of anticompetitive exclusionary behavior. However, while the willingness to examine medium and longer-term effects is to be commended, there should of course also be an awareness of the difficulty of long term prediction and the desirability of avoiding outright speculation, which may lead to the introduction of wholly subjective factors.

Emphasizing foreclosure effects instead of more narrowly focusing on price and output response allows for a number of useful additional considerations in the framework enunciated in the discussion paper that may not under current U.S. doctrine receive the attention they deserve. For example, the "form and nature of the conduct" is as critical to the investigation of foreclosure as the "specific market context" in which it occurs, including "network effects and economies of scale and scope."[22] Thus, conduct that is similar in "form and nature" may constitute exclusionary effect in one market context yet be entirely benign in another. The anticompetitive potential of, for instance, single branding contracts or refusals to deal depends almost entirely on the commercial context in which they occur.

Although the central role of the market and industrial context is acknowledged in individual U.S. judicial decisions, the recent U.S. policy debate has tended to concentrate on identifying an appropriate "standard" for the assessment of exclusionary conduct, such as the "profit sacrifice" test, the "no economic sense" test, the "less efficient rival" test, or the "balancing" test. The American tendency to focus on formulaic standards reflects the same attitudes that have contributed to the trend of non-interventionism: a desire to avoid ad hoc adjudication or enforcement, a lack of confidence that legal rules can be devised that avoid false positives, doubts about the ability of courts and government officials to fashion and administer efficient remedies, and the concern that competition policy promote rather than inhibit competition. Such reticence is not reflected in European jurisprudence (or in the discussion paper), and this imparts a healthy flexibility to the analysis of exclusionary abuse that may be

[19] D.P. at para. 54.
[20] *See* Brown Shoe Co. v. U.S., 370 U.S. 294, 320 (1962).
[21] D.P. at para. 55.
[22] D.P. at paras. 58-59.

lacking in current U.S. doctrine. Although price-based exclusionary abuses require foreclosure of a rival that is as efficient as the dominant firm, the discussion paper seems to recognize that determining whether such a condition has been met is not without its difficulties and, in any case, it is not intended to be a monolithic standard to be applied without regard to other important factors.

Requiring that any claimed efficiency benefit of conduct with an exclusionary effect must be passed on to consumers for the efficiency to be considered a defense constitutes an explicit endorsement of a consumer welfare rather than a total welfare standard.[23] In light of the variation in the U.S. judiciary on this point, such an endorsement represents a welcome modicum of certainty. Moreover, in recognition of the dynamic nature of exclusionary abuse, it is entirely appropriate that "the protection of rivalry and the competitive process is given priority over possible pro-competitive efficiency gains."[24]

4. PREDATORY PRICING

Under the rule devised in the most recent Supreme Court predatory pricing decision, *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp*.,[25] the defendant is required to have set prices below "some measure" of cost during a predatory period, followed by a period of probable recoupment. The discussion paper gives some useful guidance for determining which particular measure of costs may be appropriate in a given circumstance. However, any such test can at best lend only a veneer of objectivity to the determination of whether predation has taken place. The recognition in the discussion paper that actionable price predation may be established through the use of indirect evidence, and the enumeration of the elements that will contribute most to evaluating such evidence, offers more significant guidance for the evaluation of suspected predatory pricing.[26] Endorsement of this approach is a welcome acknowledgment that modern industrial organization economics does not consider the "profit sacrifice" definition as the only, or even most common, indicium of price predation.

The discussion paper requires a showing of objective evidence that the suspected pricing policy is "part of a strategy or plan to predate," a requirement that gives appropriate weight to the presence of "predatory intent."[27] Reliance on this type of intent evidence provides a useful counterbalance to the tendency of over reliance in this area on formulaic approaches. Moreover, the discussion paper recognizes that the *Brook Group* rule that requires the plaintiff to establish probable recoupment favors the suspected predator because it is not considered necessary to provide further separate proof of recoupment to find an abuse.[28] Upon a suitable showing that supports a presumption that the pricing conduct is predatory, shifting the burden to the defendant to show that recoupment would not be possible is a sensible alternative.

[23] D.P. at para. 88.
[24] D.P. at para. 91.
[25] 509 U.S. 209 (1993).
[26] D.P. at paras. 115-126.
[27] D.P. at para. 112.
[28] D.P. at para. 122.

Allowing for the possibility of a two-market predation strategy also represents a welcome enlargement of the *Brooke Group* standard.[29] Similarly, reputation-building predation that affects adjacent markets may also occur in several industries, but may not be reached under current U.S. doctrine.[30]

5. SINGLE BRANDING AND REBATES

The discussion paper operationalizes a general principle of Article 82 jurisprudence that a dominant firm may require single branding and offer rebates if these conditions are related to efficiencies but it may not do so for the purpose of ensuring customer loyalty or to disadvantage a competitor. Thus, the ultimate desideratum in single branding and rebate cases is the purpose for which the condition is imposed, making relevant any competent evidence that tends to illuminate the true purpose of the condition.

One immediate and beneficial result of the adoption of this principle is that conditions of trade inconsistent with efficiency-generating conduct may give rise to a rebuttable presumption of abuse. For example, the discussion paper specifies that single branding obligations that are so widespread as to affect "if not most, at least a substantial part of market demand"[31] are likely to lead the Commission to conclude that the obligations have a market distorting effect and thus constitute an abuse. Similarly, the discussion paper expresses a suspicion of "quantity forcing" discounts, *i.e.*, conditional rebates on all purchases where the threshold is set above the quantity the customer would ordinarily expect to purchase.[32] While a U.S. court in a particular case may recognize the anticompetitive potential of such conditions, such recognition is likely to be achieved only after overcoming a Chicago school perspective that assumes away most of the elements of the foreclosing dynamic. A U.S. court may assume initially that buyers are free to choose to deal with whomever they wish or that rivals that are already present or poised to enter will face little or no difficulty in supplying "commercially viable" quantities subject to discounts. As a result, the burden of establishing in a particular case that such assumptions do not hold—despite the defendant's established market power—usually falls to the plaintiff. To the extent this represents U.S. doctrine, it unfairly favors a dominant firm that is engaging in conduct that ordinarily has no efficiency justification, or is justified by efficiencies that can be achieved through less restrictive means.

Single branding obligations—or exclusive dealing arrangements—is an area in which at least one U.S. court has expressly recognized a special duty on the part of a dominant firm. In *U.S. v. Dentsply International, Inc.*[33] a U.S appellate court declared that "[b]ehavior that otherwise might comply with antitrust law may be impermissibly exclusionary when practiced by a monopolist."[34] At issue was a policy by the leading manufacturer of false teeth that its network of distributors and dental laboratories refrain from dealing in products manufactured by its rivals. Finding that "exclusive dealing arrangements can be an improper means of maintaining

[29] D.P. at para. 101.
[30] D.P. at para. 119.
[31] D.P. at para. 149.
[32] D.P. at para. 152.
[33] 399 F.3d 181 (3rd Cir., 2005).
[34] 399 F.3d at 187.

a monopoly,"[35] the court held that the policy had "a significant effect in preserving Dentsply's monopoly."[36] Finding the firm's proffered justifications for its policy pretextural, the court found that the exclusive dealing policy foreclosed competitors from a substantial portion of the available opportunities for product distribution. To the extent that the *Dentsply* decision represents current U.S. doctrine, both jurisdictions take a fairly similar approach to exclusive dealing.

With respect to quantity forcing discounts, both the specification of a commercially viable amount capable of being supplied by the class of existing or potential rivals and the attribution of the entire discount to this amount are noteworthy.[37] Specifying the commercially viable amount is critical to determining the foreclosure potential of the scheme. This metric sweeps conditions of entry, the output capacity of rivals and other features of the industry, such as the use of intellectual property licensing restrictions, into the foreclosure calculus. When the commercially viable output of its rivals is known, a dominant firm can tailor to each of its customers a rebate offer that virtually assures that the customer will make no additional purchases from the dominant firm's rivals. The central role played by the scale constraints facing the rival set is again indicative of the contextual sensitivity of rules of conduct that seek to identify exclusionary conduct.

This suggests a need for caution against over-reliance on predatory pricing formulations as the determinant of whether a quantity forcing discount constitutes abuse by a dominant firm. Attribution of the entire discount to the incremental units is, of course, a pre-condition to the employment of a predatory pricing approach. But even where this is assured, an inappropriate cost measure or unsuitable period over which the costs are measured can result in finding above-cost pricing in spite of a substantial foreclosure effect. In this regard the discussion paper recognizes that when a dominant firm enjoys "non-replicable advantages" the rebate scheme where the effective price is above cost may nonetheless entail abuse.[38] Although such "non-replicable advantages" were not precisely defined, unique advantages possessed by a dominant firm may occur on a competitively significant scale more frequently than the discussion paper suggests. Thus, where a quantity-forcing rebate scheme involves an effective price that exceeds the appropriately chosen measure of cost, an inquiry into whether such advantages are enjoyed by the dominant firm, or whether other market conditions enable the rebate scheme to foreclose entry or expansion, should follow as a matter of course. In any event, suspicion of quantity-forcing rebate schemes in market conditions in which foreclosure effects are likely as expressed in the discussion paper is a commendable approach which departs from current U.S. doctrine that entails a micro-theoretic albeit rebuttable presumption that such schemes are pro-competitive.

6. TYING AND BUNDLING

The discussion paper interprets the prohibition against tying in Article 82(d) to require four elements: dominance in the tying market, two distinct products, a likely market distorting effect (in either the tying or the tied market), and the lack of any objective justification or

[35] *Id.*
[36] 399 F.3d at 191.
[37] D.P. at para 154.
[38] D.P. at para. 165.

efficiency.[39] This departs from U.S jurisprudence in several respects. First, the standard applicable to tying under U.S. law is approaching the requirements for attempt, where the defendant has a "dangerous probability of actual monopolization."[40] Thus, despite the per se status of tying under U.S. law, which means that no actual effect need be shown once the elements of the offense have been established, tying will ordinarily not be challenged by enforcers unless a severe anticompetitive outcome in the tied market is apparent. By contrast, the discussion paper suggests no comparable requirement of dominance, or near-dominance, in the tied market, but merely a "market foreclosing distorting effect."[41] This hews much closer to earlier U.S. concepts of tying, in which a monopolist is able to "leverage" its market power in one market to obtain an unfair competitive advantage in another. Such leverage theories have been severely undermined by the "one monopoly rent" principle. However, post-Chicago scholarship indicates that leverage theory may be more valid than the one monopoly principle might suggest. To the extent the discussion paper admits of the use of tying for the purpose of monopoly leveraging, it represents a more inclusive approach to the analysis of anticompetitive harm that can flow from the practice of tying.

Another effect of tying that may also confront considerable doubt in current U.S. doctrine is the use of the practice by a firm that is dominant in the tying market to maintain its position.[42] Maintenance of existing dominance is the primary method by which exclusionary conduct may exercise an anticompetitive effect. Accordingly, a rebuttable presumption of abuse where a dominant firm ties a sufficient part of the market is appropriate, provided that the elements enumerated for the assessment of a particular instance of tying are satisfied, and not "applied in a mechanical way."[43]

With respect to bundled discounts, the discussion paper sets forth the proposition that foreclosure occurs "if the discount is so large that efficient competitors offering only some but not all of the components, cannot compete against the discounted bundle."[44] Although no comparable general principle exists under U.S. doctrine, at least one U.S. court (the same appellate court that issued the *Dentsply* opinion) has ruled against a dominant firm offering a multiproduct discount on the grounds that its policy "may foreclose portions of the market to a potential competitor who does not manufacture an equally diverse group of products and who therefore cannot make a comparable offer."[45]

The key insight of *LePage's* and of the approach taken in the discussion paper is the analysis of bundling arrangements under a tying approach rather than under a predatory pricing approach. Product bundling has the potential to affect demand cross-elasticity by affecting the product market definition in a way that pricing policy cannot. Moreover, dominance that involves efficiencies of scope may be directly exploitable through bundling in a manner that is not possible through a strategy of predatory pricing. Finally, tying and bundling may both attain exclusionary results by obscuring important pricing information which does not occur with

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[39] D.P. at para. 183.
[40] Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 455 (1993).
[41] *Id.*
[42] D.P. at para. 181.
[43] D.P. at para. 188.
[44] D.P. at para. 189.
[45] LePage's Incorporated v. 3M, 324 F.3d 141, 155 (3rd Cir., 2003).

predatory pricing. Thus, while the *LePage's* decision has come under criticism in the U.S., even some conservative commentators recognize that by combining multiple products that occupy distinct markets there is wider scope for anticompetitive effects than in cases concerning only individual product market definitions.

7. REFUSALS TO SUPPLY

Refusals to supply as a violation of Section 2 of the Sherman Act recently has been a lively area of debate in the U.S. Although the treatment of such conduct under Article 82 that is described in the discussion paper proceeds from the same initial position as does U.S. doctrine, *i.e.*, that firms "are generally entitled to determine whom to supply and to decide not to continue to supply…,"[46] the jurisdictions appear to diverge sharply over the likelihood and frequency of exceptions to this general rule. As in other areas of exclusionary conduct, the current American enforcement norms are biased toward non-interventionism, seemingly motivated by the desire to avoid over-deterrence or to create disincentives for investment. There is also the concern that courts are ill-equipped to design and implement terms of compelled trade. This was the case in the recent Supreme Court decision in *Verizon Communications, Inc. v. Law Offices of Curtis Trinko, LLP*, 540 U.S. 398 (2004), in which the Court found that a Section 2 claim against an incumbent local carrier for its delay or refusal to deal with a competitive local carrier that sought interconnection under a compulsory access provision of U.S. telecommunications law was not actionable. The Court was particularly concerned with the effect of letting the suit proceed on the investment decisions of dominant or putatively dominant firms that might face antitrust-based compulsory dealing in other, similar contexts.

By contrast, the discussion paper brings a greater balance to the issue of the investment disincentive effect of duty to deal regimes in its concern for both the short run investment disincentive effect of imposing a duty to deal on a dominant or would-be dominant firm and the medium or long run effect on smaller rivals that might be disinclined to invest in follow-on infrastructure or innovation where they risk losing access to a necessary input.[47]

More generally, the recognition that a special risk of exclusionary conduct arises when the customers of a dominant firm are also its rivals has no counterpart in U.S. doctrine, despite the fact that there exist in such circumstances particularly attractive opportunities for dominant firms to profit from exclusionary refusals to deal.[48] Such attention is particularly appropriate in communications and information technology industries where often *de facto* standards and proprietary interfaces controlled by dominant entities must be practiced to compete. However, the perspective that innovation is monotonically increasing in the strength of intellectually property rights tends to undermine U.S. antitrust enforcement in this area. The discussion paper appropriately accepts that certain features of one or more markets may lead to circumstances in which the promotion of innovation can be achieved through a regime of compulsory access based on competition law, provided such an obligation is established "only after a very close scrutiny of the factual and economic context…."[49]

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[46] D.P. at para. 207.
[47] D.P. at para. 213.
[48] D.P. at para. 209.
[49] D.P. at para. 214.

The U.S. doctrine in this area is also characterized by a substantial degree of skepticism about the ability of courts to set appropriate terms of trade for compulsory access. Clearly, where there is a discontinuation of a preexisting course of dealing these concerns are greatly ameliorated, both as to the efficiency of creating a duty to deal in a particular product and the terms on which such dealing ought to occur, as reflected in the discussion paper[50] and in the decision in *Aspen Skiing Co. v. Aspen Highlands Skiing Corp*.[51] Clearly, the more challenging case involves the claim that a dominant firm has a competition law-based duty to commence dealing, as arguably was the case in *Trinko*.

The conditions under which such a duty might arise under Article 82 closely resemble the so-called "essential facilities" doctrine under U.S. law.[52] Views on whether such a doctrine survives in the U.S. are mixed. On the other hand, every federal judicial Circuit has recognized the essential facilities doctrine in some context, and even the Supreme Court in *Trinko* declined to repudiate it. There can be little question, however, that essentiality is—and indeed, ought to be—the keystone of any such offense, corresponding to the "indispensability" element of this doctrine under Article 82 as interpreted in the discussion paper. It is no surprise, therefore, that the leading essential facilities case in U.S. jurisprudence, *Otter Tail Power Co. v. United States*,[53] arose in the context of a regulated utility. When products (*i.e.*, inputs) exhibit utility-like characteristics, for example because they are "physically or legally impossible to duplicate,"[54] the balance of investment disincentives is likely to favor compelled access to output-expanding rivals and the terms of trade are more likely to be determined by analogy with similar circumstances. By strictly interpreting the essentiality or indispensability requirement, a doctrine of access to an indispensable facility is not likely to apply outside the context of at least "utility-like" products, with one important exception.

The important exception implicates intellectual property rights, particularly in the area of interoperability standards, including standards that have been adopted by formal standard setting organizations and those chosen by the market as the *de facto* standard. In either case, the control of an interface necessary for interoperability can imbue an enterprise with dominance over an entire range of adjacent markets and, occasionally, over an entire industry. Often, the intellectual property right that is raised as the authority for retaining this type of clustered, multi-market dominance protects obvious, non-inventive, or arbitrarily chosen technology or protocols. On occasion, a formal standard setting body unwittingly selects a standard burdened by a proprietary interest. In these cases, the exercise of the intellectual property right can easily introduce market distorting foreclosure and anticompetitive effects that far outweigh the inventive contribution of the covered product or interface, and competition policy should provide the mechanism by which to reign in such out-sized economic effects.

Although the specific context of standard setting is not addressed in the discussion paper, a refusal to license by the owner of an intellectual property right that "prevents the development

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[50] D.P. at para.

[51]472 U.S. 585 (1985).

[52] D.P. at § 9.2.2.

[53] 410 U.S. 366 (1978).

[54] D.P. at para. 229.

of the market for which the license is an indispensable input"[55] may constitute an abuse and thereby provide sufficient authority to remedy a hold-up problem or the exclusionary use of an industrial standard encumbered by intellectual property rights. Moreover, the discussion paper appropriately suggests that dominance extended to additional markets by a refusal to supply even trade secret information for digital protocols and similar interfaces may also constitute abuse giving rise to remedial compelled disclosure.[56] These approaches are vitally important to ameliorate economic distortions as the dual trend continues toward stronger intellectual property rights and increasing digitization, where technological interfaces are extremely fragile.

8. AFTERMARKETS

The discussion paper embarks on important territory in its section on aftermarkets. In the U.S., the decision in *Eastman Kodak Co. v. Image Technical Services, Inc.*[57] is standard authority for the proposition that a refusal to deal that facilitates installed base opportunism in the presence of informational asymmetries and consumer lock-in can lead to liability under Section 2. In practice, however, the *Kodak* case has been largely ignored by the lower courts. Moreover, antitrust doctrine in the U.S. tends to compartmentalize individual offenses rather than examine the slightly larger scale necessary to group disparate types of exclusionary conduct together into an inclusive analysis of aftermarkets, or to include intellectual property law as part of the competitive problem.

However, for several reasons a coherent competition policy toward aftermarkets has become increasingly necessary. First, from a marketing perspective, most firms strive toward systemization. Firms are eager to convert single sale-of-goods transactions into repeated sale-of-service transactions. This is often accomplished through systemization. Thus, an automobile purchaser does not purchase an automobile, but a transportation system that delivers a flow of services over several years and includes in the purchase price the cost of repairs, maintenance, financing, and perhaps even insurance. The purchaser of a portable digital music device does not purchase a device but a flow of services in the form of downloadable music available only from a website sponsored by the device manufacturer. The purchaser of a printer purchases a flow of printing services that uses ink cartridges available only from the printer manufacturer. The purchaser of software purchases a flow of upgrades delivered over time on a subscription basis. The list is lengthy and not limited to technological interfaces. For example, the bank customer finds it more convenient and more economical to place share brokerage and retirement accounts with the same bank that provides checking account services and a line of credit. The telephone subscriber finds it much easier to purchase broadband services or video delivery service from the telephone company than to contract with additional parties. These trends are all examples of systemization and firms are becoming increasingly adept at tightening the binds between the product in the primary market and the products required to deliver a flow of services in a secondary market.

In addition, digitization permits systemization in ways that were not possible only a few years ago. Whenever interfaces depend on digital protocols, primary market participants have an

[55] D.P. at para. 239.
[56] D.P. at para. 241.
[57] 504 U.S. 451 (1992).

effective ability to lock-out rivals producing complementary products. Recent judicial developments in the U.S. indicate that copyright law may have built-in limitations on the use of copyright to protect lock-out codes. However, no such self-limitation has emerged out of the patent law. In any event, the harm stems from a distortion of the competitive process and is most appropriately dealt with through competition policy.

The use of intellectual property in ways that strengthen the binds between the primary and secondary markets presently have no little or no competition law counterweight where consumers are injured from a lack of interoperability or the ability to "mix-and-match." A naked claim by a primary market producer that customers desire "one stop shopping" should not be accepted absent a showing of real efficiencies that are actually passed on to final consumers. Most customers desire the freedom to choose, and they should not be required to sacrifice choice if they are getting nothing in return.

There is a tendency—to some extent also exhibited in the discussion paper—to believe that "systems competition" can sufficiently constrain the dominant firm and mitigate the market distorting foreclosure effects that follow from aftermarket exclusivity.[58] Such claims should be viewed with skepticism. By their nature, systems rarely permit costless switching. When switching is costly, the presence of multiple systems exerts little or no competitive constraint. Moreover, some system operators—such as wireless telephony carriers—offer bundled devices and subscription services at favorable prices, yet they severely penalize switching during a sometimes lengthy initial contract. Similarly, informational transparency is rarely available to consumers choosing between systems, and when it is, life-cycle evaluation of costs is itself costly and time consuming.

Clearly, competition law in this area must be mindful of the possibility that systemization may offer consumers legitimate benefits or produce efficiency gains that are actually passed on to end users. But the burden on the part of the dominant firm with exclusionary policies in a secondary market should be high. Systemization itself rarely requires exclusivity or non-interoperability. The ability to mix-and-match is an unambiguous consumer benefit. A dominant firm that prevents the exercise of consumer sovereignty by limiting consumer choice should meet a strict burden to justify its policies.

9. CONCLUSION

The discussion paper strikes an excellent balance between the need for administrable legal rules and the benefits of a competition law regime informed by modern economic learning. In particular, the introduction of efficiencies, while necessary, is not permitted to overshadow the principle objective of evaluating exclusionary context with due regard for the context in which it takes place. In a similar vein, the discussion paper reveals a commendable willingness to look beyond short term price and output effects to try to understand the competitive effect of an exclusionary strategy as a dynamic process, and to eschew the mechanical application of formulaic rules. The discussion paper does much to forward the cause of a rational, global competition law regime.

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[58] *E.g.*, D.P. at para. 247.