

The Journey Towards an Effects-based approach under  
Article 101

Modernisation and Hardcore Restraints

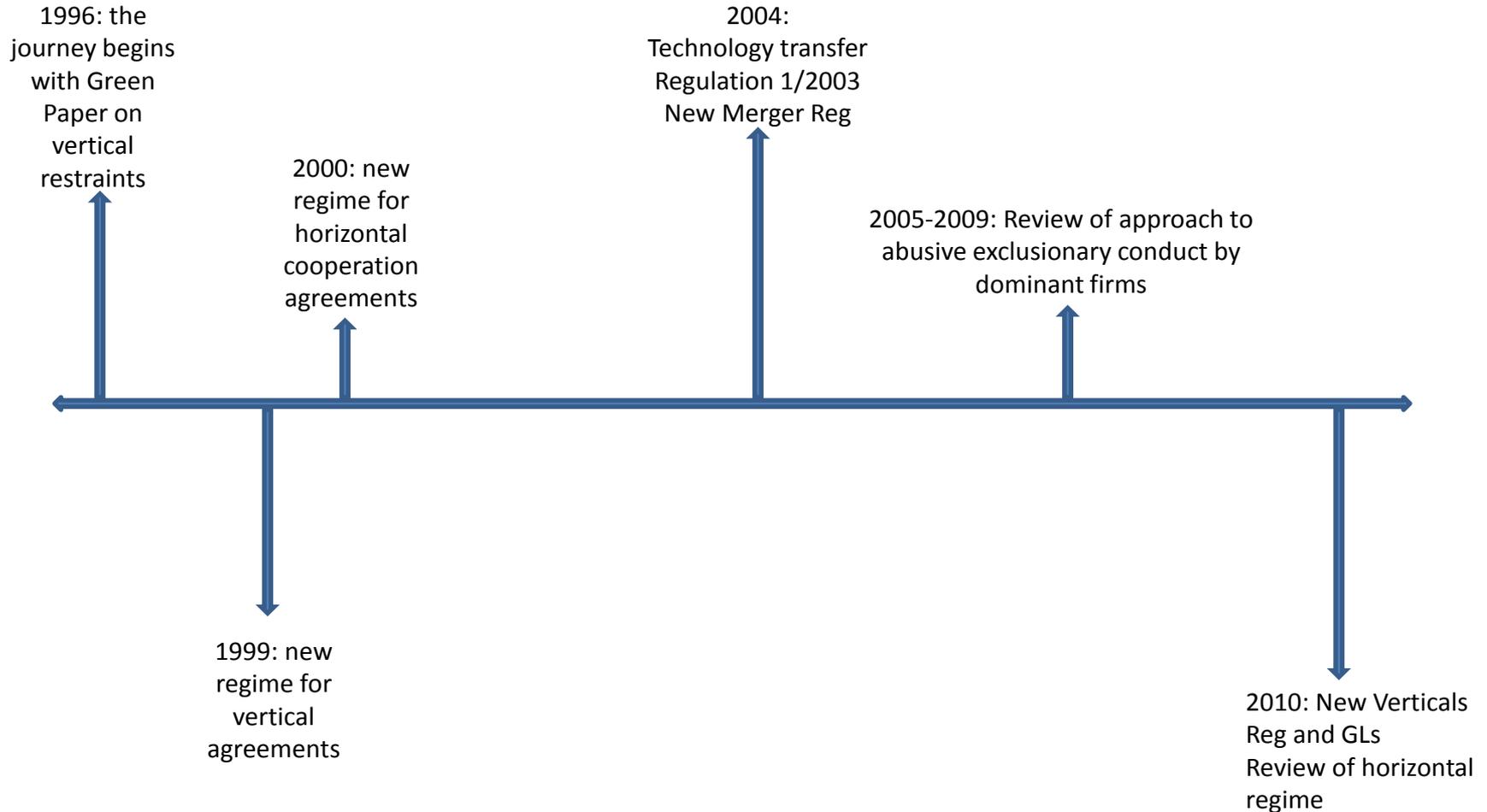
Alison Jones

# The EU Modernisation Process

A shift from rules based on form  
to ones focused on the  
economic effects of the conduct  
at issue

To reinforce the Commission's  
growing view that the central  
goal of the EU competition rules  
should be the protection of  
competition on the market as a  
means of enhancing consumer  
welfare

# The Modernisation Process



# Why was Modernisation necessary?

Difficulties in EU entangled both with bifurcation of substantive analysis under Art 101 and enforcement structure set up in 1962 (Reg 17)

Agreements 'restricting competition' (Art 101(1)) could benefit from Art 101(3) only if they were specifically 'exempted' from Art 101(1) prohibition

- either an *individual exemption* granted by the Commission, or
- a *block exemption*, granted by EU regulation to certain categories of agreement (mainly Commission regs)

# Core Criticism

A broad view of a restriction of competition (anaemic economic analysis)

Virtual impossibility of obtaining an individual exemption (NCAs and national courts could not apply)

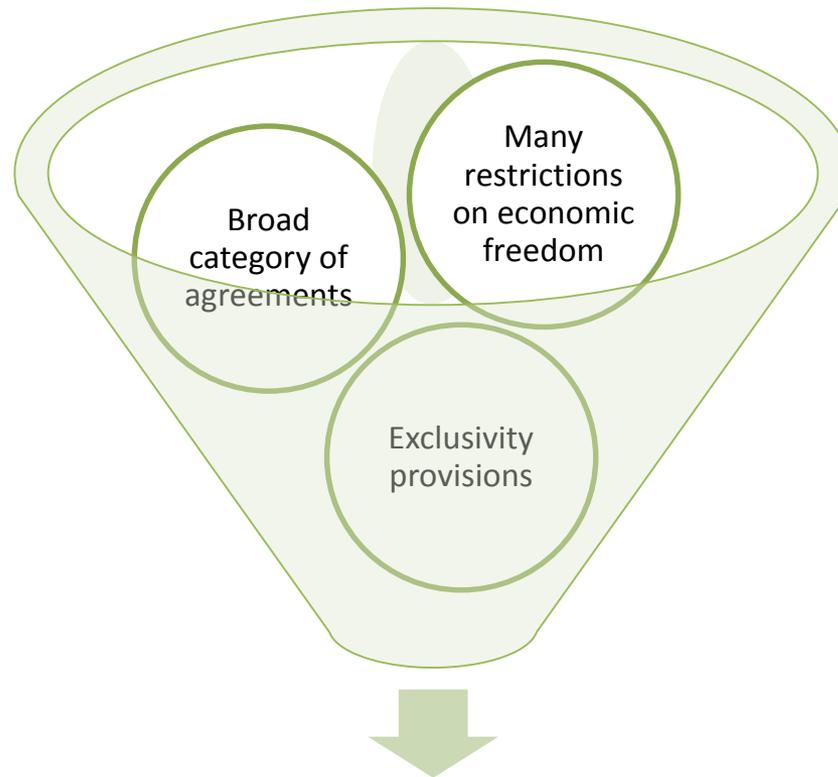
Block exemptions – straight-jacketing effect

Treatment of agreement by category/ form not by effect

Stultifying innovative and procompetitive distribution agreements

System failure (Barry Hawk)!

Too many agreements were being sucked within Article 101(1) and forced into a straightjacket to satisfy Article 101(3) – treatment of agreements by category



Art 101(3) (exclusive competence of Commission)

Rigid BERs: Franchising; Exclusive Distribution; Exclusive Purchasing; or Motor Vehicles

# Reform of Approach to Vertical Agreements – generally welcomed

1999

- Broader, more flexible BER
- Further, accepted that even agreements not within BER:
  - may not violate Article 101(1) or
  - may satisfy Article 101(3) criteria

2004

- Abolition of Exemption Process (possibility of non-infringement decisions – informal guidance)
- Article 101(3) Guidelines: analytical framework for agreements
  - narrower view of what constitutes a restriction of competition but, correspondingly,
  - narrower interpretation of Article 101(3) criteria

# Remaining problems?

## Constructed framework

Are objectives of EU competition laws as clear cut as guidelines suggest (see eg ECJ in *GlaxoSmithKline*)?

Is guidance on assessment required under Art 101(1) and (3) respectively compatible with the case law?

If more economic approach (especially under Art 101(1)) - why is overarching BER needed?

# Remaining problems

## ‘Hardcore’ restraints – *no* change in approach?

Automatically violate Article 101(1) – have as its object the appreciable restriction of competition

Presumed not to satisfy the conditions of Article 101(3) (individually and BER do not apply)

Likely to attract a significant fine if uncovered by the Commission or NCA

Modernisation exacerbated problems – narrower role and greater uncertainty over the scope of Art 101(3)?

# Hardcore restraints – those which have as their *object* the restriction of competition

## Agreements between competitors

- To fix prices, limit output or share markets (*ENS*)
- To reduce capacity (*BIDS*)

## Information exchanges between competitors

- Designed to fix purchase/selling prices (*T-Mobile*)

## Agreements between non-competitors

- Conferring ATP or otherwise prohibiting or limiting parallel trade (*Consten & Grundig/GlaxoSmithKline*)
- Imposing fixed or minimum resale prices (RPM) (*Binon*)

# Commission's view

## Object restraints

### Appreciably restrict competition

- Notice on agreements of minor importance specifically excludes agreements between non-competitors which impose fixed or minimum sale prices on buyers

### Most unlikely to satisfy the conditions of Art 101(3) (Art 101(3) GLs and 1999 Vertical GLs)

- Verticals BER does not apply
- 'Tightening' of Art 101(3) criteria – unlikely
  - to create objective economic benefits,
  - to benefit consumers and/or
  - to be indispensable to attainment of any efficiencies created by agreement (efficiencies could be achieved by less restrictive means)
- Less certainty – no Art 101(3) decisions
- Harder to rebut presumption that do not satisfy Art 101(3) conditions?

# What is wrong with this position?

Most competition law systems accept that clear, administrable bright line rules against obviously anti-competitive conduct are justifiable

- Eradicates the need to prove, at cost, the adverse consequences of such conduct.

## Best practice

- Rules drawn on the basis of accepted economic principles
- Yields minimal costs from false positives

# But ...

EU list of hardcore restraints broad similar to those illegal per se in US at end of 1960s– since then Sup Ct

- Rethought per se category (narrowed and confined to conduct having manifestly anticompetitive effects and lacking in redeeming features – essentially horizontal cartel activity) (see e.g. *Dr Miles/ Schwinn*  *Sylvania/ Leegin*)
- Held that even severe restraints should be analysed under rule of reason where a quick look establishes that the restraint might be ancillary or reasonably necessary to achieve plausible efficiencies in an efficiency enhancing integration (*BMI*)

## Complaint in the EU

- Category of 'hardcore' restraints drawn too broadly?
- Category insufficiently redefined or refined (as it has been in US)?
- Hardcore restraints treated more rigidly than the elements of Article 101 require (especially Article 101(3))

## Indeed one issue in debate preceding new Verticals block exemption regulation and Guidelines in 2010:

- Did EU regime treat hardcore vertical restraints too formalistically (especially RPM – following *Leegin*)?
- Should there be greater willingness to assess their potential procompetitive effects within the Article 101 framework.

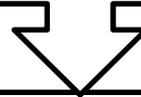
# Latest review

2009-2010

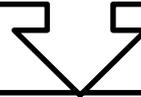
- Review of working of verticals regimes
- Changes – to provide further guidance where necessary to reflect
  - market developments
  - developments in economic thinking or
  - an ex post assessment of impact that rules have had on market

# How could change happen?

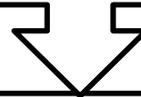
Reconsideration or refinement of object category



Acceptance that restraints between small players might not appreciably restrict competition



Reconsideration of BER?



Greater willing to accept that restraints might be indispensable to achieve efficiency in distribution the benefits of which would be passed on to consumers (Commission)

# Reconsideration of object category?

Should the EU Courts be willing to reconsider previous rulings and modernise its view on what constitutes a restriction by object?

- Less willing to discuss policy and principles underlying rules
- Rarely departs from previous rulings
- Broader objectives (including single market)
- Supreme Court's opinion in *Leegin* controversial – was it right decision (see Justice Breyer)?
- Not such a pressing need as object restraints can be justified under Art 101(3)(?) (theoretically at least)

Refinement: how is it determined whether an agreement has as its *object* the restriction of competition?

To determine whether conduct is by its *very nature* injurious to competition (restrictive by object) 'regard must be had inter alia to ***the content*** of its provisions, the ***objectives*** it seeks to attain and the ***economic and legal context*** of which it forms part', (emphasis added)

*GlaxoSmithKline/ IAZ/BIDS*

# Refining the Category

Object classification may not be justified if it is plain from the overall context in which the hardcore restraint operates that is objectively necessary for agreement's operation

*Wouters*

*Coditel (II)* (but contrast e.g., *Consten&Grundig*)

ATP imposed for two years where substantial investment nec to start up/ develop new market, 2010 Vertical GLs, para 60-1

Does this mean that abridged economic analysis required even in object cases?

*GlaxoSmithKline*, General Court

- Cannot determine whether restrictive objective simply by relying on clauses of agreement without reference to legal and economic context
- Must take account of peculiar features of pharmaceutical sector and that parallel trade might benefit only intermediaries and not consumers
- 'In this largely unprecedented situation, it cannot be inferred merely from a reading of the terms of that agreement, in its context that the agreement is restrictive of competition, and it is therefore necessary to consider the effects of the agreement' (para 138)

Does this mean that abridged economic analysis required even in object cases?

### GlaxoSmithKline, ECJ

- In principle an agreement aimed to prohibit or limit parallel trade has as its object the prevention of competition – principle applied in pharmaceutical sector
- Rule did not only apply in so far as it could be presumed that restriction would deprive final consumers of advantages of effective competition in terms of supply price
- Agreement tending to restore national divisions in trade between member states might be such as to frustrate single market objective

# No per se illegality

Even object/hardcore restraints may escape prohibition of Article 101(1) if:

- No appreciable restriction of competition
- Satisfy the Article 101(3) conditions

# No appreciable restriction of competition?

RPM or ATP by supplier with very small market shares

- *Volk v Vervaecke*
- Commission Notice on Agreements of Minor Importance n/a to agreements containing hardcore restraints but does not affect legal position (but creates uncertainty)
- Might the Commission be rethinking this notice?

# Satisfying the Art 101(3) conditions?

An object restraint will escape condemnation under Article 101(1) if it can be established, by means of convincing arguments and evidence, that all four cumulative conditions of Article 101(3) are satisfied - that is it:

contributes to improving the production or distribution of the goods in question, or to promoting technical or economic progress;

allows consumers a fair share of the resulting benefit;

does not impose on the participating undertakings any restrictions which are not indispensable; and

does not afford the parties the possibility of eliminating competition in respect of a substantial part of the products in question

# Possible change under recent Verticals review? Changes to Vertical BER?

Removal of list of hardcore restraints would create rule of per se legality for ATP and RPM where market share thresholds of BER satisfied (subject to prospective withdrawal)? Further even than US courts

Could have abolished list of hardcore restraints (art 4) and expanded list of severable, non-exempt obligations (Art 5) (OFT proposal)?

Reg 330/2010: Hardcore list essentially unchanged

Greater clarity and willingness to accept economic reality in new Vertical GLS?

## New 2010 Guidelines

- Commission will assess substantiated efficiencies of hardcore restraints against the negative impact under Article 101(3)
  - BUT still uphill struggle to show indispensable?
  - ‘There is a large measure of substitutability between the different vertical restraints. This means that the same inefficiency problem can be solved by different vertical restraints ... This is important as the negative effects on competition may differ between the various vertical restraints. This plays a role when indispensability is discussed under Article 101(3)’ (para 109).

# Efficiency Defence?

Paras 60-4 and 223-9, the Commission recognizes that in certain circumstances parties may be able to plead 'an efficiency defence' to justify both territorial and price restraints

- Territorial restraints may not violate Art 101(1) at all (para 60-1)
- RPM may be helpful for an introductory period to induce distributors to expand demand for, and promote a new product, to permit a coordinated short term low price campaign (2 to 6 weeks in most cases) in a uniform distribution system or to provide an extra margin to allow retailers to provide (additional) presales services, in particular in case of experience or complex products (para 225)

Has the Commission done enough?

As the consequence for a business of wrongly concluding that hardcore restraints are essential to the operation of its pro-competitive agreement and justifiable under Art 101 might be a substantial fine – is it likely that many (or any) firms will take the risk of inserting these restraints in an agreement?

## ATP

- Volkswagen (€90 m)
- Peugeot (€44.5 m)
- Nintendo (€167 m)

## RPM provisions

- Yamaha (€2.56m)
- £225,000,000 fine on tobacco manufacturers and retailers over retail pricing practices (OFT 2010)