The More Economic Approach to European Competition Law

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Introduction

by

DIETER SCHMIDTCHEN

Over the past ten years European competition policy has undergone dramatic change, largely inspired by the European Commission's move towards a more economics-based approach in the application of Article 81 ECT on anti-competitive agreements and in merger control. Following these reforms, the European Commission is also considering reform in the application of Article 82, concerning abuses of market dominance, and of Article 87 ECT, as regards state aid. A more economic approach to the application of competition law means that the assessment of each specific case will not be undertaken on the basis of the form or the intrinsic nature of a particular practice (form-based approach) but rather will be based on the assessment of its anti- and pro-competitive effects (effects-based approach). This move will lend itself to a rule of reason approach in Antitrust proceedings, and efficiency as a goal of Antitrust can be expected to play a more important role in the future. The effects-based approach is well illustrated by Recital 29 of Regulation 139/2004 (the Merger Regulation),[1] which reads as follows: "In order to determine the impact of a concentration on competition in the common market, it is appropriate to take account of any substantiated and likely efficiencies put forward by the undertakings concerned. It is possible that the efficiencies brought about by the concentration counteract the effects on competition, and in particular the potential harm to consumers, that it might otherwise have and that, as a consequence, the concentration would not significantly impede effective competition, in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position. The Commission should publish guidance on the conditions under which it may take efficiencies into account in the assessment of a concentration."[2]

While economic reasoning is becoming increasingly common in the study of substantive Antitrust, little attention has been devoted to procedural and enforcement issues. The main purpose of this conference was to investigate a number of basic questions concerning the law and economics of EC Antitrust enforcement, thereby taking into account the three dimensions in which methods of Antitrust enforcement can generally differ: the timing of legal intervention (ex ante enforcement through pre-screening and ex post

[1] See Regulation 139/2004 [2004] O. J. L24/1.

[2] An excellent discussion of an effects-based rather than a form-based approach to competition policy can be found in: An economic approach to Article 82, Report by the EAGCP Group, July 2005; see also Röller (2005) and Van den Bergh/Camasesca (2006).

enforcement through deterrence), the form of sanctions (whom sanctions should be imposed on and what form sanctions should take) and the role of private vs. public enforcement (including the assignment of tasks among different public enforcement agents). Quite naturally, the nature of enforcement and litigation problems as well as the feasible solutions also depend on the goals of Antitrust and the organisational architecture of the enforcement and litigation industry (including Public Choice issues).

Economists and jurists both from academia and practice have contributed to this volume, both as authors and commentators. The aim is to create a collection of papers which is as stimulating to read as were the discussions at the conference which took place in October 2006 in Saarbrücken, Germany. All papers are accompanied by a comment that was also presented at the conference. An interdisciplinary approach was realized here not only insofar as representatives of various disciplines contributed to the volume but also because we tried to select commentators from different disciplines as the paper presenters. We succeeded in most cases, but not in all.

In his paper *Goals of Antitrust and Competition Law Revisited*, Christian Kirchner provides a positive analysis of the process in which goals of competition law are being defined. The paper starts by distinguishing the following three levels: (1) competition as a game, (2) competition law as a set of rules of the game, and (3) law-making in the field of competition law as a game on the level of rule-making. Subsequently, the relevant actors on the third level are identified: The Member States, the Council and the Parliament as legislature of the European Community, the European Commission as executive power and the European Court of Justice as judiciary of the European Community. Having introduced these actors, the 'more economic approach' as a relevant factor for changing the game is being brought into play. The paper analyses the attitudes of the various actors towards the introduction of the 'more economic approach' and the expected impact on 'goals of competition law'. In the end a hypothesis on expected 'revisited goals of competition law' is formulated, accompanied by a plea to better study the process of revisiting goals of competition law than the expected outcomes of that game.

In his paper *The "More Economic Approach" and the Rule of Law*, Wulf-Henning Roth addresses the question whether there is a conflict between the 'more economic approach' which is pursued by the EU-Commission, and advocated by its (former) chief economist and its economic advisors on the one hand, and the need for a rule-based legal order on the other. First, he attempts to define what is meant by the 'more economic approach' and the 'rule of law' in a nutshell. Then, Roth examines the *lex lata* of European competition law and to what extent limitations are set to a 'more economic approach', as well as to what extent non-economic (social) objectives have to be taken into account. In a further step Roth tries to indicate to what extent judgments of the European Court of Justice (including the Court of First

Instance), as well as guidelines and pronouncements of the Commission are inspired by some sort of economic approach. Roth then turns to some of the issues where a conflict between the 'more economic approach' and the 'rule of law' may arise and, finally, makes some concluding observations.

In his paper *The Second Devolution of European Competition Law: The Political Economy of Antitrust Enforcement Under a 'More Economic Approach'*, Clifford Jones analyses the development of the system of EU competition law enforcement from its decentralized beginning in 1958 through the centralized regime set up by Regulation 17 (1962) and the 'First Devolution' following the European Court of Justice's decision in Delimitis (1991) to the 'Second Devolution', namely the reforms contained in Regulation 1/2003 and the pursuit by the European Commission of a 'more economic approach' to competition law. The paper then discusses the implications of these changes for competition law enforcement and suggests some of the likely consequences from a political economy perspective. It is suggested that more public and private enforcement activity are likely to result, but that reasonable levels of a coherent enforcement policy are to be expected despite the increase in the number and type of enforcers due to the cooperation and supervision mechanisms contained in Regulation 1/2003. It is also suggested that a dual public-private enforcement system will be more efficient, and that rent-seeking behaviour by private undertakings or government enforcers is unlikely to be a serious problem. On the whole, Jones expects an improvement of the enforcement system, while finding that it is too soon to render a fair judgement of the results of the changes.

In December 2005, the EU Commission published a Green Paper on actions for damages for the breach of EC Antitrust rules, according to which injured consumers and firms shall find it easier to reclaim losses from parties in breach of competition law. Furthermore, Antitrust enforcement is to be strengthened. In his paper *Should Private Enforcement of Competition Law Be Strengthened?*, Wernhard Möschel remains rather sceptical towards this trend.

In the first part of his paper, Möschel describes the experiences in private enforcement of competition law from the point of German, European and US-American competition law. In the second part, he discusses advantages and disadvantages of public enforcement of competition law. Finally, the third part examines advantages and disadvantages of a strengthened private enforcement regime. In Möschel's view, the disadvantages clearly dominate: Policies which result in facilitating the award of compensatory damages to injured parties are rather connected to the general principles of awarding damages than to the specific aspects of competition law. The sanctioning procedure appears to be totally deficient under corporate governance aspects: Shareholders turn against managers who partake in prohibited competitive practices. In the context of merger control, the possibilities of actions by

private third parties should rather be reduced, since the danger of abuse of private actions is particularly acute. In order to raise the efficiency of competition law on the sanctioning level, criminal sanctions in the form of imprisonment – thinking of Wouter Wils and US American Antitrust Law – appear to be the more promising approach.

In his paper *Effective Cartel Enforcement in Europe*, Maarten Pieter Schinkel works out the net effective (expected) liability of a representative modern international cartel. His back-of-envelope calculus reveals that future punishments for discovered cartels are tough. Yet the expected net cartel liability, even when it fully materializes on the high levels called for by the Commission, is likely to remain still far too low to deter collusion. The Commission should therefore create high (perceived) probabilities of detection across the board and set the right priorities in enforcement.

The paper by Hans Friederiszick and Frank P. Maier-Rigaud entitled *The Role of Economics in Cartel Detection in Europe* first provides an introduction to the nature of collusion and the role of economics. It then discusses the legal basis and the enforcement instruments available to the Commission in fighting cartels. The implementation of leniency programs is considered a great success both on Community and individual member state level. While accepting the contribution of leniency in pursuing the overarching objective of antitrust policy in the context of cartels – deterrence and desistence of collusive agreements – the authors argue in favour of a more balanced set of tools to detect cartels, including economic methods. They first discuss the interdependency and the individual advantages of leniency and ex officio cartel detection and then put forward the main challenges any economic methodology triggering ex officio inspections has to deal with. The last part of the paper deals with the two main methods for cartel detection – top down and bottom up approaches. The authors favour 'bottom up approaches', which include market screenings in the light of the application of the economics of tacit collusion to publicly available information. A methodology to proactively monitor markets based on economic criteria is put forward, thus limiting the resources needed to implement such a policy mix.

In his paper *Leniency in Antitrust Enforcement: Theory and Practice*, Wouter P. J. Wils discusses theory and practice of granting immunity from penalties or the reduction of penalties for antitrust violations in exchange for cooperation with the antitrust enforcement authorities. After a description of leniency practice in the US and the EU, and of its history, the paper analyses the positive effects and the possible negative effects of leniency on optimal antitrust enforcement, and the extent to which these effects can be measured. Matters of principle and institutional problems that may constitute obstacles to the introduction of leniency policies are discussed. Also, the impact on the effectiveness of leniency of the following is examined: Criminal penalties on

individuals, subsequent private actions for damages, penalties in other jurisdictions, 'Amnesty Plus', and positive financial rewards or bounties.

In late 2005, the Directorate General for Competition of the European Commission published a study on the effectiveness of merger remedies (DG Comp, 2005). This study reviews the design and implementation of 85 different remedies applied in 40 decisions of the European Commission between 1996 and 2000. The paper *Remedies in Merger Control* by Tomaso Duso, Klaus Gugler and Burcin Yortoglu, compares the main results of the DG Comp study, which used interviews as the main method, with a recent study conducted by the authors, in which an event study on merging and rival firms' stocks was applied as method. The main results of the authors' study suggest that only outright blockings solve the competitive problems generated by the merger. Remedies are not always effective in solving the market power concerns, at least not on average. Nevertheless, both structural (divestitures) and behavioural remedies are held to help restore effective competition when correctly applied to anticompetitive mergers during the first investigation phase. Yet, on the whole they are perceived ineffective, even detrimental, when applied in the second investigation phase. Furthermore, remedies – in particular behavioural ones – seem to constitute a rent transfer from merging to rival firms when wrongly applied to pro-competitive mergers. These results are consistent with the recent DG Comp study on the effectiveness of merger remedies.

In recent years, there have been significant developments in the use of merger simulations as a tool for many transactions that raise competitive concerns. An article by two leading figures in the field – Roy Epstein and Daniel Rubinfeld – entitled "*Merger Simulation: A Simplified Approach with New Applications*" (already published in the Antitrust Law Journal) is reprinted in this volume. The article is accompanied by a brief overview over recent trends written for this volume by Daniel Rubinfeld and entitled *Empirical Methods in Antitrust: New Developments in Merger Simulations.*

The article by Epstein and Rubinfeld first offers a relatively non-technical description of the principles of merger simulation, describes PCAIDS (Proportionality-Calibrated Almost Ideal Demand System), a new calibrated-demand merger simulation methodology, and presents examples that apply PCAIDS. It also suggests how simulation analyses might be used to evaluate the safe harbours of the US Merger Guidelines. According to the authors, the PCAIDS simulation approach represents a simplification compared to existing techniques. It only requires information on aggregate market shares, the industry price elasticity, and the own-price elasticity for a single brand in the relevant market.

Under Art 87 (1) of the EC Treaty, Member States are prohibited from granting state aid that distorts competition and trade in the EU, unless the European Commission exempts the aid from this prohibition under Article 87

(3) of the Treaty and declares the aid compatible with the Common Market. Since the launch of the State Aid Action Plan by the European Commission in 2005 there is reason to expect that State aid control in Europe is going to aim at an effects-based approach that is based on economic principles. In their paper *Comments on State Aid Reform – some Implications of an Effects-based Approach*, Rainer Nitsche and Paul Heidhues suggest that when investigating whether State aid is compatible with the Common Market, the European Commission should study the effect on welfare – considering both the effect on rivals and consumers. In addition, Member States must prove that State aid is targeted to effectively address a significant market failure. The paper also discusses some practical implications of the current process of State Aid reform.

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Goals of Antitrust and Competition Law Revisited

by

Christian Kirchner

1 Introduction

1.1 Preliminary remarks

The discussion of 'goals of antitrust' has been of practical and intellectual relevance since the first antitrust act of the United States of America – the Sherman Act – has been passed.[1] In the European Community, later the European Union, the goals of competition policy and competition law have been a matter of dispute since the early days of the European integration process.[2] The characteristic feature of Community competition law has been, that it served two goals: the competition goal and the integration goal. Whereas the former is focussing on promoting and protecting competition, the latter stresses the impact of competition and competition law on the process of integrating formerly separated national markets into one Single European Market. Today the focus of the European discussion has shifted towards the competition goal[3] and has thus been moving closer to goals of US antitrust law. Thus a transfer of antitrust concepts and goals to European competition law has been facilitated.

The perspective of this paper will be a European one. In the European Union competition policy means application and enforcement of competition law by the European Commission, the European Courts (and to a certain degree by national competition authorities and national courts of Member States). Thus it makes sense to focus on goals of Community competition law rather than of competition policy.

The present discussion on revisiting goals of European competition law may be seen as part of a world-wide trend into the direction of an 'economic approach'.[4] In Europe this trend was first visible in Commission statements in the late 1990s and early in the first decade of the new century under the name of 'more economic approach'.[5] This approach has been first adopted in the revised Merger Regulation of 2004.[6] Meanwhile the economic approach

[1] Jones (2006), pp. 18 – 23; Act of July 2, 1890, ch. 547, 26 Stat. 209, known as 'Sherman Act'.

[2] Kirchner (2005a), pp. 409 – 411.

[3] Ehlermann/Laudati (1998).

[4] Voigt/Schmidt (2005), pp. 53 – 117.

[5] See Monti (2001); Schmidtchen (2006).

[6] Council Regulation (EC) No. 139/2004 of 20 January on the control of concentration between undertakings, in: Official Journal L 24, 29/01/2004, pp. 1 – 22.

has reached the competition law provisions of the EC Treaty (Art. 81 and 82 EC).

1.2 Economic and legal approaches

To revisit 'goals of competition law' is an economic topic and a legal topic as well. In economic theory competition and competition law are subject matters of industrial organisation.[7] But from a legal perspective goals of Economic competition law are a subject matter of law.[8]

Economic and legal approaches are structurally different. Economic approaches are often using formal models which are to demonstrate welfare effects of different goals of competition law (e.g. maximisation of total welfare vs. maximisation of consumer welfare). Legal approaches may – from a constitutional perspective – view goals of competition law as sub-goals. They have to be defined in a manner that they best fit into the constitutional set of goals. To define goals of competition law becomes an exercise of law-making institutions, such as the legislature or law courts, so far as they go beyond applying Community law but engage in law-making via interpreting the law.

From a normative perspective economic approaches and legal approaches differ in so far as (mainstream) economic approaches stress welfare goals and ultimately efficiency,[9] whereas legal approaches are functional and focus on economic goals of the European Union and on 'constitutional goals' like 'the rule of law', 'legal certainty' and 'legitimacy of law-making'. Behind the two approaches, the economic and the legal one, stand different legitimisation concepts. Whereas (main stream) economists use a utilitarian concept (enhancing welfare), legal scholars leave the legitimisation to the legislature and courts. Whereas the legislature derives its legitimacy from democratic elections, law-making of law-courts rests upon a different legitimisation concept: they are supposed to be the 'mouth of the legislature'. Ultimately their power is based on the constitution (i.e. the Treaties establishing the European Community and the European Union).

From an economic perspective 'revisiting goals of competition law' means that new developments in economic theory are taken to be relevant factors for re-defining the normative goals of competition law. From a legal perspective 'revisiting goals of competition law' means that law-making institutions see good reasons to re-define such goals. One factor – amongst others – may be new economic insights. Thus, the economic and the legal perspective are

[7] Bishop/Walker 2002; Hildebrand 2002.

[8] Möschel 1991.

[9] See the critical evaluation of the Chicago School of Antitrust Analysis by Schmidt/Rittaler (1989).

connected. But that is not to say, that the legal definition of goals of competition law is being fully determined by economic reasoning. In order to study the process of revisiting goals of competition law neither a purely economic approach nor a purely legal approach would be appropriate. Whereas legal scholars tend to argue normatively and defend such goals which are purportedly legal ones,[10] it might be helpful to have a look into the interrelationship between the economic and the legal approaches and to concentrate rather on a positive than a normative analysis. Such type of analysis could add to the understanding of how goals of competition law are being revisited and what are the relevant factors in such a process.

1.3 Methodological issues: Means and ends-paradigm and new institutional economics

Because a discussion of competition law goals combines aspects of economics with those of law, it is necessary to clarify the methodological approach in a way that both aspects can be brought into play in one common methodological framework. There are two possible solutions of this problem: One may take recourse to the means and ends-paradigm and treat competition low goals as an instrument to pursue goals on a meta-level. Or one may treat legal norms as institutions in the sense of the New Institutional Economics and study the process of defining competition law goals by interaction between different groups of actors (positive analysis).

The means and ends-paradigm[11] plays a role in the study of economic policy and in judicial law-making. It thus could help to bridge the gap between the economic and the legal approach. The relationship between the 'goals of competition law' and general goals of economic policy in the means and ends-paradigm is the following one: Competition law is understood as an instrument to pursue goals of economics policy. Thus the goals of competition policy have to be defined in a manner that they serve the general goals of competition law best. This paradigm plays a similar role in the theory of legal interpretation, when the so-called teleological method of interpretation (method of finality)[12] comes into play, which can be understood as a device of legitimising law-making of law courts, which try to find out how an objective legislature would have solved the underlying problem of the given case. This method proceeds in two steps: (1) Identify the goals of the legal norms to be interpreted! (2) Search for a solution which best fits these goals best! The

[10] Immenga (2006).

[11] Kirchner (2006), p. 31; Streit (2005), p. 270; Mertens/Kirchner/Schanze (1982), pp. 46, 47; Kirchner (2006), p. 26, 31.

[12] Bydlinski (1991), pp. 435 – 453; Kirchner (2006), p. 26; Koch/Ruessmann (1982), pp. 222 – 227; Röhl (2001), pp. 600 – 603; Ruethers (2005), No. 717 – 730.

search for the best fitting solution is nothing else than an optimisation process. This is true for the application of the means and ends-paradigm in economics and in law.

If the means and ends-paradigm does not meet serious methodological objections, it would be possible to derive 'goals of competition law' from a given set of meta-goals. The problem would thus be moved to a higher level. It would have to be found out whether or not economists and legal scholars could agree on common meta-goals in the field of economic policy and thus in economic law. This might be doubtful.[13]

But in case serious methodological objections against the means and ends-paradigm exist, the issue of shared meta-goals between economists and legal scholars could be set aside. A new approach, which could bridge the gap between the economic and the legal approach have to be found. The means and ends-paradigm is under heavy methodological attack.[14] The determination of the proper meta-goal cannot be derived from the means and ends-paradigm as such. Meta-goals may be derived from meta-goals on higher levels. But that leads to an infinite regress. In the end the determination of the definite meta-goal is axiomatic, or a method has to be found how to legitimise the definite meta-goal. But even if this first problem has been solved another shortcoming of the means and ends-paradigm poses even bigger problems: If instruments are being applied in order to achieve a certain goal, they may – and of do – produce unintended side-effects. If such side-effects are not taken into account the result cannot be an optimum. If they are taken into consideration this leads to necessary changes of the given goal. Thus the means and ends-paradigm is circular in itself. As a consequence it appears reasonable for this analysis not to take recourse to the means and ends-paradigm but rather to engage in a positive analysis of the process of defining competition law goals.

'Goals of competition law' are legal rules on a meta-level. Legal rules may be viewed as 'institutions' in the sense of New Institutional Economics.[15] This economic approach is studying the creation and change of institutions, as well as their impact. Traditional legal approaches – namely on the European continent – are not so much interested in the law-making process. The exception is judicial law-making, where the teleological method of interpretation allows the judge to determine how the objective legislature would have solved the problem of the given case. But even if legal scholars are interested in a law-making process they do not define the assumptions of their analysis precisely. But that is a necessary prerequisite if a positive analysis is to produce testable results, i.e. hypotheses which can be falsified. The new institutional economics-approach may fill the existing gap thus enabling legal scholars to better analyse a law-making process.

[13] Immenga (2006).
[14] Kirchner (2006), pp. 31 – 48.
[15] Richter/Furubotn (2003), p. 7; Voigt (2002), pp. 33 – 41.