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THE U.S. ANTITRUST LAWS IN A GLOBAL CONTEXT
DIANE P. WOOD

USING ECONOMICS TO IMPROVE ANTITRUST POLICY
DENNIS W. CARLTON

ANTITRUST AND THE REGULATORY ENTERPRISE
HERBERT HOVENKAMP

SUPPLEMENT TO THE 2003 MILTON HANDLER ANNUAL ANTITRUST REVIEW PROCEEDINGS
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SUPPLEMENT TO THE 2003 MILTON HANDLER ANNUAL ANTITRUST REVIEW PROCEEDINGS

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PART ONE

A REVIEW OF SIMILARITIES AND CONTRASTS BETWEEN AMERICAN ANTITRUST AND EUROPEAN UNION COMPETITION LAW

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I. INTRODUCTION

On the eve of the expansion of the European Union to no fewer than twenty-five countries comprising more than 380 million consumers,[1] it is inevitably the case that more and more American corporations will find the way they do business to be influenced by the European Union's competition law regime. It is, therefore, increasingly important for United States corporations and their legal counsel to understand not only the key differences in the U.S. antitrust and E.U. competition enforcement regimes, but why those differences exist and how they matter to a corporation's day-to-day business conduct. As Judge Wood notes,[2] both the U.S. and the E.U. systems are based on principles that free markets and full-throated competition will produce the best mixture of goods and services in the most efficient way. Within this broad umbrella of philosophical agreement, however, important differences exist.

In this section, we explore recent developments in three such areas: (i) the treatment of single-firm conduct; (ii) regulation of "gray market" or parallel imports by the European Union, and (iii) analysis of the risk of coordinated effects in merger reviews. This analysis reveals that, while areas of convergence in substantive analysis do exist, the type of economic analysis that is characteristic of recent U.S. antitrust developments has been constrained in the European Union by two unique political imperatives: the objective of integrating diverse national markets into a "single market," while in the process protecting small- and medium-sized enterprises. As alluded to in Judge Wood's remarks,[3] both of these objectives are steeped in history and

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[1] *See* Press Release, Eurostat, First Demographic Estimates (Jan. 9, 2004) *available at* http://europa.eu.int/comm/eurostat/Public/datashop/print-product/EN?catalogue=Eurostat&product=3-09012004-EN-BP-EN&mode=download.

[2] Diane P. Wood, *The U.S. Antitrust Laws In A Global Context*, 2004 COLUM. BUS. L. REV. 265.

[3] *Id.*

thus likely to remain significant factors forming the development of E.U. competition law.

II. U.S. AND E.U. TREATMENT OF SINGLE FIRM CONDUCT

Both U.S. and E.U. law prohibit certain types of conduct undertaken by single firms that possess exceptionally large market shares. In the United States, Section 2 of the Sherman Act prohibits monopolization, attempts to monopolize, and conspiracies to monopolize.[4] In the European Union, Article 82 of the European Community Treaty prohibits "abuse . . . of a dominant position."[5]

These two regimes have much in common, but also have many differences. Both, for example, require the examination of a firm's conduct within the context of a "relevant market," which is defined in roughly the same way in the United States and the European Union.[6] Both also limit the application of monopoly control to firms that have the power to control price or act without regard to their competitors. In the United States, Section 2 requires that a firm possess "monopoly power," usually defined as "the power to control prices or exclude competition."[7] Generally, a firm has monopoly power if it possesses substantial market share and has the power unilaterally and profitably to raise prices "substantially above the competitive level."[8] In the European Union, Article 82 requires that a firm have "a dominant market position," defined as "a position of economic strength enjoyed by an undertaking which enables it to hinder the maintenance of effective competition in the

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[4] 15 U.S.C. § 2 (2000).

[5] TREATY ESTABLISHING THE EUROPEAN COMMUNITY, Nov. 10, 1997, art. 86 (now art. 82), O.J. (C 340) 3 (1997) [hereinafter EC TREATY].

[6] *See* Henry Huser & Frederic Depoorteere, *Substantive Enforcement Standards in Horizontal Mergers Under the EC Merger Regulation*, 17 ANTITRUST 44 (2002).

[7] United States v. E.I. du Pont de Nemours & Co., 351 U.S. 377, 391 (1977).

[8] United States v. Microsoft Corp., 253 F.3d 34, 51 (D.C. Cir. 2001).

relevant market by allowing it to behave to an appreciable extent independently of its competitors and customers and ultimately of consumers."[9] Neither the United States nor the European Union sanctions a firm merely for being large or for possessing monopoly power or dominance. In both jurisdictions, a monopolist must engage in certain anticompetitive conduct intended to maintain or expand its market position before it will be found to have acted unlawfully.[10]

Beyond these similarities, however, lie some important differences between U.S. and E.U. treatment of firms possessing commanding market shares. Perhaps the key difference is that the enforcement goal of U.S. antitrust law is generally to enhance consumer welfare through high output and low consumer prices. Consistent with this bedrock principle, the United States will permit monopolies to engage in activities where they maintain their position by becoming more efficient.[11] However, the type of conduct that may violate Article 82 demonstrates that E.U. competition law is also concerned with the goal of maintaining a level playing field for competitors, which is not as significant a concern in the United States.[12]

This philosophical difference between the two regimes is reflected in their differing views of a monopolist's duties

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[9] Case 322/81, Nederlandsche Banden Industrie Michelin NV v. Commission, 1983 E.C.R. 3461, 1 C.M.L.R. 282 (1985). *See also* Case 85/76, Hoffman-LaRoche & Co. AG v. Commission, 1979 E.C.R. 461, 3 C.M.L.R. 211 (1979).

[10] *See, e.g.*, United States v. Grinnell Corp., 384 U.S. 563, 570-71 (1966); A.B.A. SECTION OF ANTITRUST LAW, COMPETITION LAWS OUTSIDE THE UNITED STATES, European Union-49 (H. Stephen Harris, ed., 2001) ("EC law prohibits not the dominant position, but its abuse.").

[11] *See, e.g.*, United States v. Syufy Enters., 903 F.2d 659, 669 (9th Cir. 1990) ("[A]n efficient, vigorous, aggressive competitor is not the villain antitrust laws are aimed at eliminating.").

[12] *See, e.g.*, Press Release, European Commission, Commission Gives Microsoft Last Opportunity to Comment Before Concluding its Antitrust Probe, (Aug. 6, 2003), *available at* http://europa.eu.int/rapid/start/cgi/guesten.ksh?p_action.gettxt=gt&doc=IP/03/1150 | 0 | AGED&lg=EN&display=.

toward its competitors. In the United States, a monopolist's duty is limited to avoiding conduct that is intended to maintain or expand its position where that conduct cannot be justified on business or efficiency grounds.[13] A monopolist generally has no duty to deal with its competitors, and is not required to pull its punches; to the contrary, it is encouraged by the antitrust laws to engage in vigorous competition.[14] Article 82, however, has been interpreted to impose a "special responsibility" on a dominant firm "not to allow its conduct to impair undistorted competition."[15] This responsibility has been interpreted, for example, to prohibit such conduct as "monopoly leveraging," defined as the use of a firm's monopoly power in one market to gain a competitive advantage in another.[16] It also has been held in some cases to prohibit the sale of goods at low prices that are specifically targeted to drive competitors out of business, even where the prices charged are still in excess of some measure of seller's costs.[17] Finally, a dominant firm's offering of fidelity discounts, whereby discounts are conditioned on a buyer's purchasing all or most of its requirements from the seller, have proven problematic under E.U. law.[18]

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[13] *See* Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585, 605 (1985).

[14] *See, e.g.,* Verizon Comm. Inc. v. Law Offices of Curtis V. Trinko, L.L.P., 124 S. Ct. 872, § III (2004).

[15] Case 322/81, Nederlandsche Banden Industrie Michelin NV v. Commission, 1983 E.C.R. 3461, ¶ 57, 1 C.M.L.R. 282 (1985). *See also* Case 85/76, Hoffman-LaRoche & Co. AG v. Commission, 1979 E.C.R. 461, 486, 3 C.M.L.R. 211 (1979).

[16] *See, e.g.,* Case T-83/91, Tetra Pak Int'l SA v. Commission, 1994 E.C.R. II-755, 4 C.M.L.R. 726, ¶¶ 102-23 (1997), *aff'd* C-333/94 P, 1996 E.C.R. I-5951, 4 C.M.L.R. 662, ¶¶ 34-62 (1997).

[17] *See* Case C-62/86, AKZO Chemie BV v. Commission, 1991 E.C.R. I-3359; *see also Tetra Pak*, 1994 E.C.R. II-755.

[18] Most recently, the Court of First Instance upheld the European Commission's decision to fine Michelin •19.76 million for abusing its dominant position in the French replacement tire market in violation of Article 82. *See* Case T-203/01, Manufacture Française des Pneumatiques Michelin v. Commission, 2003 O.J. (C 304) 24. Michelin gave no economic justification for its system of quantity discounts, which, because it was

While U.S. antitrust law can also theoretically be applied to control conduct such as predatory pricing, its application is quite limited in the absence of at least a dangerous possibility of monopolizing the second market. For example, monopoly leveraging, at least as an independent basis for Section 2 liability, has been rejected in the United States.[19] While E.U. law may allow a predatory pricing claim under certain circumstances where the defendant sells at prices above cost and may not require a showing of the ability to recoup losses,[20] the Supreme Court's *Brooke Group* decision explicitly bars Section 2 predation claims absent proof that the predator sold its products at a price below some measure of cost and that it had a reasonable prospect of recouping its losses through monopoly pricing following the elimination of a competitor.[21]

The state of the law in the United States regarding loyalty (or market share) discounts remains a topic of considerable discussion.[22] That discussion includes whether, and to what extent, loyalty-discount agreements may be

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loyalty-inducing, tended to prevent French dealers in truck and bus tires not only from ascertaining the price at the time of purchase but also from obtaining supplies from competing manufacturers. The service bonuses operated by Michelin, which supposedly rewarded after-sales services provided by dealers, also had an abusive effect: they were unfair since they were based on subjective criteria, were loyalty-inducing and were in the nature of a tied sale in that they encouraged dealers to give priority to Michelin when having tires retreaded. *See also* Commission Decision of 14 July 1999, Relating to a Proceeding under Article 82 of the E.C. Treaty, Case IV/D-2/34.780, Virgin/British Airways, 2000 O.J. (L 30) 1, *aff'd*, Case T-219/99, British Airways v. Commission, 2003 E.C.R. I-0000; Case T-228/97, Irish Sugar v. Commission, 1999 E.C.R. II-2969, 5 C.M.L.R. 1300 (1997); *Michelin*, 1983 E.C.R. 3461; *Hoffman-LaRoche*, 1979 E.C.R. 461.

[19] *See Trinko,* 124 S. Ct. at 883 n.4 (citing Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 459 (1993)).

[20] *Tetra Pak*, 1994 E.C.R. II-755.

[21] Brooke Group Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 222-25 (1993).

[22] *See, e.g.*, Dep't of Justice, Exclusionary Pricing Conference, Washington, D.C. (Mar. 18, 2004); LePage's Inc. v. 3M, 324 F.3d 141 (3d Cir. 2003); Concord Boat Corp. v. Brunswick Corp., 207 F.3d 1039 (8th Cir. 2000), *cert. denied*, 531 U.S. 979 (2000).

found to restrict competition unlawfully as exclusive dealing agreements by monopolists have been found to do.[23]

Two additional differences between the U.S. and E.U. approaches to monopoly control are also worthy of note. First, the market share test used to identify monopolists differs in the two jurisdictions. U.S. courts will usually find monopoly power only when market shares exceed sixty or seventy percent,[24] while, in the European Union, a market share in excess of 50 percent is strong *prima facie* evidence of dominance.[25] Second, the two regimes have significantly different attitudes toward monopoly pricing. The E.C. Treaty prohibits a dominant firm from "imposing unfair purchase or selling prices or unfair trading conditions."[26] In the United States, by contrast, a firm that lawfully acquires monopoly power does not violate Section 2 merely by exercising that power and charging prices higher than those that would prevail in a competitive market. Indeed, in the United States, the "charging of monopoly prices [] is not only

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[23] *See* Lorain Journal Co. v. United States, 342 U.S. 143, 157 (1951) (affirming a district court finding that a monopolist violated Section 2 of the Sherman Act by refusing to sell its advertising services to any firm that bought advertising services from a competitor whose entry threatened to weaken the defendant's existing monopoly); *see also* United States v. Microsoft Corp., 59 Fed. Reg. 42,845, 42,848 ¶¶ 26-28 (Aug. 19, 1994) (consent decree entered in the District of Columbia district court, in part, barring Microsoft, the leading manufacturer of operating system software for personal computers, from requiring computer manufacturers to pay a royalty for each computer regardless of whether the unit was shipped with a Microsoft operating system or that of some other firm); United States v. Microsoft Corp., 56 F.3d 1448 (D.C. Cir. 1995) (upholding consent decree).

[24] *See, e.g.,* United States v. E.I. du Pont de Nemours & Co., 351 U.S. 377, 391 (1956) (citing United States v. Aluminum Co. of Am., 148 F.2d 416, 429 (2d Cir. 1945); Am. Tobacco Co. v. United States, 328 U.S. 781 (1946)).

[25] *See* Case C-62/86, AKZO Chemie BV v. Commission, 1991 E.C.R. I-3359 ¶ 60; *see also* JONATHAN FAULL & ALI NIKPAY, THE EC LAW OF COMPETITION, ¶ 3.39 (1999).

[26] EC TREATY, *supra* note 5, art. 82(a).

not unlawful; it is an important element of the free-market system."[27]

Two recent U.S. and E.U. enforcement actions highlight some of the practical effects of these differences between U.S. and E.U. treatment of monopolies: the now scuttled General Electric/Honeywell merger and the Microsoft litigation. These two cases, involving divergent U.S. and E.U. treatment of two of the world's largest corporations, illustrate that differences between U.S. antitrust law and E.U. competition law may have significant consequences. These cases also highlight how procedural differences, including differing degrees of judicial oversight, may contribute to divergent outcomes in United States and European Union enforcement actions.

A. General Electric/Honeywell

The differences between U.S. and E.U. law were placed in stark relief by the differing approaches of the U.S. and E.U. merger authorities to the proposed merger of Honeywell International Inc. ("Honeywell") and General Electric Co. ("GE") in 2001. That transaction was abandoned following the European Commission ("E.C.") announced its intention to block the merger,[28] the first occasion in which European regulators sought to block a U.S. transaction that had been cleared by U.S. antitrust authorities.[29] While merger law is not, at least technically, part of the law that governs single-firm conduct, the differing approaches to the GE/Honeywell merger offer a window into important substantive differences in U.S. and E.U. attitudes toward single-firm conduct and monopoly market structure. The transaction also reveals how differences in U.S. and E.U. enforcement

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[27] Verizon Comm. Inc. v. Law Offices of Curtis V. Trinko, L.L.P., 124 S. Ct. 872, § III (2004).; *see also* Alaska Airlines v. United Airlines, 948 F.2d 536, 548-49 (9th Cir. 1991).

[28] Lou Whiteman, *GE-Honeywell: Merger Redux?*, DAILY DEAL, Dec. 2, 2002.

[29] Jay Pil Choi, *A Theory of Mixed Bundling Applied to the GE / Honeywell Merger*, 16 ANTITRUST 32 (2001).

procedures affected the outcomes of the two merger reviews. The merger-specific efficiencies that allowed the parties to convince U.S. regulators that the merger would be welfare-enhancing and beneficial to consumers of the combined firms' products were among the factors that caused the European Commission to vote to block the merger based on a "portfolio effects" theory.

The driving force behind the GE/Honeywell merger was the two companies' complementary aviation product lines. GE manufactures, sells and services large jet engines and offers financing to aircraft purchasers through its GE Capital Aviation Services ("GECAS") subsidiary. Honeywell manufactures smaller aircraft engines, avionics, and other aircraft parts. The two companies had virtually no overlapping product lines, but the combination of their complementary lines would have enabled the merged entity to offer a full range of products to purchasers of jet engines, avionics, parts, and aircraft financing. In effect, the merged entity would have been a "one-stop shop" for such purchasers.

Following a five-month investigation, the Antitrust Division of the U.S. Department of Justice ("DOJ") announced that it had reached an agreement in principle with the parties to the transaction resolving the DOJ's antitrust concerns by requiring some relatively minor divestitures.[30] As a conglomerate merger—a merger that did not involve the combination of competitors or suppliers and customers—the transaction was relatively uncontroversial under U.S. antitrust law and raised no serious competition concerns. As a senior DOJ official commented, "the U.S. antitrust agencies concluded that antitrust should rarely, if ever, interfere with any conglomerate merger."[31]

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[30] Press Release, U.S. Department of Justice, Justice Department Requires Divestitures in Merger Between General Electric and Honeywell, (May 2, 2001), *available at* http://www.usdoj.gov/atr/public/press_releases/2001/8140.pdf.

[31] Deborah Platt Majoras, Deputy Assistant Attorney General, Antitrust Division, U.S. Department of Justice, Remarks before the Antitrust Law Section, State Bar of Georgia, GE-Honeywell: The U.S.

Two months later, however, the European Commission reached the opposite conclusion, finding that GE's size and financial strength (at the time, GE had the largest market capitalization of any company in the world) were a source of GE's dominance in the market for large engines, and were likely to be used by GE to strengthen the Honeywell product lines post-merger and foreclose competition. The European Commission concluded that the combination of GE's financial strength, the merged entity's ability to offer one-stop shopping and attractive financing from GECAS would be anticompetitive, even though such offerings might be highly attractive to aircraft customers. The European Commission wrote: "Indeed, the ability to put together its considerable financial strength . . . and to offer comprehensive packaged solutions to airlines have given GE the ability to foreclose competition."[32]

While arguments of this kind held currency in the United States in the 1960s, modern U.S. antitrust economic analysis has long since rejected the "big is bad" theory of antitrust.[33] Under U.S. law, a transaction that will enable the merged firm to offer lower prices and better terms to its customers is considered pro-competitive, regardless of the ability of the firm's competitors similarly to cut prices. This is in keeping

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Decision (Nov. 29, 2001), at 13-14, *available at* http://www.usdoj.gov/atr/public/speeches/9893.pdf.

[32] Commission Decision of 3 July 2001, Declaring a Concentration to be Incompatible with the Common Market and the EEA Agreement, Case COMP/M.2220, GE/Honeywell, 2004 O.J. (L 48), ¶ 163. While the parties immediately appealed the EC's decision to the European Union's Court of First Instance ("CFI"), they are still awaiting a decision more than two years later. *See* Case T-209/01, Honeywell Int'l Inc. v. Commission, 2001 O.J. (C 331) 23; Case T-210/01, Gen. Elec. Co. v. Commission, 2001 O.J. (C 331) 24.

[33] *Compare* United States v. Von's Grocery Co., 384 U.S. 270 (1966) *with* United States v. Gen. Dynamics Corp., 415 U.S. 486 (1974). *See also* U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, 1992 HORIZONTAL MERGER GUIDELINES (1992) (with 1997 revisions), § 1.51 [hereinafter MERGER GUIDELINES] (presumption of market power due to high level of market concentration can be overcome by other factors, including entry, efficiencies, and imminent failure of a party involved).

with the fundamental axiom in the United States that "antitrust protects competition, not competitors."[34] Indeed, this is the basic reason why U.S. law recognizes an "efficiencies defense" in merger law, whereby an otherwise anticompetitive merger can be saved if the parties can establish that its anticompetitive effects are outweighed by efficiencies that are likely to be realized as a result of the transaction.[35]

Though the business logic of the GE/Honeywell transaction was driven by merger-specific efficiencies, the European Commission did not view these efficiencies as a positive factor. To the contrary, the European Commission took a negative view of the deal's efficiencies,[36] fearing that they would tilt the playing field, giving GE such an attractive offering to customers that its competitors would be effectively foreclosed from the market.[37] This was plainly contrary to the U.S. approach in that case.

B. Microsoft

The continuing antitrust saga of Microsoft Corporation also highlights important contrasts between U.S. and E.U. treatment of single-firm conduct. Both the DOJ and the

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[34] Brunswick Corp. v. Pueblo Bowl-O-Mat Inc., 429 U.S. 477, 488 (1977).

[35] *See* MERGER GUIDELINES, *supra* note 33, § 4.

[36] E.C. officials, in speeches following the decision, have denied that their approach was based on perceived deleterious effects of merger efficiencies. *See, e.g.*, Mario Monti, European Competition Commissioner, Address Before Merchant Taylor's Hall, London, United Kingdom, The Future for Competition Policy in the European Union, July 9, 2001, *available at* http://europa.eu.int/comm/competition/speeches/index_2001.html; comments of Francisco-Enrique Gonzalez-Diaz, then-head of the European Commission's Merger Task Force, *in Transatlantic Antitrust: Convergence or Divergence*, Roundtable Discussion, 16 ANTITRUST 5, 8 (2001) ("The Commission has nothing against efficiencies, and has never prohibited or interfered with a deal that was shown to be likely to lead to significant efficiencies.").

[37] *See, e.g.,* Donna E. Patterson & Carl Shapiro, *Transatlantic Divergence in GE/Honeywell: Causes and Lessons*, 16 ANTITRUST 18, 20-21 (2001).

European Commission have investigated Microsoft's business practices for a number of years, and the European Commission continues to do so. In the United States, the investigation led to two lawsuits by the DOJ and a number of states attacking Microsoft's business conduct.[38]

In the second of those cases, the DOJ and the states alleged that Microsoft had employed a range of unlawfully restrictive agreements with computer manufacturers to protect the Microsoft operating system monopoly against threats from "middleware" software such as the Netscape Navigator web browser and Sun Microsystems' Java programming platform.[39] After a lengthy and highly publicized trial, the trial court concluded that Microsoft had engaged in monopolization, attempted monopolization and tying, in violation of Sections 1 and 2 of the Sherman Act.[40] The U.S. Court of Appeals for the D.C. Circuit affirmed many of the trial court's findings that Microsoft committed significant violations of Section 2, holding that certain Microsoft business practices, including licensing restrictions and the technological binding of Microsoft's web browser, Internet Explorer, to its Windows operating system, were illegal.[41]

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[38] The first lawsuit, which is not addressed in this article, resulted in the entry of a consent decree which prohibited Microsoft from (i) obtaining a royalty on the sale of computers that did not include its operating system, (ii) entering into licenses of more than one year, and (iii) requiring unreasonably restrictive nondisclosure agreements. *See* United States v. Microsoft Corp., 1995-2 Trade Cases (CCH) ¶ 71,096 (D.D.C. 1995).

[39] The European Commission recently announced that it has initiated a related investigation into Microsoft's license agreements with computer hardware manufacturers. *See Monopolization: EC Initiates Investigation of Microsoft License Agreements with Hardware Makers*, BNA ANTITRUST & TRADE REGULATION DAILY, Oct. 31, 2003.

[40] United States v. Microsoft Corp., 187 F. Supp. 2d 30 (D.D.C. 2000).

[41] United States v. Microsoft Corp., 253 F.3d 34, 46 (D.C. Cir. 2001) (affirming in part and reversing in part findings of violations of Sections 1 and 2 of the Sherman Act.) The Court of Appeals held that "Microsoft's exclusion of [Internet Explorer] from the Add/Remove Programs utility and its commingling of browser and operating system code constitute exclusionary conduct, in violation of § 2." *Id.* at 67.

One key holding of the court of appeals related to a tying claim in which the DOJ argued, and the district court agreed, that Microsoft committed a per se illegal tie-in by forcing computer manufacturers to pre-install the Internet Explorer browser on Windows machines and by making it difficult or impossible for end users to "uninstall" Internet Explorer.[42] The court of appeals reversed the district court's holding of per se illegality, and remanded the tying claim for reexamination under a fuller rule of reason analysis.[43] The court held that, in the context of the "platform software market" for so-called "middleware" (such as web browsers), a rule of per se illegality for tying might "stunt valuable innovation."[44] Its reasoning was twofold: first, the court held, a rule of per se illegality would prevent an innovator who integrates two previously separate products from defending his actions on the basis that efficiency gains from the integration adequately offset any distortion of consumer choice. Second, and perhaps more importantly, the D.C. Circuit admitted that courts may not have the capacity or experience to evaluate efficiencies gained by integrating previously separate products. In light of the "pervasively innovative character of platform software markets," the court held, these efficiencies may not have been factored into the per se rule as originally formulated by the Supreme Court.[45] This ruling reflects a profound concern that innovation, even by a monopolist, be encouraged and not stifled.

The case brought by the European Commission against Microsoft, which was recently decided, may be viewed as

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[42] *Microsoft*, 187 F. Supp. 2d at 47-51.

[43] *Microsoft*, 253 F.3d at 94. In another portion of the same opinion, however, the court of appeals held that the commingling of code between the browser and the operating system, together with the exclusion of the browser from Microsoft's "Add/Remove Programs" utility, was an independent basis for liability under the government's Section 2 monopoly maintenance claims. *Id.* at 67.

[44] *Id.* at 92.

[45] *Id.* at 93.

reaching the opposite conclusion.[46] That case dealt with a different, though similar, subject—Microsoft's integration of the Windows Media Player ("WMP") software into the latest versions of Windows.[47] The European Commission found that, by including WMP as a part of Windows, Microsoft abused its market power in the market for computer operating systems and "significantly weakened competition on the media player market."[48]

According to the European Commission's announcement of its decision,

> This part of the investigation concluded that the ubiquity which was immediately afforded to WMP as a result of it being tied with the Windows PC OS artificially reduces the incentives of music, film and other media companies, as well software developers and content providers to develop their offerings to competing media players.
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> As a result, Microsoft's tying of its media player product has the effect of foreclosing the market to competitors, and hence ultimately reducing consumer choice, since competing products are set at a disadvantage which is not related to their price or quality.[49]

The European Commission thus reached the conclusion with respect to WMP that the DOJ (unsuccessfully) asked the D.C. Circuit to reach with respect to Internet Explorer.[50] In essence, just as the DOJ attacked Microsoft's alleged

[46] At the time of publication, the text of the European Commission decision had not yet been made public.

[47] WMP is a "software product that is able to 'play back' music and video content over the Internet." Press Release, European Commission, Commission Concludes on Microsoft Investigation, Imposes Conduct Remedies and a Fine (Mar. 24, 2004), *available at* http://europa.eu.int/rapid/start/cgi/guesten.ksh?p_action.gettxt=gt&doc=IP/04/382|0|RAPID&lg=EN&display=.

[48] *Id.*

[49] *Id.*

[50] *Microsoft*, 253 F.3d at 84.

effort to dominate the market for web browsers by including Internet Explorer in Windows, the European Commission attacked Microsoft's incorporation of WMP into Windows and found it to be unlawful tying under E.U. competition law.

These two decisions raise the issue of whether U.S. and E.U. law diverge on the legality of a monopolist's incorporation of a previously separate product into the monopolist's monopoly product. The U.S. and E.U. Microsoft decisions diverge as to outcome—Microsoft's bundling was condemned as a tie in the European Union but not in the United States. However, they may not represent a divergence in the law. The D.C. Circuit in *Microsoft* did not hold that Microsoft's tying of the browser to the operating system was legal.[51] It held that the issue could only be resolved after a full review under the rule of reason—something the trial court had not done. In reaching its decision in Microsoft, the European Commission announced that its ruling was fully consistent with that of the D.C. Circuit because it based its ruling on a full rule of reason review.[52] Thus, according to the European Commission, while the results in the two cases may be different, that does not represent a divergence in the law. An assessment of that position should probably await a review of the full E.C. decision and the legal contours it establishes.

In sum, there is, at least on the surface, similarity between the U.S. and E.U. approaches to monopoly control. Beneath the surface, however, there are significant substantive and procedural differences. For the businessperson (or advising counsel) conducting business in both jurisdictions, these differences may merit careful attention.

[51] *Id.*

[52] Press Release, European Commission, Commission Concludes on Microsoft Investigation, Imposes Conduct Remedies and a Fine (Mar. 24, 2004), *available at* http://europa.eu.int/rapid/start/cgi/guesten.ksh?p_action.gettxt=gt&doc=IP/04/382 | 0 | RAPID&lg=EN&display=.

III. "GRAY MARKET" OR PARALLEL IMPORTS IN E.U. LAW

Unlike the U.S. model, the E.U. competition rules were adopted and have developed within a legislative framework established to help forge a common market out of countries that, as noted by Judge Wood, had more than a millennium of independent existence.[53] Because of this integration objective, the relationship between producers and distributors and other vertical relationships in the distribution chain has been of particular concern for E.U. competition policy.

In the European Union, anticompetitive agreements or concerted practices are governed by Article 81(1) of the E.C. Treaty, which prohibits agreements that "may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition . . . ."[54] This provision has become one of the

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[53] Wood, *supra* note 2, at 270.

[54] Article 81(1) of the E.C. Treaty (formerly Article 85) provides:

> 1. The following shall be prohibited as incompatible with the common market: all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market, and in particular those which
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> (a) directly or indirectly fix purchase or selling prices or any other trading conditions;
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> (b) limit or control production, markets, technical development, or investment;
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> (c) share markets or sources of supply;
>
> (d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;
>
> (e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by

principal vehicles used by the European Commission to achieve its long-standing objective of market integration.[55] Through a long line of cases, the European Commission has sought to achieve market integration by restricting the ability of manufacturers to divide geographic markets by imposing territorial limits or other restrictions on cross-border sales.[56]

If a manufacturer prices its products differently along national boundaries, its distributors are presented with an arbitrage opportunity—the potential to buy the same product at a low price in one country and sell it at a higher price in another country. Such arbitrage has become known in the European Union as "parallel trade," and creates what is known as a gray market—goods being sold outside the official distribution channels of the manufacturer.[57]

> their nature or according to commercial usage, have no connection with the subject of such contracts.

EC TREATY, *supra* note 5, art. 81(1).

It should also be noted that Articles 28-30 of the E.C. Treaty, under Title 1, Free Movement of Goods, govern state restrictions on parallel trade between member states. *See* Peter Stig Jakobsen & Morton Broberg, *The Concept of Agreement in Article 81 E.C.: On the Manufacturer's Right to Prevent Parallel Trade Within the European Community*, 23(3) E.C.L.R. 127, 128 n.9 (2002) (considering possibility that Article 28 may apply not only to states but also to undertakings).

[55] "The creation of a single market is one of the main objectives of the European Union's competition policy." European Commission, Green Paper on Vertical Restraints in E.C. Competition Policy, exec. summary at i (Jan. 22, 1997), *available at* http://europa.eu.int/comm/competition/antitrust/96721en%5Fen.pdf. *See also* Commission Notice, Guidelines on Vertical Restraints, 2000 O.J. (C 291) 1, § I.2, ¶ 7, *available at* http://europa.eu.int/eurlex/pri/en/oj/dat/2000/c_291/c_29120001013en00010044.pdf.

[56] "In the context of a Common Market in Europe, parallel importers are generally seen by the E.U. authorities as a means of breaking down national barriers and cementing the Single Market." Julie S. Nazerali, *Parallel Imports of Pharmaceuticals—A Prescription for Success or a Free Market Overdose*, 19(6) E.C.L.R. 332, 332 (1998).

[57] *See* European Commission's Directorate-General for Competition glossary, *available at* http://europa.eu.int/comm/competition/general_info/p_en.html#t25; *cf.* World Trade Organization, Fact Sheet: TRIPS and

Manufacturers taking action to diminish such intrabrand competition and curtail the gray market trade in their own products generally impose vertical agreements upon their distributors. Vertical agreements are "relationships between firms which operate at different levels within the chain of distribution, for example between a manufacturer and a distributor or between a wholesaler and a retailer."[58]

To further the European Union's market integration objectives, the European Commission has pursued a competition policy that seeks to prevent manufacturers from insulating national markets from intrabrand competition by restricting parallel imports and cross-border sales.[59] The European Commission has systematically prosecuted and won cases against companies that have taken action to restrict parallel or gray market trade. In two recent high profile cases, however, the Court of First Instance annulled these E.C. decisions. These cases were *Bundesverband der Arzneimittel-Importeure v. Bayer Commission* ("*Bayer*"), which was affirmed by the European Court of Justice ("ECJ")

Pharmaceutical Patents: Obligations and Exceptions (April 2001), *available at* http://www.wto.org/english/tratop_e/trips_e/factsheet_pharm02_e.htm#parallelimports ("Parallel or grey-market imports are not imports of counterfeit products or illegal copies. These are products marketed by the patent owner (or trademark- or copyright-owner, etc.) or with the patent owner's permission in one country and imported into another country without the approval of the patent owner.").

58 H.H. Paul Lugard, *Vertical Restraints Under EC Competition Law: A Horizontal Approach*, 17(3) E.C.L.R. 166, 168 (1996). *See also* Commission Regulation 2790/1999 of 29 December 1999 on Article 2(1), 1999 O.J. (L 336) 21 (defining vertical agreements as "agreements or concerted practices entered into between two or more undertakings each of which operates, for the purposes of the agreement, at a different level of the production or distribution chain, and relating to the conditions under which the parties may purchase, sell or resell certain goods or services.").

59 *See, e.g.*, Commission Decision of 29 June 2001, on a Proceeding under Article 81 of the E.C. Treaty, Case COMP/F-2/36.693, Volkswagen, 2001 O.J. (L 262) 14, ¶ 17 (explaining that the Commission's goal in publishing a biannual survey of car prices in the European Union is "to ensure that, through increased price transparency, price differentials will diminish as a result of the market forces released.").

on January 6, 2004,[60] and *Volkswagen AG v. Commission* ("*Volkswagen*"), decided by the CFI on December 3, 2003.[61] The *Volkswagen* and *Bayer* decisions are significant setbacks for the European Commission, and may effectively limit the European Commission's ability to use the competition laws to forge an integrated market.[62]

A. *Volkswagen v. Commission*

Volkswagen involved the European Commission's investigation into Volkswagen AG's pricing policies with its dealers. By contract with its authorized dealers, Volkswagen had issued non-binding price recommendations for retail prices and discounts, which had resulted in higher prices on specific car models in the German market as compared to other E.U. markets.[63] The technical question of law in the case was whether certain price recommendations became integrated into the underlying distribution contracts such that an anticompetitive agreement was formed between Volkswagen and the German dealers to maintain retail prices.

Just as in the United States, non-binding price recommendations from a manufacturer to a dealer are not,

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[60] Judgment of the Court of 6 January 2004, Joined Cases C-2/01 P & C-3/01 P, Bundesverband der Arzneimittel-Importeure v. Bayer, 2004 O.J. (C 59) 2.

[61] Judgment of the Court of First Instance of 3 December 2003, Case T-208/01, Volkswagen v. Commission, 2004 O.J. (C 71) 24 (on application for annulment of Commission Decision of 29 June 2001, Relating to a Proceeding Under Article 81 of the E.C. Treaty, Case COMP/F-2/36.693, Volkswagen).

[62] *See* Paul Meller, *Europe Effort to Control Pricing is Set Back*, N.Y. TIMES, Jan. 7, 2004, at W1. For a critique of the basis of the *Volkswagen* decision, see Jakobsen & Broberg, *supra* note 54, at 133 (2002) ("It is in particular worth noting that in reaching its conclusion, the CFI seems to have tightened the requirements as to the burden of proof which the Commission has to lift. By choosing this approach the CFI has to a large extent been able to avoid having to decide the more substantive question of when the attempt by a manufacturer to prevent re-export by an exclusive distributor must be considered to fall within Article 81(1).").

[63] *Volkswagen*, 2004 O.J. (C 71) 24, ¶ 2.

standing alone, unlawful under the E.C. Treaty.[64] If a manufacturer recommends a retail price and distributors are not compelled or unduly incentivized to sell at that price, such conduct is considered unilateral and therefore outside the scope of conduct prohibited by Article 81(1). Unless it constitutes an abuse of dominant position,[65] unilateral conduct is not proscribed by European competition law.[66] If, however, a manufacturer forms an agreement with a

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[64] *See* Damien Gerard, *"Regulated Competition" in the Automobile Distribution Sector: A Comparative Analysis of the Car Distribution System in the US and the EU*, 24(10) E.C.L.R. 518, 521-22 (2003).

[65] Article 82 of the E.C. Treaty (formerly Article 86) provides:

> Any abuse by one or more undertakings of a dominant position within the common market or in a substantial part of it shall be prohibited as incompatible with the common market insofar as it may affect trade between Member States.
>
> Such abuse may, in particular, consist in:
>
> (a) directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions;
>
> (b) limiting production, markets or technical development to the prejudice of consumers;
>
> (c) applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;
>
> (d) making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

EC TREATY, *supra* note 5, art. 82.

[66] "The case-law also shows that, where a decision of the manufacturer constitutes unilateral conduct of the undertaking, that decision escapes the prohibition in Article 81(1) EC. . ." Judgment of the Court of First Instance of 3 December 2003, Case T-208/01, Volkswagen v. Commission, 2004 O.J. (C 71) 24 ¶ 33 (citing *Bayer* and other precedents). *See also* Judgment of the Court of 6 January 2004, Joined Cases C-2/01 P & C-3/01 P, Bundesverband der Arzneimittel-Importeure v. Bayer, 2004 O.J. (C 59) 2.

distributor to set prices, that conduct may infringe Article 81(1).[67] Such agreement need not be formal to present an antitrust problem; "it is sufficient that the reseller accepts, at least tacitly, the anticompetitive prohibition which the supplier imposes upon him."[68]

The European Commission found that Volkswagen infringed Article 81(1) in setting the resale price of the Passat "on the basis of exhortations to its German authorized dealers to grant limited discounts or no discounts at all to customers in selling the VW Passat."[69] Central to this conclusion was the European Commission's reasoning that the communications, or circulars, Volkswagen sent to its dealers were "to be seen against the background of the contractual relations between Volkswagen AG and its dealers . . . The circulars therefore became part and parcel of the agreements between Volkswagen AG and its authorized dealers, since they are to be regarded as part of a set of continuous business relations based on an existing general agreement (the dealer agreement)."[70]

The European Commission imposed a fine of •30.96 million on Volkswagen for having instructed its dealers in 1996 and 1997 to observe "strict price discipline."[71] Commissioner Monti hailed the decision as "a clear signal that competition policy serves consumers' interests."[72] This statement echoes the E.C. *Guidelines on Vertical Restraints*, which provide that "[t]he protection of competition is the

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[67] *See supra* note 54 for text of Article 81(1).

[68] Case T-43/92, Dunlop Slazenger International Ltd. v. Commission, 1994 E.C.R. II-441, ¶ 60 (though not recorded in writing, efforts of Dunlop subsidiaries to attain price equilibrium across Member States fell within the meaning of agreement or concerted practices.).

[69] Commission Decision of 29 June 2001, on Article 1, Case COMP/F-2/36.693, Volkswagen, 2001 O.J. (L 262) 14, ¶ 125.

[70] *Id.* ¶ 57.

[71] *Id.* ¶ 1.1(1).

[72] Press Release, European Commission, Commission Imposes a •30.96 million Fine on Volkswagen AG for Retail Price Maintenance Measures on the German Market (May 30, 2001), *available at* http://europa.eu.int/rapid/start/cgi/guesten.ksh?p_action.gettxt=gt&doc=IP/01/760|0|AGED&lg=EN&display=.

primary objective of E.C. competition policy, as this enhances consumer welfare and creates an efficient allocation of resources."[73]

However, the CFI annulled the European Commission's *Volkswagen* decision, finding that the European Commission failed to prove the existence of an agreement within the meaning of Article 81(1).[74] Liability under Article 81(1) is premised on finding an anticompetitive agreement:[75] There must be a "concurrence of wills," or meeting of the minds, between at least two parties for conduct to be found unlawful.[76] The CFI wrote, "It follows that the concept of agreement within the meaning of Article 81(1) EC, as interpreted by the case-law, centres around the existence of a concurrence of wills between at least two parties . . . ."[77] The European Commission had argued in defense of its case that the dealers had tacitly accepted Volkswagen's resale price recommendations *in advance* by their initial entry into the manufacturer's distribution network.[78] Rejecting this characterization, the CFI found that a manufacturer's policy recommendations issued after the formation of the formal

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[73] Commission Notice, Guidelines on Vertical Restraints, 2000 O.J. (C 291) 1, § I.2, ¶ 7.

[74] Judgment of the Court of First Instance of 3 December 2003, Case T-208/01, Volkswagen v. Commission, 2004 O.J. (C 71) 24, ¶ 68 (on application for annulment of Commission Decision of 29 June 2001, on a Proceeding under Article 81 of the E.C. Treaty, Case COMP/F-2/36.693, Volkswagen, 2001 O.J. (L 262) 14). ("It follows from all the above considerations that the Commission has not proved, in the contested decision, a concurrence of wills between the applicant and its dealers in relation to the calls at issue. It follow that the contested decision was taken in breach of Article 81(1) E.C. and must therefore be annulled . . ."). As of the date of publication, the CFI's *Volkswagen* decision has yet to be appealed.

[75] *Id.* ¶ 32 ("It follows that the concept of agreement within the meaning of Article 81(1) EC, as interpreted by the case-law, centres around the existence of a concurrence of wills between at least two parties . . .").

[76] *Id.*

[77] *Id.*

[78] *Id.* ¶¶ 39-40.

distribution contract did not, without more, become an integral part of the contract, and could not therefore constitute sufficient evidence of concurrence of wills between the manufacturer and the distributors.[79]

B. *Bundesverband der Arzneimittel-Importeure v. Bayer and Commission*

Bayer involved a lengthy E.C. investigation into Bayer AG's attempts to curtail parallel imports of its various preparations of its drug Adalat, a calcium channel blocker prescribed for cardio-vascular disease.[80] In most member states, national health authorities regulate drug prices, and the prices fixed by government agencies tend to be far lower than corresponding drug prices in unregulated member states.[81] Between 1989 and 1993, prices fixed by authorities in France and Spain were approximately forty percent lower than prices for the same drugs in the United Kingdom.[82] In 1989, wholesalers in Spain took advantage of this discrepancy by overstocking Adalat, selling a portion to the domestic market and then re-exporting their surpluses to the

[79] *Id.* ¶ 45 ("[I]t cannot be accepted that an unlawful contractual variation could be regarded as having been accepted in advance, upon and by the signature of a lawful distribution agreement."). In contrast, the ECJ recently confirmed the imposition of a •90 million fine on Volkswagen for restricting the re-exportation of VW and Audi cars by Volkswagen's Italian dealers. Amongst the means employed by Volkswagen in restricting parallel imports from Italy were the imposition of supply quotas to Italian dealers and a bonus system discouraging them from selling to non-Italian customers. The Court found that Volkswagen had imposed the quotas on Italian dealers for the express purpose of inhibiting re-exports and that by accepting the dealership contract, Italian dealers had consented to these restrictions. As a result, Italian dealers had been incentivized to sell almost exclusively in Italy. Case 388/00, Volkswagen AG v. Commission, 2003 E.C.R. I-0000.

[80] Judgment of the Court of 6 January 2004, Joined Cases C-2/01 P & C-3/01 P, Bundesverband der Arzneimittel-Importeure v. Bayer, 2004 O.J. (C 59) 2, ¶ 1.

[81] *Id.* ¶ 2.

[82] *Id.*

United Kingdom.[83] Wholesalers in France followed suit beginning in 1991.[84] Bayer's U.K. subsidiary lost substantial sales volume as a result of the competition from these parallel imports.[85] Bayer reacted by implementing a unilateral policy aimed at curtailing the gray market in Adalat, one which did not require any action or agreement by its wholesalers.[86] Instead, based on estimates of domestic demand per Member State, Bayer set quantity limits on orders from Spain and France.

Acting on complaints filed by wholesalers about the Bayer policy of limiting the supply of Adalat, the European Commission investigated and issued a decision holding that Bayer had effectively incorporated an export ban into its continuing business relations with its wholesalers in violation of Article 81(1).[87] "According to settled case law, a prohibition against parallel trade within the Community constitutes a restriction of competition."[88] Where a defendant does not occupy a dominant position, however, its policy of preventing parallel imports may be subjected to the Treaty's provisions on competition only if the policy originated from an agreement within the meaning of Article 81(1).[89]

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[83] *Id.* ¶ 3. Independent wholesalers distribute about 90 percent of medicinal products in most Member States. *See* Hans Henrik Lidgard, *Unilateral Refusal to Supply: An Agreement in Disguise*, 18(6) E.C.L.R. 352, 353 n.8 and accompanying text (1997).

[84] *Bayer*, 2004 O.J. (C 59) 2, ¶ 3.

[85] "According to Bayer, sales of Adalat by its British subsidiary, Bayer UK, fell by almost half between 1989 and 1993 on account of the parallel imports, entailing a loss in turnover of DEM 230 million for the British subsidiary, representing a loss of revenue to Bayer of DEM 100 million." *Id.*

[86] Jakobsen & Broberg, *supra* note 54, at 132; Mark Jephcot, *Commentary on Case T-41/96* Bayer AG v. Commission, 22(10) E.C.L.R. 469, 469-476 (2001); *Bayer*, 2004 O.J. (C 59) 2, ¶ 152.

[87] Commission Decision of 10 January 1996, Relating to a Proceeding under Article 85 of the E.C. Treaty, Case 96/478, Bayer AG (Adalat), 1996 O.J. (L 201) 1, 5 C.M.L.R. 416 (1996).

[88] Jakobsen & Broberg, *supra* note 54, at 131.

[89] *Id.* at 131, 140.

The CFI annulled the European Commission's *Bayer* decision on the ground that there was no "agreement or concerted practice" within the meaning of Article 81(1)[90] and the ECJ dismissed the European Commission's appeal finding that, absent extrinsic evidence that the wholesalers concurred in Bayer's efforts to restrict parallel trade, the mere existence of continuous business relations governed by pre-established general agreements was insufficient to imply a concurrence of wills. Bayer argued that the European Commission's case "conceal[ed] an attempt to introduce into Community competition law a general prohibition on any hindrance to parallel imports which is foreign to the system created by Articles [81 and 82] of the Treaty but appears to have been based generally on the objective of achieving the internal market."[91] Though the ECJ did not address this argument in its opinion, the judgment establishes that unilateral efforts by a manufacturer to limit parallel imports will be tolerated or, at least, not prohibited under the competition laws. The European Commission has to prove to the 'requisite legal standard' the existence of an 'agreement' within the meaning of Article 81, and cannot intervene merely because the objective of a particular course of action contravenes E.U. policy on the creation of a single market.

C. Conclusion

The European Commission's capacity to use the competition laws to prohibit restrictions on parallel imports has been dealt a significant blow by *Volkswagen* and *Bayer*. The consumer welfare benefits of parallel trade hailed by Commissioner Monti are not always self-evident, and the European Commission's analysis ignores the welfare-enhancing aspects of vertical restraints, such as limiting free-riding by distributors, promoting inter-brand competition, and protecting intellectual property rights. Various studies have been conducted on the economic impact

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[90] Case T-41/96, Bayer v. Commission, 4 C.M.L.R. 126 (2001).

[91] *Bayer*, 2004 O.J. (C 59) 2, ¶ 139.

of parallel trade. One of the most recent, which considers the findings of other significant studies, is the Organization for Economic Cooperation and Development Synthesis Report.[92] The Synthesis Report concludes that more and better data is needed to determine how parallel imports affect economic welfare.[93] The effects of parallel imports on consumer welfare are dependent on a number of complex factors, and benefit to consumers through lower prices could well be offset by adverse effects.[94]

Volkswagen and *Bayer* are also legally significant because they limit the definition of "agreement" under 81(1). In the name of market integration, the European Commission has traditionally adopted an expansive view of conduct constituting an agreement under Article 81(1).[95] Until

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[92] JOINT GROUP ON TRADE AND COMPETITION, ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT, SYNTHESIS REPORT ON PARALLEL IMPORTS (June 26, 2002), *available at* http://www.olis.oecd.org/olis/2002doc.nsf/43bb6130e5e86e5fc12569fa005d007c/9dc5047a2329c883c1256be400510e2f/$FILE/JT00128903.pdf [hereinafter SYNTHESIS REPORT]. For a more thorough discussion of economic impact studies on parallel trade, see Kimberly Reed, Levi Strauss v. Tesco *and E.U. Trademark Exhaustion: A Proposal for Change*, 23 NW. J. INT'L L. & BUS. 139, 175-82 (2002).

[93] SYNTHESIS REPORT, *supra* note 92, ¶ 4.

[94] See *id.* ¶ 114 (summarizing NERA market research results):

> Parallel traders themselves, especially, and transport were seen as clear gainers from increased parallel trade. However, *the view of the impact on consumers is not clear cut. Consumers were seen at best as slight gainers with a number of adverse effects offsetting price and, perhaps, availability gains*. . . . There was some perception, even amongst the consumer groups, that the benefits through lower prices and, perhaps, greater availability, would be accompanied by adverse effects on after sales services, guarantees and provision of product information. This helps to account for consumers not being seen as clear gainers from additional parallel imports.

(emphasis in original).

[95] *See, e.g.*, Joined Cases 32/78 & 36-82/78, BMW Belgium v. Commission, 1979 E.C.R. 2435, 1 C.M.L.R. 370 (1980); Case 107/82, AEG v. Commission, 1983 E.C.R. 3151, 3 C.M.L.R. 325 (1984); Joined Cases C-25/84 & C-26/84, Ford v. Commission, 1985 E.C.R. 2725, 3 C.M.L.R. 528 (1985); Case T-43/92, Dunlop Slazenger International Ltd. v. Commission,

recently, the ECJ had not acted to limit this trend. In 1990, in *Sandoz prodotti farmaceutici v Commission* ("*Sandoz*"), the ECJ upheld the European Commission's judgment against an Italian pharmaceutical subsidiary that had unilaterally included the words "export prohibited" on its invoices to distributors.[96] Despite the one-sided nature of the company's action and the fact that several distributors did, in fact, re-export the products, the ECJ found an agreement to restrict exports between the manufacturer and its distributors. In marked contrast to *Sandoz*, the CFI's decision in *Volkswagen* and the ECJ's decision in *Bayer* represent refusals to find an agreement in the face of apparently unilateral conduct. Again, however, *Volkswagen* and *Bayer* also highlight the fact that *ex post* judicial review in the European Union may significantly impact a company's ability to defend business practices ultimately found to be legitimate. Thus, these decisions may be cold comfort for companies looking to dampen gray market intra-brand competition, unless they are committed to withstanding a lengthy investigation by the European Commission, and possibly appealing an adverse decision to the European courts. The European Commission shows no sign of relenting.[97]

1994 E.C.R. II-441; Case C-70/93, BMW v. ALD Auto-Leasing, 1995 E.C.R. I-3439, 4 C.M.L.R. 478 (1996).

[96] Pharmaceutical prices, fixed by the Italian Ministry of Health, were substantially lower in Italy than for comparable products in other Member States. This provided the incentive for parallel trade. *Sandoz*, 1987 O.J. (L 222) 28, ¶ 9, *aff'd* Case 277/87, 1990 E.C.R. I-45. For an earlier example of a case finding an agreement between a manufacturer and a distributor to impede imports, see *Ford*, 1985 E.C.R. 2725.

[97] *See* Meller, *supra* note 62 (reporting that Commission spokeswoman Amelia Torres commented that the *Bayer* ruling "would not deter the competition department from pursuing other suspected antitrust behavior by drug companies, and insisted the ruling only reflected a lack of proof.").

IV. E.U. AND U.S. CONVERGENCE IN ANALYZING COORDINATED BEHAVIOR IN MERGER REVIEWS

Conflicting views on the competitive effects of the high profile mergers in *GE/Honeywell*[98] and *Boeing/McDonnell Douglas*[99] have highlighted the potential obstacles for companies navigating merger investigations on both sides of the Atlantic. Such cases are exceptional, but they do reveal differences in the economic principles and policy goals that animate the respective regulatory regimes.

However, in recent years, the European Commission has launched a number of initiatives that should improve consistency in evaluating the benefits and competitive threats of mergers in the European Union and United States. This trend is apparent in recent enforcement efforts on both sides of the Atlantic to address concerns about mergers that may facilitate coordinated behavior in a market. The European Commission's enforcement experience in this area is relatively new, but in applying its "collective dominance" theory to oppose mergers, it has taken a similar approach to the United States in challenging mergers based on "coordinated effects."

In the United States, mergers are reviewed under a standard that seeks to prevent the substantial lessening of competition.[100] In the Federal Trade Commission/Department of Justice *Horizontal Merger Guidelines* "coordinated effects" are defined as "actions by a group of firms that are profitable for each of them only as a

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[98] Commission Decision of 3 July 2001, Declaring a Concentration to be Incompatible with the Common Market and the E.E.A. Agreement, Case COMP/M.2220, GE/Honeywell, 2004 O.J. (L 48) 1.

[99] Commission Decision of 30 July 1997, Declaring a Concentration Compatible with the Common Market and the Functioning of the E.E.A. Agreement, Case IV/M.877, Boeing/McDonnell Douglas, 1997 O.J. (L 336) 16.

[100] The statutory prohibition in Section 7 of the Clayton Act encompasses any acquisition the effect of which "may be *substantially to lessen competition*, or to tend to create a monopoly." 15 U.S.C. § 18 (2000) (emphasis added).

result of the accommodating reactions of the others."[101] In contrast, the European Union's "dominance" test does not explicitly address the threat of coordinated action resulting from increased market concentration as a basis for prohibiting a merger.[102] Since the European Union's "dominance" test is expressed in terms of a single firm's market position, the European Commission had to be more creative in developing a theory to challenge mergers based on the risk of coordination. As discussed further below, the European Union has recently adopted a more expansive test for evaluating mergers that do not create or strengthen a dominant position in the traditional sense, but nevertheless may significantly impede effective competition.

Despite their different origins and labels, when the U.S. agencies assess whether "coordinated interaction" will lessen competition and the European Commission evaluates the prospect of "collective dominance," both are evaluating whether firms in the post-merger world are more likely to act collusively and agree on competitive terms in such a way that harms consumers. However, there are also some important differences in how the theories of "collective dominance" and "coordinated effects" are applied in practice that may lead to divergent results in some cases. These include the role of efficiencies as a counterbalancing factor and the role of the courts in merger enforcement actions.

A. Key Factors Applied By The E.C. And U.S. Enforcement Agencies

As shown in recent cases, both the E.C. and U.S. agencies apply a similar set of factors under a "coordinated effects" or

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[101] *See* MERGER GUIDELINES, *supra* note 33, § 2.1.

[102] Council Regulation 4064/89 of 21 December 1989 on the Control of Concentrations Between Undertakings, art. 2(3), 1989 O.J. (L 395) 1. "Collective dominance" is also a basis for challenging conduct after the fact under Article 82 as an "abuse by *one or more undertakings of a dominant position*." EC TREATY, *supra* note 5, art. 82 (emphasis added); *see* Case T-228/97, Irish Sugar plc v. Commission, 1999 E.C.R. II-2969; Joined Cases C-395/96 P & C-396/96 P, Compagnie Maritime Belge Transports v. Commission, 2000 E.C.R. I-1365.

"collective dominance" analysis in determining whether a proposed merger will lead to tacit collusion. William J. Kolasky, a former deputy assistant attorney general in the Antitrust Division of the DOJ, stated that "the approach . . . appears to be very similar in Brussels to the approach we take here . . . and the factors it considers in determining whether a market is conducive to coordinated interaction are very similar to ours."[103] These include: (1) homogeneous products; (2) highly concentrated markets; (3) stable market demand; (4) prior history of industry collusion;[104] (5) market transparency; (6) frequent and public purchases by buyers; (7) symmetry of costs; and (8) the absence of "maverick" firms to prevent other firms from successfully coordinating.[105]

One area of divergence has been in the treatment of efficiencies as a defense. The United States recognizes that efficiencies may overcome concerns about coordinated effects where the parties demonstrate that such efficiencies are (i) merger-specific; (ii) benefit consumers; and (iii) outweigh the possible anti-competitive effects of the merger.[106] In contrast, until recently, the European Commission has not recognized efficiency claims as a potential mitigating factor in mergers that raise competitive concerns. However, the new E.C.

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[103] William J. Kolasky, Coordinated Effects in Merger Review: From Dead Frenchmen to Beautiful Minds and Mavericks, Address Before the ABA Section of Antitrust Law Spring Meeting, Wash. D.C., (Apr. 24, 2002) at 21, *available at* http://www.usdoj.gov/atr/public/speeches/11050.pdf [hereinafter Kolasky Apr. 24, 2002 Speech].

[104] For a recent U.S. example of the use of prior history of price fixing in a "coordinated effects" challenge to a merger, see the DOJ's opposition to the proposed SGL Carbon, Carbide/Graphite Group merger, *in* Press Release, Department of Justice, Department of Justice Files Suit To Stop SGL Carbon From Acquiring Carbide/Graphite Group's Graphite Electrode Assets (Apr. 15, 2003), *available at* http://www.usdoj.gov/atr/public/press_releases/2003/200954.htm.

[105] *See, e.g.*, MARC IVALDI ET. AL., THE ECONOMICS OF TACIT COLLUSION (Mar. 2003), *available at* http://www.idei.asso.fr/Commun/WorkingPapers/2003/Tacit%20Collusion.pdf; Kolasky Apr. 24, 2002 Speech, *supra* note 103, at 11-21 & fig.11.

[106] *See generally* MERGER GUIDELINES, *supra* note 33, § 4.

Horizontal Merger Guidelines expressly state that efficiencies will be considered in the overall competitive assessment of a merger.[107]

B. Recent U.S. "Coordinated Effects" Cases

1. Union Pacific Co./Southern Pacific Transportation Merger[108]

In 1996, the DOJ opposed the merger of Union Pacific and Southern Pacific, two of the three major rail carriers in the western United States, on the presumption that there would be an increased ability to coordinate rates in markets with only two players.[109] In its administrative review, the Surface Transportation Board ("STB") rejected the DOJ's claim of likely coordinated interaction, advancing a variety of reasons such as the lack of transparency of sales and service data, service (product) heterogeneity, and the widespread use of long-term, individually-negotiated contracts by large shippers.[110] Additionally, the STB found that the elimination of Southern Pacific as an independent competitor was unlikely to increase the probability of coordination post-merger because Southern was a relatively weak bidder for customers.[111] Finally, the STB believed that any possibility of coordination would be offset by substantial efficiencies generated by the merger.[112]

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[107] *See* Commission Notice of 5 February 2004, Guidelines on the Appraisal of Horizontal Mergers under the Council Regulation on the Control of Concentrations Between Undertakings, 2004 O.J. (C 31) 3 [hereinafter E.C. Horizontal Merger Guidelines].

[108] Union Pac. Co./Southern Pac. Transp. Co., No. 32760, 1996 WL 467636 (S.T.B. Aug. 12, 1996).

[109] *See* United States v. Philadelphia Nat'l Bank, 324 U.S. 321 (1963).

[110] *See* Kolasky Apr. 24, 2002 Speech, *supra* note 103, at 13-14 (summarizing the efficiency arguments in this proceeding).

[111] *Id.*

[112] *See Union Pac. Co.*, 1996 WL 467636, at *93 (stating that the merger would generate efficiencies, such as streamlining and

2. *FTC v. H.J. Heinz*

An efficiency analysis was again highlighted in the Federal Trade Commission's ("FTC") 2000 challenge of the Heinz/Beech-Nut merger.[113] Gerber, Heinz, and Beech-Nut were the three major manufactures and distributors of jarred baby food in the United States. Gerber was the largest manufacturer with a market share of sixty-five percent, while Heinz and Beech-Nut held seventeen and fifteen percent, respectively. The FTC sued in the D.C. District Court to enjoin the merger primarily on fears that it would facilitate post-merger coordinated interaction.

The critical issue was whether the merger was a 3-to-2 merger of head-to-head competitors or, instead, a transaction that would actually enhance competition by combining two weak brands into one that could challenge the dominance of Gerber. In its decision to deny the injunction, the district court took the latter view. While acknowledging that a merger creating a duopoly was presumptively illegal,[114] the court found that any anticompetitive effects in this case were offset by substantial efficiencies, such as cost savings based on the consolidation of the two brands, and reductions in distribution costs.

However, the D.C. Circuit reversed the district court decision and enjoined the merger.[115] The D.C. Circuit found that the lower court had erred in ruling that the duopoly presumption of illegality had been rebutted. The court referred to evidence of "past price leadership in the baby food industry"[116] and the transparency of sales data as factors which would make the policing and monitoring of coordinated behavior fairly simple. The court stressed that "extraordinary efficiencies" are needed to offset the likely anticompetitive effects of mergers in highly concentrated

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consolidating operations at major common terminals and combining terminal and station facilities at a number of common points).

[113] FTC v. H. J. Heinz Co., 116 F. Supp. 2d 190 (D.C.C. 2000).

[114] *Id.* at 196-97.

[115] FTC v. H. J. Heinz Co., 246 F.3d 708 (D.C. Cir. 2001).

[116] *Id.* at 724.

markets and no amount of efficiencies could justify a merger to monopoly or near-monopoly.[117] Further, in this case it was questionable whether the efficiencies were merger specific.[118]

3. *United States v. UPM-Kymmene OYJ*[119]

In July 2003, UPM, one of the largest producers of forestry and paper products in the world, sought to purchase MACtac, a seller of bulk labelstock wholly owned by the Bemis Corporation. UPM was parent company to another seller of bulk labelstock, Raflatac, and with this proposed purchase, UPM would hold a twenty-five percent share on the market.

The Northern Illinois District Court focused strongly on the susceptibility of the market to coordination. It found that the merger would leave UPM and Avery Dennison (the largest pressure-sensitive labelstock manufacturer in North America) with seventy percent of the market, which in turn positioned them to suppress competition in the sale and production of pressure-sensitive labelstock. The increase in market concentration, product homogeneity, transparency of sales data (including prior detection of undercutting within the industry), and the fact that UPM was a major supplier of raw materials to Avery were important factors in the court's analysis. Additionally, the court noted that if Raflatac acquired MACtac, it would control MACtac's excess production capacity. With two suppliers controlling seventy percent of the market post-merger and much of the industry's excess capacity, the court found it probable that Raflatac/MACtac would be able to raise prices over the long term.[120] Finally, the court found that none of the smaller

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[117] *Id.* at 720.

[118] *Id.* at 721-22.

[119] United States v. UPM-Kymmene OYJ, No. 03-C2528, 2003 WL 21781902 (N.D. Ill. July 25, 2003).

[120] The DOJ presented evidence that MACtac's CEO, who was chosen to lead UPM's labelstock business, told an analyst that the merger would bring pricing "discipline" to UPM. *See* Deborah Platt Majoras, Vigorous Antitrust Enforcement Covering the Waterfront: An Update from the

competitors could effectively take market share from Raflatac, MACtac, and Avery, and they would have the incentive to follow their lead in price increases. Taking all these factors into account, the court enjoined the proposed merger.[121]

C. "Collective Dominance" in E.U. Merger Control

The European Commission first used "collective dominance" to evaluate the Nestlé/Perrier merger in 1992.[122] It subsequently prohibited the Gencor/Lonrho transaction in 1996 on "collective dominance" grounds.[123] To date, the most

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Antitrust Division, Address Before the State Bar of California, Antitrust and Unfair Competition Law Section (Oct. 23, 2003) at 5, *available at* http://www.usdoj.gov/atr/public/speeches/201435.pdf. Most recently, in its April 1, 2004, complaint to enjoin Arch Coal, Inc.'s $364 million acquisition of the Triton Coal Company frpm New Vulcan Coal Holdings, L.L.C., the FTC has alleged that the merger risks unlawful coordinated effects based inter alia on various public statements made by top management of the merging and "competing" companues allegedly seeking to curtail industry outpu in the relevant market until prices increased. *See* Press Release, Fed. Trade Comm'n, FTC files Federal Complain Challenging Arch Coal's Proposed Acquisition of Triton Coal Company (Apr. 1, 2004), *available at* http://www.ftc.gov/opa/2004/04/archcoal.htm. Six states, Missouri, Arkansas, Illinois, Iowa, Kansas, and Texas, have also sued to enjoin this transaction based on the same coordinated effects theory. See Press Release, Missouri Attorney General's Office, Nixon Leadss Six-State Effort to Block Proposed Merger of Major Producers of Coal Used to Generate Electricity (Apr. 1, 2004), available at http;//ago.missouri.gov/newsreleases/2004/040104.htm.

[121] For a recent example of the FTC closing an investigation where the empirical evidence did not support a "coordinated effects" theory of harm, see Federal Trade Commission, Statement Concerning Royal Caribbean Cruises, Ltd./P&O Princess Cruises plc and Carnival Corporation/P&O Princess Cruises plc (Oct. 4, 2002) *available at* http://www.ftc.gov/os/2002/10/cruisestatement.htm.

[122] Commission Decision of 22 July 1992, Relating to a Proceeding Under Council Regulation No. 4064/89, Case IV/M.190, Nestlé/Perrier, 1992 O.J. (L 356) 1.

[123] In its 1999 *Gencor v. Commission* ruling, the CFI affirmed the European Commission's decision to block a proposed merger in the platinum industry based on the feasibility of "tacit collusion," where the merger would have resulted in two major platinum producers controlling

significant merger case involving "collective dominance" is the CFI's June 6, 2002, *Airtours v. Commission*[124] decision where, for the first time, the CFI annulled an E.C. decision to prohibit a merger.

On September 22, 1999, the European Commission blocked a proposed hostile takeover by Airtours of First Choice, the second- and fourth-largest U.K. "short-haul" holiday package operators, on the ground that the merged entity would enjoy a collectively dominant position with two other leading operators in the U.K. market for "short-haul" package holidays. The European Commission prohibited the merger after concluding that the three leading providers would be able to coordinate their behavior by restricting the supply of capacity, and small independent operators would be further marginalized, ultimately raising prices for British travelers.[125]

The CFI agreed with the European Commission's use of a "collective dominance" theory in merger reviews and laid down the standard for blocking a merger based on "collective dominance." However, the CFI stated that the European Commission had failed to meet its burden with "convincing evidence."[126] In its decision, the CFI stated that there are three prerequisites to establish "collective dominance": (1) "sufficient market transparency"; (2) "adequate deterrents to

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more than seventy percent of the market worldwide. Case T-102/96, Gencor v. Commission, 1999 E.C.R. II-753; *see also* Cases C-68/94 & 30/95, France v. Commission, 1998 E.C.R. I-1375 (ECJ confirmed that the Merger Regulation applies to "collective dominance").

[124] Case T-342/99, Airtours v. Commision, 2002 E.C.R. II-2585.

[125] EUROPEAN COMMISSION, DIRECTORATE-GENERAL FOR COMPETITION, EUROPEAN UNION COMPETITION POLICY, XXXIIND REPORT ON COMPETITION POLICY 52 (2002), *available at* http://europa.eu.int/comm/competition/annual_reports/2002/report_short_en.pdf [hereinafter 2002 ANNUAL REPORT].

[126] *Airtours*, 2002 E.C.R. II-2585, at ¶ 63 ("The evidence must concern, in particular, factors playing a significant role in the assessment of whether a situation of collective dominance exists, such as . . . the lack of effective competition between the operators alleged to be members of the dominant oligopoly and the weakness of any competitive pressure that might be exerted by other operators.").

ensure that there is a long-term incentive in not departing from the common [anticompetitive policy]; and that (3) the reaction of actual and potential competitors and consumers "would not jeopardise the results expected from the common policy."[127] However, the CFI concluded that "far from basing its prospective analysis on cogent evidence, [the European Commission's decision was] vitiated by a series of errors of assessment as to factors fundamental to any assessment of whether a collective dominant position might be created."[128] In particular, the European Commission had not shown that the process by which Airtours and other tour operators reserved resort space for travelers was transparent and that output could be increased quickly to act as a credible punishment scheme.[129] The CFI also pointed to the history of competition and low entry barriers in this market.[130]

Although *Airtours* highlights the substantive similarities between "collective dominance" and "coordinated effects," it also illustrates that judicial review, more than two years after the fact, effectively allowed the European Commission to be the judge, jury, and prosecutor in its own case. In the United States, the agencies must go to court and demonstrate likely harm from a merger to obtain a court order prohibiting the transaction. By contrast, the European Commission is authorized to block a merger without judicial intervention and, as *Airtours* demonstrates, it may take several years to appeal an adverse decision before the CFI under the normal review process.[131] Even if the parties

[127] *Id.* ¶ 62.

[128] *Id.* ¶ 294.

[129] *Id.* ¶¶ 173, 203.

[130] The CFI relied on findings in a 1997 United Kingdom Monopolies and Mergers Commission report that the market was competitive and entry barriers were low. *Id.* ¶¶ 93-101.

[131] In 2000, a "fast-track" procedure was implemented to hasten the judicial review process and both the Case T-310/01, Schneider v. Commission, 2002 E.C.R. II-4071, and Case T-5/02, Tetra Laval v. Commission, 2002 E.C.R. II-4381 decisions were reviewed by the CFI under the "fast-track" procedure within a year's time. *See* 2002 ANNUAL REPORT, *supra* note 125, at 51, 53-54.

ultimately prevail, they usually have little hope of resurrecting their merger at this stage. As one DOJ official has observed "the most important differences that remain . . . in this area relate not to the analytical framework we use, but to process issues."[132]

D. E.U. Merger Reform

Following an in-depth review and consultation process, the European Commission adopted significant reforms to E.U. merger law including a new substantive standard for assessing the legality of mergers in the European Union. The new E.U. merger regulation—effective May 1, 2004—expands the scope of merger review beyond the traditional "dominance" test [133] to prohibit mergers that would "significantly impede effective competition . . . ."[134] The new test is intended to deal with situations of "non-collusive oligopoly" where a merger may reduce competition, even though it does not result in single firm or collective dominance, and thus addresses a perceived "gap" in E.U. merger enforcement.[135] The expanded scope of E.U. merger control may result in more merger challenges akin to *Airtours* since the European Commission is no longer required to establish single firm or collective dominance as grounds for prohibiting a merger.

To help provide legal certainty to the business community, the European Commission has also published *Horizontal Merger Guidelines* that are generally consistent with the U.S. model. The *Guidelines* clarify that mergers in

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[132] Kolasky Apr. 24, 2002 Speech, *supra* note 103, at 23. *See also* Patterson & Shapiro, *supra* note 37, at 21-23; Stephen M. Axinn, *In Search of Convergence between Legislative Purpose and Administrative Policy*, 2003 COLUM. BUS. L. REV. 431, 433-34 (2003).

[133] Council Regulation 139/2004 of 20 January 2004 on the Control of Concentrations Between Undertakings, 2004 O.J. (L 24) 1, 4.

[134] *Id.* art. 2(3).

[135] *See* Mario Monti, Competition Enforcement Reforms In the EU: Some Comments by the Reformer, Address Before Georgetown University, Washington, D.C. (Apr. 4, 2003), *available at* http://europa.eu.int/comm/competition/speeches/index_2003.html.

"oligopolistic markets," can now be challenged under the "significant impediment to competition" test "even where there is little likelihood of coordination between the members of the oligopoly."[136] Also, the *Guidelines* bring the European Union into line with the U.S. model by specifying that efficiencies will be considered in the overall assessment of a proposed merger.[137] The European Commission recognizes that in the case of mergers raising non-collusive oligopoly or "collective dominance" concerns, evidence of efficiencies that will strengthen a merged firm's incentives to increase output and reduce prices, may make successful coordination more difficult.[138] As in the United States, the burden of proof will be on the merging parties to demonstrate that claimed efficiencies are merger specific and verifiable.[139] However, "the devil is in the details," and it remains to be seen whether companies can successfully assert an efficiencies defense to overcome non-collusive oligopoly or "collective dominance" concerns.

In sum, U.S. and E.U. law is converging in this substantive area and both the E.C. and U.S. enforcement agencies seem to be analyzing the same set of factors likely to increase "coordinated effects" or "collective dominance." However, "[w]hat matters, of course, is how these factors are applied in practice,"[140] especially in light of the European Union's new, and more expansive, standard for reviewing potentially anticompetitive mergers. Given this new development and the differences in the scope of judicial review and the fact specific inquiries required to validate claimed efficiencies, the possibility for divergent outcomes still remains.

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[136] E.C. Horizontal Merger Guidelines, *supra* note 107, ¶ 25.

[137] *Id.* ¶¶ 76-88.

[138] *Id.* ¶ 82.

[139] *Id.* ¶¶ 85-88.

[140] Kolasky Apr. 24, 2002 Speech, *supra* note 103, at 21.

E. Conclusion

This quick comparison between U.S. antitrust law and E.U. competition law reveals both substantive convergence and persistent areas of divergence. Judge Wood raises interesting historical reasons that may explain *why* such divergence continues to exist, and what the implications might be for future U.S. antitrust policy. At the day-to-day business level for American corporations, however, one fact is certain: divergence in important aspects of U.S. antitrust and E.U. competition policy will continue to affect U.S. corporations as the European Union expands eastward and brings new markets within its reach, and as other countries adopt competition regimes modeled on the European Union's experience.