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# **Article 82 Guidance: A Closer Look at the Analytical Framework and the Paper's Likely Impact on European Enforcement Practice**

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The new Guidance Paper on the European Commission's enforcement priorities in applying Article 82 EC Treaty to abusive exclusionary conduct by dominant undertakings<sup>1</sup> constitutes a major step in European antitrust enforcement. The present paper reviews the Guidance Paper's general approach to dominance and anticompetitive foreclosure (Section 1) and assesses its likely impact on future Article 82 enforcement (Section 2). Concluding considerations relevant for dominant companies and potential complainants are set out at the end (Section 3).<sup>2</sup>

**I. DOMINANCE AND ANTICOMPETITIVE FORECLOSURE**

***A. Recalibration of the Concept of Dominance***

The Guidance Paper condenses the notion of dominance to the formula that dominance requires the company in question to enjoy "substantial market power over a period of time."<sup>3</sup> Two years will normally be sufficient, but shorter or longer periods may

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<sup>1</sup>Made available on December 3, 2008 on the Commission's website <http://ec.europa.eu/competition/antitrust/art82/guidance.pdf>. The final authoritative text will be published in the *Official Journal* at a subsequent date.

<sup>2</sup>A general overview of the new Guidance Paper is provided in a client advisory published by Arnold & Porter LLP, which is available at [http://www.arnoldporter.com/resources/documents/CA\\_EuropeanCommissionEndorsesMoreEconomicBasedApproach\\_121908.pdf](http://www.arnoldporter.com/resources/documents/CA_EuropeanCommissionEndorsesMoreEconomicBasedApproach_121908.pdf).

<sup>3</sup>Guidance Paper, paragraph 10.

be looked at depending on the circumstances of each case.<sup>4</sup> Substantial market power exists if the company in question does not face effective competitive constraints from existing competitors, the threat of expansion of competitors or entry of new competitors, countervailing buyer power, or other sources.<sup>5</sup>

Under a new “soft safe harbor” rule, companies with a market share below 40 percent are generally unlikely to be dominant.<sup>6</sup> Above 40 percent, the Guidance Paper expresses an increased openness to accept that high market shares do not necessarily indicate dominance. Market shares are characterized as a “useful first indication” of the market structure, but more important are the relevant market conditions, dynamics of the market, product differentiation, and development of market shares over time.<sup>7</sup> The Guidance Paper also does not suggest that dominance is highly likely to be present when market shares exceed 50 percent.<sup>8</sup> At least on its face, the Guidance Paper therefore increases the chances of companies with significant market shares to escape a finding of dominance.

### ***B. Anticompetitive Foreclosure as the Key Concept of Exclusionary Abuse***

The overreaching abuse concept for all types of exclusionary conduct is that the conduct must lead to “anticompetitive foreclosure,” a notion newly introduced by the Guidance Paper. It contains two aspects: (i) foreclosure, which occurs when the dominant

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<sup>4</sup>Guidance Paper, paragraph 11 with footnote 6.

<sup>5</sup>Guidance Paper, paragraph 12.

<sup>6</sup>Guidance Paper, paragraph 14.

<sup>7</sup>Guidance Paper, paragraph 13.

<sup>8</sup>The 50 percent presumption of dominance is, however, supported by court precedent. *See* ECJ, judgment of 3 July 1991, C-62/86, *AKZO Chemie v. Commission*, [1991] ECR I-3359, paragraph 60.

company makes access to customers<sup>9</sup> more difficult or impossible for actual or potential rivals; and (ii) consumer harm resulting from this foreclosure.<sup>10</sup>

## **1. The Relevance of Consumer Harm**

The focus on consumer harm is the cornerstone of the Guidance Paper. During its preparation, there had been significant controversy about whether an abuse can be found on the basis alone that the behavior has a significant negative impact on market structure (or the process of competition)—as the European courts and the Commission have suggested in past cases—<sup>11</sup> or whether evidence of (likely) consumer harm is required in addition.

The Guidance Paper adopts a middle ground. It postulates that the Commission will focus its enforcement efforts on exclusionary conduct that leads to consumer harm. But the Guidance Paper’s analytical framework fudges the issues of foreclosure and consumer harm. Its key paragraph 20 lists the factors that will generally be relevant for establishing “anticompetitive foreclosure” without identifying factors that would speak to the question of foreclosure and those that would speak to the question of consumer harm. These factors are: (i) the position of the dominant company (notably its market share); (ii) barriers to entry and expansion and other relevant market conditions; (iii) the position (and notably the market shares) of the dominant company’s competitors; (iv) the position

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<sup>9</sup>The Guidance Paper acknowledges that anticompetitive foreclosure can also result if competitors are foreclosed from access to inputs (rather than from access to customers). However, input foreclosure is more fully discussed only in the Guidance Paper’s section on refusal to supply and mentioned in footnote 23 in the context of exclusive supply obligations.

<sup>10</sup>Guidance Paper, paragraph 19.

<sup>11</sup>See ECJ, judgment of 15 March 2007, C-95/04 P, *British Airways v. Commission*, [2007] ECR I-2331, paragraphs 106 and 107.

of the customers or input suppliers; (v) the extent of the allegedly abusive conduct, notably the duration of the conduct and the percentage of total market sales affected by it; (vi) possible direct evidence of actual anticompetitive foreclosure, such as an increase of the dominant firm's market share or market exit or failed entry of competitors; and (vii) direct evidence of an exclusionary strategy.<sup>12</sup>

Arguably, all of these factors could be part of a traditional market structure analysis. The Guidance Paper does not require separate evidence that the conduct in question has led, or is likely to lead to price increases, less consumer choice, or less innovation, although this would constitute the most direct manifestation of consumer harm. Perhaps surprisingly, paragraph 20 does not even list these factors as being part of the general analysis of anticompetitive foreclosure. The Guidance Paper therefore leaves the Commission significant flexibility to infer consumer harm from the conduct's negative impact on market structure. This means, for example, that a dominant company is unlikely to escape a finding of abuse simply because the Commission has not established by direct evidence that a negative price impact has resulted, or is likely to result from the dominant company's behavior.

## **2. As Efficient Competitor Test and Efficiency Defense**

Consumer harm provides, however, the conceptual underpinning for two important assessment elements that the Guidance Paper explains in some detail: the "as efficient competitor test" and the "efficiency defense."

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<sup>12</sup>Additional factors are relevant for specific types of abuses, but, again, the Guidance Paper discusses them mostly under a combined heading of "anticompetitive foreclosure". It is only for refusal to supply cases that the Guidance Paper sets out a clear two-step analysis of foreclosure (elimination of effective competition on the downstream market, paragraph 84) and consumer harm (paragraph 85-87).

Under the “as efficient competitor” concept, a dominant company’s pricing conduct is not normally seen as leading to consumer harm—and the Commission therefore is not likely to intervene—if it forecloses only actual or hypothetical rivals that are less efficient than the dominant firm.<sup>13</sup> The test compares the dominant company’s costs and sales prices for the products in question. If the sales prices are above the long-run average incremental cost (“LRAIC”),<sup>14</sup> then equally efficient rivals are not normally foreclosed. If sales prices are below LRAIC, anti-competitive foreclosure has to be assessed in more detail and becomes likely if the dominant company’s prices are below its average avoidable cost (“AAC”).<sup>15</sup>

Under the “efficiency defense,”<sup>16</sup> which parallels Article 81(3) EC Treaty, there is no net consumer harm, and hence no reason for the Commission to intervene, if (i) identifiable efficiencies result from the conduct; (ii) the conduct is indispensable to the realization of these efficiencies; (iii) the efficiencies outweigh any negative effects on competition and consumer welfare resulting from the conduct;<sup>17</sup> and (iv) the conduct does not eliminate effective competition by removing all or most existing sources of actual or potential competition—which would be the case if the exclusionary conduct maintained,

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<sup>13</sup>Guidance Paper, paragraph 22.

<sup>14</sup>LRAIC is the average of all the (variable and fixed) costs that a company incurs to produce a particular product, and often will correspond to average total cost (Guidance Paper, footnote 18).

<sup>15</sup>AAC is the average of the costs that could have been avoided if the company had not produced the extra output to which the conduct in question relates. Often, AAC will correspond to average variable costs (Guidance Paper, footnote 18). For conditional rebates, paragraphs 40 *et seq.* of the Guidance Paper set out more specific rules for the calculation of AAC and LRAIC.

<sup>16</sup>Guidance Paper, paragraphs 29 *et seq.*

<sup>17</sup>It is arguably in the context of this balancing that evidence on direct manifestations of consumer harm or benefit will become most relevant. Regrettably, the Guidance Paper does not provide any guidance about how to carry out this balancing exercise.

created, or strengthened a market position approaching that of a monopoly.<sup>18</sup> The recognition of an efficiency defense in Article 82 cases marks a major development. Not too many years ago, the prevailing view was that Article 82 left no room for an efficiency defense.

### **3. Standard of Proof and Type of Evidence**

The Guidance Paper requires “cogent and convincing” evidence for a finding of anticompetitive foreclosure.<sup>19</sup> However, it primarily anticipates the use of qualitative evidence, allowing quantitative evidence where this is “possible and appropriate.”<sup>20</sup> This rather cautious endorsement of quantitative evidence leaves the Commission considerable flexibility to base its findings on whatever evidence is available in a specific case. While the use of econometric analysis will certainly play an important role in future Article 82 enforcement, at present it cannot be expected that cases will systematically be decided by complex econometric studies.

Overall, the Guidance Paper does not break with prior abuse analysis, and some may criticize that it does not go far enough.<sup>21</sup> But the emphasis on consumer harm constitutes a significant step forward in bringing the Commission’s enforcement practice more in line with economic theory and international enforcement practice. On the basis of this conceptual underpinning, the Guidance Paper also provides a more coherent overall

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<sup>18</sup>Guidance Paper, paragraph 29, sub-paragraph four. The Guidance Paper does not set a maximum market share level that would normally preclude the efficiency defense.

<sup>19</sup>Guidance Paper, paragraph 20.

<sup>20</sup>Guidance Paper, paragraph 19.

<sup>21</sup>For example, it may be argued that the Guidance Paper departs from the consumer harm paradigm by not requiring recoupment in predatory pricing cases. Absent recoupment, it can be argued that consumers obtain a net benefit from the dominant company’s below-cost pricing.

framework of analysis, something that many practitioners have called for in light of a number of diverging Commission decisions and European court judgments. Moreover, the emphasis on consumer harm coincides with a more explicit recognition of the consumer benefits that can result from fierce competition on the merits by dominant companies.

## **II. IMPACT ON ARTICLE 82 ENFORCEMENT PRACTICE**

The Guidance Paper emphasizes that it does not seek to state the law but to explain the criteria according to which the Commission is likely to decide whether to investigate a specific exclusionary conduct case as a matter of enforcement priority.<sup>22</sup> Accordingly, the Guidance Paper does not produce any legally binding effects. Against this background, it can be expected that it will impact the enforcement practice of EU and Member State courts and authorities to a different extent.

### ***A. Commission***

The Commission can be expected to follow the Guidance Paper's approach wherever possible, in order to enhance legal certainty and predictability of its enforcement action. Also, the Guidance Paper's persuasiveness vis-à-vis other European competition law enforcers will, to a significant extent, depend on its consistent and successful application by the Commission.

Where a case does not meet the Guidance Paper's prioritization criteria but could arguably violate Article 82 EC Treaty, EU law normally grants the Commission the necessary discretion to not intervene.<sup>23</sup> However, it is clear that the Guidance Paper does

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<sup>22</sup>Guidance Paper, paragraphs 2 and 3.

<sup>23</sup>CFI, judgment of 18 September 1992, T-24/90, *Automec v. Commission*, [1992] ECR II-2223.



not aim to reduce the Commission's enforcement efforts.<sup>24</sup> In December 2008 and January 2009 alone, significant procedural steps were taken in cases against EdF (Statement of Objections for alleged exclusionary conduct on the French electricity market), RWE (market testing of commitments in a case alleging exclusionary conduct on the German gas supply markets), Microsoft (Statement of Objections for alleged tying of its Internet Explorer web browser to the Windows operating system), and Standard & Poor's (formal initiation of proceedings for alleged levy of licensing fees from financial institutions for use of US International Securities Identification Numbers).

### ***B. European Court of Justice (ECJ) and Court of First Instance (CFI)***

In annulment actions against Commission infringement decisions, the CFI (and, on appeal, the ECJ) may have little opportunity to criticize the approach suggested in the Guidance Paper to the extent that this approach generally matches or exceeds the requirements for a finding of abuse set by court precedent. If there are specific situations for which existing case law sets stricter requirements than the Guidance Paper, the Commission may well be able to find a way to incorporate such additional factors in its decision, so that it would withstand court scrutiny. There may be a greater possibility for divergence with the Guidance Paper if the ECJ has to decide questions referred to it by Member State courts under the preliminary ruling procedure of Article 234 EC Treaty. Commission officials hope that the Court will endorse the Commission's approach; they

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<sup>24</sup>In the Commission press release on the publication of the Guidance Paper (IP/08/1877), Commissioner Kroes states that the Guidance Paper "should leave dominant undertakings in no doubt that they will find the Commission in their way wherever their conduct risks increasing prices, limiting consumer choice or dissuading innovation."

refer to previous instances where that has been the case when the Commission developed the interpretation of EU competition law beyond established paths.<sup>25</sup>

### *C. National Competition Authorities (NCAs)*

The Member States' NCAs were closely involved in the preparation of the Guidance Paper, and the Commission expects them to generally follow its approach when applying Article 82 EC Treaty. However, a risk of divergence persists in two respects.

First, not all Member States have fully endorsed the move towards a more economics-based approach. The president of the German Federal Cartel Office, Dr. Bernhard Heitzer, stated only a few days prior to the publication of the Guidance Paper:

However, the risk of divergence is real. [...] [I]n its Priority Paper [the Commission] focuses very heavily, at times exclusively, on a *consumer welfare approach*—which is not in line with European jurisprudence [...] If the proof of harm to consumers were to become a central criterion for instituting proceedings in the future—this would lead to highly complex examinations. Consequently, abuse control would fail in view of this excessive demand for proof.<sup>26</sup>

Statements like these suggest that some Member State authorities may deviate from the Guidance Paper or apply it differently than the Commission would. The Commission will seek to avoid conflicts by closely coordinating with NCAs in specific cases, as is foreseen in Article 11 Regulation 1/2003 and the Commission's Network

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<sup>25</sup>For example, the Court accepted in joined cases C-68/94 and C-30/95, *Kali+Salz*, [1998] ECR I-1375 the Commission's application of the dominance test of the old Merger Regulation (before the 2004 revision) to situations of collective dominance, although it was disputed at the time whether this would be possible.

<sup>26</sup>Statement at the European Competition Day in Paris, 18-19 November 2008, available at [http://www.bundeskartellamt.de/wDeutsch/download/pdf/Diskussionsbeitraege/081127\\_ECD\\_Paris.pdf](http://www.bundeskartellamt.de/wDeutsch/download/pdf/Diskussionsbeitraege/081127_ECD_Paris.pdf), pages 5-6. (Emphasis in the original.) See also Dr. Bernhard Heitzer, Statement delivered at the CRA International Annual Conference of 3 December 2008 (available at [http://www.bundeskartellamt.de/wDeutsch/download/pdf/Diskussionsbeitraege/081203\\_CRA.pdf](http://www.bundeskartellamt.de/wDeutsch/download/pdf/Diskussionsbeitraege/081203_CRA.pdf)), page 8: "As an economist, I am far from disputing that the [consumer] welfare standard currently provides the only suitable point of reference for sound *theoretical* analysis. But if you consider only some of the issues connected with making this concept operational, strong doubts arise as to whether it is a good *practical* point of reference for enforcement practice." (Emphasis in the original.)

Notice.<sup>27</sup> But it is questionable whether the Commission would use its powers under Article 11(6) Regulation 1/2003 and take a case away from an NCA that is about to adopt a decision that would conflict with Commission policy. The Commission has not used this power in the past and has agreed to invoke it only under limited circumstances,<sup>28</sup> which are not likely to be present as long as the NCA can base an intended Article 82 decision on ECJ jurisprudence.

Second, some Member States' national laws against unilateral conduct continue to be stricter than Article 82 EC Treaty. For example, the German rules can apply to companies that are not dominant in the sense of the Guidance Paper and to exclusionary behavior that does not meet all requirements set in the Guidance Paper. Notably, specific proof of consumer harm has not in the past played a prominent role in the German enforcement practice. Accordingly, it is at least conceivable that, where national law so permits, an NCA not agreeing with the Guidance Paper might base an infringement decision on national law rather than on Article 82 EC.

#### *D. Member State Courts*

Member State courts play an important role in applying Article 82 EC Treaty, notably in the context of private litigation. But even more so than with regard to Member State authorities, it is presently uncertain to what extent the Guidance Paper will influence the decisional practice of Member State courts. Courts may be inclined (and find it more convenient to the extent this facilitates their decision making) to follow ECJ

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<sup>27</sup>Commission Notice on cooperation within the Network of Competition Authorities, 2004 O.J. C 101/43.

<sup>28</sup>Commission Notice on cooperation within the Network of Competition Authorities, 2004 O.J. C 101/43, paragraph 54.

and CFI precedent rather than a non-binding expression of the Commission's enforcement priorities. The Commission has no powers similar to those of Article 11(6) of Regulation 1/2003 vis-à-vis Member State courts and very limited "soft" tools to influence national judges.

### **III. CONCLUSIONS FOR POTENTIALLY DOMINANT COMPANIES AND COMPLAINANTS**

Companies doing business in Europe will benefit from the fact that there is now a single document that lays out the Commission's approach to exclusionary conduct. Overall, this improves legal certainty and predictability of the Commission's likely enforcement action. The Guidance Paper also provides wider opportunities to companies with significant market shares to defend themselves against a finding of infringement. At the same time, it raises the bar for would-be complainants, who, in the future, will have to bring significant evidence of anticompetitive foreclosure; evidence showing the foreclosure of the complainant will not suffice.

Despite these improvements, potentially dominant companies will continue to face significant uncertainty when self-assessing the risk that a specific commercial conduct could be seen as exclusionary abuse. The Guidance Paper often requires complex analysis and, in part, reliance on information that companies often will not be able to establish with a high degree of certainty.<sup>29</sup> Moreover, the Guidance Paper grants the Commission significant flexibility not only regarding the type of evidence it will look at,

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<sup>29</sup>For example, in the area of exclusionary rebates, it may be difficult to determine the "effective price," the "relevant range," and "contestable shares" that are relevant for the calculation of AAC and LRAIC. Also, dominant companies may face difficulties in carrying out a self-assessment of the efficiency defense.

but also regarding the weight to be attributed to the various factors that are part of the assessment. There are very few bright line rules.

Even if potentially dominant companies adjust their commercial behavior to the Guidance Paper, and thereby minimize the risk of Commission intervention, there remains a significant possibility that Member State authorities or courts might adopt a stricter approach to Article 82 EC Treaty or seek to apply stricter national rules. It remains to be seen whether this risk will decrease over the coming years. For the time being, complainants might seek to take advantage of the situation by approaching the Commission and some potentially more interventionist Member State authorities in parallel.

Finally, the Guidance Paper reduces the international divergence of the rules against unilateral conduct. But significant differences remain. In the United States, the report on single-firm conduct under Section 2 of the Sherman Act, which the U.S. Department of Justice ("DOJ") published in September 2008,<sup>30</sup> sets considerably higher substantive requirements before the DOJ is prepared to intervene against unilateral conduct. Even though the practical relevance of the DOJ paper may be limited under the new Obama administration and, also, because the U.S. Federal Trade Commission distanced itself from the paper, differences between the U.S. enforcement practice and the European practice will remain for the foreseeable future. In addition, the Canadian Competition Bureau in January 2009 launched a review of the Canadian rules against unilateral conduct,<sup>31</sup> and China and other jurisdictions are still defining their approach.

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<sup>30</sup> Available at <http://www.usdoj.gov/atr/public/reports/236681.pdf>.

<sup>31</sup> Available at <http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/02942.html>.

Accordingly, companies with high market shares will continue to face significant difficulty in defining a single commercial worldwide strategy that best serves their commercial interests and respects antitrust rules in different jurisdictions. Complainants have the possibility of forum shopping. Compared to other available possibilities, lodging a complaint with the European Commission continues to be a relatively inexpensive and promising way of action against allegedly exclusionary conduct of a dominant company. Complaints to the Commission by globally active U.S. companies against other globally active U.S. companies, such as a complaint lodged by T3 Technologies Inc. against IBM in January 2009, appear to confirm this approach.