

SYMPOSIUM ON COMPETITION POLICY

DENIS CAGNEY

Matheson, Ormsby and Prentice, Dublin

(read before the Society, 3 March 1994)

1. INTRODUCTION

Competition policy can be a fascinating topic, particularly for those with an economic or legal frame of mind. This same intellectual fascination can also be a pitfall. One can easily be drawn into conceptual minefields when all a client wants to know is "Can I go ahead with this joint venture or is there some competition problem?" Or "Is my rival engaging in predatory pricing or is he staying within the rules of the game?" The list is endless. The last thing the client wants to hear is: "Well there are different schools of thought on this issue...."!

Perhaps the single biggest challenge facing competition policy-makers is to enable business operate in a climate of reasonable certainty while developing a consistent body of rules on what can sometimes be very difficult questions. In Ireland, policy really only emerges through individual cases because of the Competition Act, 1991. This does not help matters.

There will always be some uncertainty in living with the competition rules. But we should keep it to the minimum necessary.

2. THE OBJECTIVES OF COMPETITION POLICY

Efficiency

Underlying any competition policy is a belief in the economic virtues of the marketplace. The free operation of market forces is seen as the best way of ensuring efficiency in the allocation and distribution of resources, adaptation to change and, ultimately, maximisation of consumers' welfare.

Fairness

There is also an underlying concern to ensure *fairness*. This latter can be a rather subjective and elusive concept.

Personally, I feel that a concern with fairness must always be present, certainly in considering competition policy *at national level*. The European Commission can

concentrate on the broad policy considerations which are thrown up by individual cases. But there must be some recourse available to an aggrieved party, no matter how economically insignificant the case. Otherwise, the law will not command respect. This is why I am not at all enthusiastic about introducing a *de minimus rule* in the Irish law.

EU - Market Integration

The European Union competition rules have the additional and unique mission of promoting the integration of national markets into a single market. This unique mission of the EU rule has influenced, I think, the structure of the EU rules. What is best for the EU may not necessarily be the best model for a small homogeneous economy like Ireland. This is *not* an argument for complacency or doing nothing!

3. THE EUROPEAN UNION INFLUENCE

It is remarkable the extent to which the European Union has determined the operation of competition policy in Ireland. Mostly we had no choice in the matter: we had to comply with Directives, etc. With the Competition Act we *chose* to follow the EU model of anti-trust law.

We can set out three broad principles which derive from the Treaty:

1. Markets should be opened up.
2. Markets should be kept open
3. Where market distortions are allowed (e.g. State aid) the criteria allowing such distortions should be agreed and transparent in advance.

In recent years, we have also seen a whole wave of EU measures designed essentially to achieve 1. above and complete the internal market. I am thinking particularly of:

The Public Procurement Rules

The market for contracts in a public sector in the EU is vast - up to 15 per cent of the Union's GDP. In 1985, the Commission estimated that only 2 per cent of public contracts actually cross Community frontiers. The single market programme for opening public procurement markets was completed in 1993. All contracts for works, supplies and services above certain thresholds must now be advertised in the Official Journal and awarded on strictly commercial criteria. New rules on ensuring

that adequate remedies are in place for persons who are aggrieved by failure to respect the rules are in place.

In my experience public authorities have become very aware of the need to be seen to observe both the letter and the spirit of the EU rules.

It is interesting to note in passing that the *OECD* in a recent study on *Competition Policy in Ireland* found that Irish manufacturing value added is relatively concentrated in those sectors which stand to be most affected by the elimination of intra EEC non-tariff barriers, most notably those operating in public procurement markets (e.g. office machines, telecommunications equipment, medico surgical equipment, pharmaceuticals). The authors drew largely on indicators of revealed comparative advantage ratios. Our more highly specialised industries within this sector are "well placed to gain from the creation of a single European Market".

Deregulation of the Public Utilities

This is an area where we have seen a major rolling back of the State-backed monopoly powers in recent years. Most of the impetus has come from the Commission (Article 90 Directives on Telecommunications, Energy, Postal Green Paper etc.). The European Court of Justice has also forced the pace with a number of individual rulings. Perhaps the most important impetus has come from technological development. Legislators can often find it impossible to keep pace with these developments, never mind anticipate them.

Remember the *EU has no mandate to promote privatisation*, as such. Article 222 of the EEC Treaty stipulates that: "This Treaty shall in no way prejudice the rules in Member States governing the system of property ownership". The most difficult issue is to balance the universal service requirement with the need to promote competition. The private sector should not be allowed "cherry pick".

Completion of the single market in the services sector

The EU programme here is more or less complete now. One sector very obviously affected is financial services: banking, insurance, investment services and, before too long, pension fund liberalisation. The paper on Irish banking by Brian Lucey delivered to the Society in November last illustrated the extent to which the banking sector in Ireland has become far more competitive. Much of the credit for this must be due to EU liberalisation measures.

State aid rules

These are well known and I will only make one point. While EC approved aid schemes in Ireland may appear very generous - allowing aid intensity up to 75 per

cent in some cases - this can give a very misleading impression. The average aid intensity in Ireland is far lower than the permitted ceiling for obvious reasons. By contrast, in some of the wealthier states, such as Germany, the aid ceilings on regional aids may be more modest but the state usually pays up to that ceiling. So the differences in actual aid *payments* between the richer and poorer States are not near as great as the terms of the approved aid *regimes* would suggest. To overcome this problem, the Commission has introduced sectoral aid frameworks for particular sectors (e.g. synthetic fibres, motor vehicles). They are a second best solution.

The European Commission's third survey on state aids in the European Community carried out in 1992 found, for example, that overall state aid in 1988-1990 in Ireland constituted 2.0 per cent of GDP, the same figure as for the total Community. Aid per person employed was actually lower than in the Community. When the analysis is confined to the manufacturing sector, Ireland's aid as a percentage of GDP (4.9 per cent) is a little higher than the Community (3.5 per cent) but the gap was narrowing and continues to do so.

4. THE RULES IN A NUTSHELL AND HOW THEY ARE ENFORCED

The following slides give a synopsis of the rules and how they are enforced.

SLIDE 1: PRINCIPLES OF COMPETITION POLICY

Markets should be opened up:

- Public Procurement Rules
- Completing single market in services (banking, investment services, professions, etc.)
- Deregulation of the utilities: Art 90 Directives. How to balance universal service obligation against "cherry picking".

Markets should be kept open and undistorted:

- Anti-Trust Rules (Articles 85, 86).
- Inspired our Competition Act, 1991.

Where exceptions are allowed, the criteria should be established in advance, transparent and strictly adhered to.

- State Aid Rules

SLIDE 2: THE COMPETITION RULES IN A NUTSHELL

1. Restrictive agreements are prohibited if they affect trade:

- Between Member States (EEC Treaty - Arts 85 & 86)
- In the State or in any part of the State (Competition Act, 1991)

2. Restrictive agreements may be exempted/licensed for a limited period if they meet the "four conditions":

- Improve production/distribution/progress
- Allow consumers a fair share of resulting benefit
- Impose only indispensable restrictions
- Do not eliminate competition

3. To be sure of a licence you must either:

- Notify to Brussels/Dublin
- Draw up agreement to comply with one of the standard EU block exemptions or domestic Category Licences (exclusive distribution, motor fuels).

4. Abuse of a dominant position is prohibited. No question of a licence.

- Examples: Imposing unfair trading conditions, limiting markets or production, unjustified tie-in clauses, etc.

5. Jurisdiction

- Arrangements can come within both National and EU Jurisdictions
- If conflict between EU and Irish law, EU law prevails
- De minimus applies in EU law, not in Irish law

SLIDE 3: ENFORCEMENT OF EU COMPETITION RULES

COMMISSION is executive/enforcement arm of the Union

- Notifications: Formal Decisions (rare) or (dis)comfort letters.
- Complaints
- Own Initiative Investigations
- Commission can order firms to desist and impose fines

National courts have full jurisdiction to decide if infringements of treaty rules have taken place.

National courts cannot grant exemptions.

- Commission jealously guards this exclusive right. "Brussels knows best" philosophy prevails because of market integration mission of the competition rules.

Commission claims it wants more cases resolved by national courts. Why?

- Let Commission concentrate on priority cases
- Subsidiarity
- National courts can award damages, Commission cannot.

Beware: Commission also wants to retain all its exclusive powers on exemptions. Commission enjoys best of both worlds.

Downside: The complaints path to Brussels (e.g. B & I/Sealink dispute) may become more closed off. Parties may have to follow more expensive and uncertain path of remedies through national courts. "Subsidiarity" has its price!

SLIDE 4: ENFORCEMENT OF IRISH COMPETITION RULES

Right of action in court

- Any party who is aggrieved by an anti-competitive arrangement can seek relief by way of damages, injunction, declaration.
- Minister may also seek redress in court.

[Note: Minister also has special power to order abuse of a dominant position to cease on foot of a report from Competition Authority. No need to go through courts. Unconstitutional?]

Role of competition authority

- Parties to an agreement may notify it to Authority.
- Authority will examine it and issue either a:
 - *certificate*: opinion that it is not restrictive
 - *licence*: opinion that it is restrictive but meets the "four conditions".
- Remember that Authority may refuse to issue a certificate or licence unless/until agreement is amended.
- Authority has no formal enforcement powers.
- Legal status of a *certificate/licence*? The Act is ambivalent here. As a minimum, these opinions would have a very persuasive effect in court. Don't underestimate the deterrent effect.
- Authority may carry out studies and analysis at request of Minister.
- Authority also examines and reports to Minister on mergers/acquisitions notified to him under *Mergers, Takeovers and Monopolies (Control) Act, 1978* (e.g. Independent/Tribune Newspapers case).

5. CONCEPTUAL PROBLEMS IN COMPETITION LAW

The major issues arising in competition policy are essentially economic. But they have to be resolved in a legal framework. Very often, the issues are clear cut e.g. if two large firms agree to share a market then there is a clear loss in efficiency and a breach of the law. If a dominant firm refuses to supply particular customers for no objective reason, then again there is an efficiency/loss and abuse of dominance.

But when we probe deeper into a case, often conceptual problems arise, Examples:

How to define the product market?

(e.g. *Independent/Tribune* case; *Continental Can* case: Commission won a major principle, but lost because of faulty definition of the market).

At EU level, the Mergers Task Force has used econometric studies on cross elasticities of demand. But generally, there is a preference for the "intelligent layperson" approach (e.g. Ford/VW experience with multi purpose vehicles).

How to define the geographic market?

In Ireland, how to measure market share?

Predatory Pricing

Would the following OECD definition of "true predatory pricing" stand up in court?

"The predatory pricing requires the perpetrator to incur substantial losses or at least to forego present profits in the hope that those losses can be more than recouped in the future through the exercise of market power".

Where is the illegal intent to abuse here? Contrast with EU approach of focusing on the "*intent*" of the dominant party.

Joint Ventures

How do you judge if the parties would not have developed the product/service separately and thereby enhanced competition? Often a JV is the only way two sizeable Irish parties may gain a foothold in overseas markets. Similar issues arise at EU level viz. Japanese/US competitors.

By way of illustration, I set out in the Annex a note on one of the most interesting EU cases in recent times: *Woodpulp*. The Commission found in 1984 an elaborate price fixing cartel to exist. Nine years later the Court said it wasn't a cartel at all, but legitimate economic behaviour!

6. SECOND THOUGHTS ON IRELAND FOLLOWING THE EU MODEL

The Market Integration Mission

The Commission's greatest success in implementing the Treaty competition rules has been in using them as an instrument to integrate the different national markets. So many of the "classic" decisions involved restrictions in trade arising, directly or indirectly, at national frontiers. This is the natural focus for restrictions, market sharing, etc. DG4 sees as one of its glories, the fact that it insisted from the outset that the fiction of the single market was true: It did not tolerate excuses or pre-conditions from offending companies (e.g. absence of tax harmonisation, common currency, common Community policy for sector x). Generally, the Court endorsed the Commission's approach.

This market integration mission of the EU competition rules explains in large part, I feel, why the founders of the Treaty opted for the "prohibition system" which underlies Articles 85 and 86 rather than the more laconic "rule of reason" approach which exists in, say, US competition law. To oversimplify the distinction:

The *US "rule of reason" approach* says that, in effect, a "restriction" is not always a restriction; you have to analyse all the relevant circumstances, akin to the Article 85.3 analysis in the EEC system).

The *EU prohibition* is to say that a restriction is a restriction. The only way the "overall analysis" comes into play is if you *notify*. Only the central authority (Commission) is allowed do the balancing act.

The "Notification Culture"

This is the inevitable result of the Commission insisting that only it could oversee the market integration mission of the EU competition rules. In reality, the case by case approach never really worked with the Commission. Firms notified any agreements they thought might pose problems in order to save themselves from being fined afterwards if they were found to be restrictive. But the Commission always selected only the priority cases for detailed consideration. Otherwise, the system would have ground to a halt.

Many notified cases gather dust in Brussels. Does it matter? Probably not, as long as firms don't mind paying the costs of notification.

Does it matter in Ireland? Yes, because we have created a legal "entitlement" to an opinion from the Authority. Did we really think through the practical consequences of the notification procedures when we drew up the Competition Act?

Remember the Commission will always be a federal authority. It will always be able to pick the priority cases and rely on generous *de minimis* rules. It is becoming even more selective in deciding which cases to follow up. Our Authority cannot enjoy these "luxuries". Should we not therefore move away from the "notification" path?

Decisions are Policy Documents

Increasingly, there is a perception that formal decisions by the Commission are intended as policy documents as much as legal instructions addressed to the parties to an agreement (e.g. Ford/VW case).

7. IDEAS FOR FUTURE OF IRISH COMPETITION ACT

We must try to balance the ambitious sweep of EU competition rules with the need for business to operate in a climate of reasonable legal certainty. I appreciate the task is a hard one and that there are no easy answers.

I would prefer to see the priority shift away from processing of the hundreds of arrangements notified to the Competition Authority to date - many of them routine and harmless - towards setting out broad policy guidelines in a number of key areas. Can we try to establish the ground rules and then promote more of a "self assessment" culture among business and rely on complaints for enforcement?

The Minister for Employment and Enterprise has stated he will shortly propose amendments to the Competition Act. I would make *two specific suggestions* and *advance two general ideas*.

Remove all mergers from the competition act

It is recognised in most jurisdictions that the rules and procedures for assessing mergers must be different from those for assessing the day to day business behaviour of firms. This has been the EU Commission's policy for many years, as was confirmed by the Director General for competition at an IBEC conference in Dublin last December. Merger control is essentially a matter of *public policy* which should be decided exclusively by the Minister for Enterprise and Employment under the Mergers Takeovers and Monopolies (Control) Act, 1978. By contrast, whether a firm's behaviour is anti-competitive is a matter of legal interpretation by the Authority and ultimately for the courts to decide upon.

Under the 1978 Act all mergers and acquisition above certain financial thresholds must be notified to the Minister who has a limited period within which to decide

whether to let the merger go ahead or not. However, the Competition Authority gave rise to much controversy and uncertainty when it concluded in its Woodchester decision of August 1992 that mergers could in certain circumstances infringe the Competition Act if they "resulted in a diminution in competition in the market concerned". Whether the merger had been notified to the Minister under the 1978 Act was irrelevant. I personally think this view is wrong and that the Authority misdirected itself on the EU law in this area.

If the Minister removes from the 1991 Act only those mergers which have to be notified to him under the 1978 Act, this will in some respects leave us with a worse situation than at present. It would amount to saying that large mergers do not break the law if the Minister says so, but smaller ones may do so if the Authority or the courts say so. This would be an absurd situation in terms of economics and equity. It could even invite a challenge on constitutional grounds. If it is *really* felt that smaller scale mergers should not "go unchecked" then the logical solution is to lower the thresholds in the 1978 Act. I am not advocating this, mind you.

Enforcement - allow competition authority act on complaints

The Act would have more teeth if the Authority could follow up complaints. The EU Commission's powers here are possibly the most effective tool in enforcing the EU competition rules. This is evidenced by several recent Irish cases: *Irish Distillers*, *B&I/Sealink*, *Aer Lingus/British Midlands*, *RTE/Magill*. The 1991 Act's solution of relying on private actions through the courts might well work in other jurisdictions but not in Ireland.

Parties who feel they are suffering because of anti-competitive or abusive behaviour by others should be allowed lodge a formal complaint with the Authority. They should be required to pay a significant deposit to deter frivolous complaints. The Authority could draw on its expertise and experience to decide which complaints to follow up.

By limiting the Authority's role to responding to notified agreements, we are wasting resources and reducing the effectiveness of the Act. There is no perfect system but we have to allow the Authority more freedom to set its own agenda.

Enforcement - possible constitutional problems

Giving the Authority powers similar to the EU Commission to *order* firms to desist and to impose fines could well be unconstitutional as it would amount to exercising a judicial power beyond those limited powers allowed to non-judicial bodies in Article 37.1 of our Constitution. However, this may not be such a serious handicap to enforcement. The Authority would be in a strong position to prosecute through the courts. Alternatively, if the complainant was armed with a strong "opinion" from

the Authority in his favour he would be in a stronger position to insist the other party cease the anti-competitive behaviour or face the threat of court action.

The courts

I am no expert in this field but I found the ideas advanced by John Cooke, S.C. at the IBEC conference on Competition Policy in December 1983 very interesting and hopeful. Essentially, these were to develop a role of the Competition Authority as advisor to the courts; the "amicus curiae" idea practised on the Continent. The objective is to try to achieve some fruitful merging of the inquisitorial civil law tradition from the Continent with our adversarial common law tradition. Hopefully, Mr Cooke's "modest experiment" will be followed up.

ANNEX

CONCEPTUAL DIFFICULTIES IN COMPETITION LAW - THE "WOODPULP EXAMPLE".

According to the Commission, whenever a producer has charged the same price as another producer for a given product in a given region and during a given quarter, it must, in principle, be regarded as having concerted with the other producer..... It must be noted that parallel conduct cannot be regarded as furnishing proof of consultation unless consultation constitutes the only plausible explanation for such conduct. It is necessary to bear in mind that, although Article 85 of the Treaty prohibits any form of collusion which distorts competition, it does not deprive economic operators of the right to adapt themselves intelligently to the existing and anticipated conduct of their competitors".

Source: European Court of Justice ruling on *Woodpulp* case, 1993.

This case gives the flavour of the problems that can arise in trying to resolve difficult economic issues in a legal framework.

In March 1993, the European Court of Justice finally closed one of the longest running cases in competition law - the *Woodpulp* case - 9 years after the original decision by the Commission! This was a case where the Commission had found that a group of Scandinavian, Canadian and US woodpulp producers had operated a price cartel over a sustained period. The parties challenged the Commission decision. They usually do nowadays!

First of all, they challenged it on grounds of jurisdiction. The Court found that, providing the arrangements challenged in the decision had *effects* within the Community, the Commission was perfectly entitled to make a ruling on it, regardless of the place of origin of the parties or where the agreements were actually drawn up and signed.

More importantly, however, the parties claimed that all the evidence of "parallel price behaviour", even if it were upheld, did not amount to collusion. They claimed it could be explained by the operation of legitimate market behaviour. This was the key issue at the end of the day.

Eventually, the Court commissioned two reports by economic consultants to try to help them come to a ruling on the case. The first report dealt with parallelism of prices and, in particular, whether the evidence relied on by the Commission justified the finding of parallelism of announced prices and transaction prices. The second report analysed the woodpulp market during the period in question.

According to the experts' report, the system of price announcements agreed between the parties to the arrangement was introduced in response to demand from the producers' customers. The quarterly cycle was the result of a compromise between the customer's desire for a degree of foreseeability as regards the price of pulp and the producer's desire not to miss any opportunities to make a profit in the event of a strengthening of the market. As regards the simultaneity or near simultaneity of the announcements, the consultant said this could be explained as a direct result of the very high degree of market transparency. This transparency, far from being artificial, was explained by the extremely well developed network of relations which, in view of the nature and structure of the market, had been established between the various traders and the trade press.

On the parallelism of announced prices, the experts concluded that this could be plausibly explained by market conditions rather than collusion. The market in question was oligopolistic on the producers side but also on the customers side. This, coupled with the high degree of market transparency in elasticity of demands, led to a situation where prices were slow to react in the short term. All in all, they concluded, the consultation was not the only plausible explanation for the parallel conduct.

On the basis of the consultant's report, the Court largely upheld the appeal by the companies and quashed the fines imposed by the Commission.

Issues arising from Woodpulp

Several general points emerged from this remarkable case.

- The economic issues which can arise under competition law can be extraordinarily complex. It can sometimes be very difficult to draw a definitive conclusion. If there is a doubt the innocent economic rationale must prevail over the guilty economic rationale.
- Ruling on individual competition cases can be a very protracted and uncertain affair. Remember the Court of Justice in the Woodpulp case was a highly specialised court with a wealth of experience in competition law matters. Yet, it had to commission two economic consultancy experts to advise it on the economic issue. Remember also that there was no question here of trying to balance the pro- and anti-competitive effects of an arrangement to see if an exemption was merited. The only concern here was whether the arrangement was restrictive in the very first place!
- At the end of the day, economic considerations can be just as important, if not more so, than legal ones in deciding the fate of a case. Perhaps the EU institutions formerly had a preference for a legalistic rather than the economic

approach to deciding competition cases, but I think this has changed considerably. One only has to look at the decisions of the Merger Task Force established in 1989 to see how economic considerations underlie policy-making in this field.

- The Irish courts are very ill equipped to deal with the type of considerations which arise in competition policy matters. This is not just a question of inexperience. Competition law of the type embodied in the Competition Act is the product of a civil law accusatorial system. Our adversarial common law tradition finds it very hard to accommodate this. The shortcomings in our judicial system in this regard have been well described elsewhere by people far more qualified than I am.*
- Lastly, I would caution against dismissing Woodpulp as an esoteric or extreme case. I would suggest that the issues it throws up are not a hundred miles removed from cases that could arise in Ireland!

* See **John D Cooke, S.C.**, "The Competition Act and the Courts", IBEC Conference on Competition Policy, Dublin, 6 December 1993.