



Competition Law Forum

Stop Micro-managing the European economy

European judges have a unique opportunity to free dominant companies from *Über*-regulation

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Is there an unwritten rule that Microsoft should only get bad press? That's all we hear about the company's competition case in Europe at least. We're told that it is dragging its feet and not complying with the orders of the European Commission. But when you look at the actual record, this is just plain wrong. Microsoft has been complying, even with Commission orders that make no commercial sense, handicap the company to benefit its rivals, delay its innovations and require it to introduce products that provide less value for money.

The European Commission is often criticised for acting too readily on competitor complaints. The *Microsoft* case is no different. Meanwhile, forward-thinking officials at the Commission's policy unit are trying to develop rules for dominant companies that accord with modern economic thinking, and which would screen out strategic complaints. Unfortunately, the past approach of the Commission and the courts and the current standoff on *Microsoft* is blocking this sensible reform.

In the *Microsoft* case, European Court judges have a unique opportunity to require proof of consumer harm before a company is fined for trying to compete. Competition authorities should allow dominant firms to introduce better and cheaper products, even if less-efficient rivals can't keep up. Such would also help the Commission's own Lisbon Agenda of making Europe 'the most competitive knowledge-based economy in the world by 2010'.

Compliance matters - but the goalposts have to stop moving sometime

When the Commission ordered Microsoft to provide its rivals with information to help their software operate more smoothly with Windows, the company spent 30,000 hours preparing over 12,500 pages of material, and offered them unlimited free technical support. The task was monumental, yet Microsoft met the deadline; a considerable achievement when the Commission's demands seemed to change depending on which of the complainants it had spoken to last. Nevertheless, a Commission-appointed expert took just two days to declare the information 'totally useless'. He couldn't say how it might be improved, however. That is not surprising, since several other experts found Microsoft's documentation exceeded industry practice, and six technology companies have already told the Commission that it helped them design fully inter-operable products. Where is the 'non-compliance'? What more is Microsoft supposed to do?

Its rivals had wanted Microsoft's trade secrets, a demand that the Commission actually supported, ordering the company to provide all information not subject to patent protection. Not surprisingly, Microsoft refused to commit corporate suicide; but again, it tried to help by offering up limited access to its 'holiest of holies': the source code to Windows. The Commission rejected this obvious short cut though.

Reversing evolution

Other parts of the case saw the Commission order Microsoft to provide a version of Windows without its audiovisual software Media Player. While naturally reluctant to dismantle its invention, Microsoft did so and, not surprisingly, the product languishes on the shelves. The Commission was so keen to prevent Microsoft from providing more value for money, that it didn't order it to sell the downscaled version for less. Did the case team really not grasp such an obvious market fundamental?

Then there is the not-so-little matter of the fines. When the Commission ordered Microsoft to pay half a billion euros - the largest fine on record ever, let alone for a single company - the company paid up. The fine was a gutsy move by the Commission considering that recidivist cartel members and protectionist Member States have never had to stump up such a bill. Saying that Microsoft can afford it misses the point. Its decision to pay, while appealing the case on the merits, was a significant act of compliance, especially when there is doubt that its conduct was even anti-competitive. Now the company is facing fines of 2 million euros a day for supposed non-compliance, when it has actually done more than it should.

Delaying innovation

The Commission's objections to Microsoft's business model - of bundling new software with its operating system - has cast a shadow over the company's product development: Microsoft has to run its next launches past the Commission, including the pending release of its new operating system Vista. Such advance product screening by a competition agency is very unwelcome regulatory creep. It is certainly not conducive to the rapid development and distribution of new product offerings that benefit consumers. The Commission's 'market testing' does help Microsoft's rivals gain an insight into what is coming next though, and to complain if they can't match it. Is that what this case is all about - helping rivals compete with the first mover? Throughout this case, the Commission has relied on competitor complaints, without making its own assessment of whether Microsoft is harming competition in the marketplace.

There's a simple reason why the Commission hasn't engaged in such analysis: it has never thought it had to. Possible exclusion of competitors is its current, but out-dated, test. This is why none of the Commission's demands of Microsoft were made by the US authorities, who only act to prevent harm to competition, not competitors, and who recognise that ordering product unbundling is a consumer harm in itself. It's not just the *Microsoft* case though: the over-concern with competitor exclusion is a common theme in European competition law that has to be corrected.

- Vodafone acquired Mannesmann's network and proposed to offer a one-rate roaming service throughout Europe that was priced far lower than anything on offer before. Rivals complained and the Commission told Vodafone it could only offer the new service if it allowed its competitors access to the same underlying rate. Needless to say, this delayed the rollout of the service, consumers were denied the resulting benefit, and competitors had no incentive to develop their own competing service.
- The Commission blocked the merger of GE and Honeywell because it believed Rolls Royce and Pratt & Whitney's claims that they could never compete with the merging parties' bundle of avionics, jet engines and aircraft financing. In contrast, the US authorities approved the deal with minimal divestments, seeing no harm to competition and overwhelming benefits to the market.
- British Airways offered travel agents significant commissions if they increased their sales of BA tickets every year. Virgin, being smaller and having fewer flights over which to offer such commissions, couldn't match BA's offer. The Commission ordered BA to remove the price cuts, and fined it millions. But when Virgin made the same complaint in a US court, its claim was summarily dismissed for not showing any 'antitrust injury' to consumers from the resulting low prices, let alone harm to Virgin itself, which was hardly being forced out of the market, and was growing at the time in question.

What is at the heart of this disconnect? Like *Microsoft*, these are all cases where Commission intervention denied consumers an immediate and likely lasting benefit because of speculative harm to competitors. The Commission's operating theory of harm in all of these cases is that competitors will be excluded, the dominant firm will raise price, this will not be bid down because the rivals could not react, and so consumers will be harmed. There is no direct consideration of consumer harm though; each step is just assumed, despite all being highly unlikely.

Should such speculative harm continue to control European competition policy? It will if enforcers at the Commission to continue to believe that the market is best served by 'gentlemanly competition' among a number of relatively equally matched rivals. But that view is dangerous and deprives the market of aggressive price competition and innovative product offerings. This is why the *Microsoft* case is so important.

Don't let Microsoft's hard case maintain bad law

We should be grateful that Microsoft is appealing the Commission's decision. If the Commission's current approach goes unchallenged, it will continue to harm the competitiveness of the European economy in incalculable ways. The Commission's view of product bundling and low pricing is so out of date with current economic thinking that it is the focus of a massive reform

of the law on abuse of dominance that has only just begun. Already though the Commission has made welcome noises that it would like to move towards a test where likely harm to consumers must be shown (before a competitor's complaint will be given any sort of hearing, let alone enforcement support). However, the approach that the Commission itself is taking in the *Microsoft* case undermines its own policy movement. The case has taken on a life of its own, wholly separate from considerations of consumer welfare harm, let alone the Commission's Lisbon Agenda to encourage companies to be more competitive. Instead, the Commission is harming consumers by stripping value-adding features out of products, hampering product development and deterring pro-competitive conduct with unprecedented fines.

Screen out strategic complaints: test for harm to competition, not competitors

The judges in the *Microsoft* case have a unique opportunity to depart from the blinkered precedents of the past. They should adopt the consumer harm test that the Commission itself is promoting. It is all the more important to get it right now, and set a sensible, modern precedent that other courts can rely on. Competition cases are on the rise, and the Commission itself is promoting private actions as a method of deterring competition law violations. As a result, in every court in Europe competitor complainants are going to have more opportunity to harass more successful companies strategically through litigation. A clear judicial statement that one needs to prove likely harm to consumers to have standing in a competition case would do much to reduce potential abuse of the legal system.

Dominant firms do have to be reined in from time to time, but this should only occur where there is evidence of likely harm to the ultimate beneficiaries of sound competition policy – consumers – and not just some speculative harm to rivals. There is precedent for this approach as well. As some other competition judges have said: 'The successful competitor having been urged to compete must not be turned upon when he wins.'¹ A 'monopolist, no less than any other competitor, is permitted and indeed encouraged to compete aggressively on the merits'.² That is the competitive conduct we should be encouraging in Europe, not more regulation and strategic litigation. We should let competitors better each other in the marketplace, and be grateful for - rather than punish - cost-reducing innovations with clear consumer gains.

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¹ *U.S. v Alcoa*, 148 F2d 416 (2d Cir. 1945) at 430.

² *Olympia Equipment Leasing Co v Western Union Telegraph Co* 797 F 2d 370, 375 (7th Cir 1986)