

“Article 82 and Structural Remedies After Microsoft”¹

International Competition Forum

St. Gallen

22-23 May 2008

Dr. Philip Marsden
Competition Law Forum

Carl Baudenbacher is sly. He asked us to discuss: “Article 82 and Structural Remedies After Microsoft.” But what structural remedies? The *Microsoft* case in Europe was resolved without structural remedies. They were not even seriously considered. The remedies eventually applied, and upheld by the Court of First Instance, involved ordering the creation of a different product and the provision of inter-operability information.

Is **unbundling** Media Player from the operating system a structural remedy? It splits up a product, but doesn’t affect the structure of the defendant company (other than to create a “Less Functional Software” Division). Nor does it affect the structure of the market: Windows XPN was purchased only by a few die-hard geeks who wanted a souvenir of the first product mandated by a competition authority. Unbundling didn’t seem to remedy anything anyway, unless it was supposed to help competitors catch up by distracting Microsoft from its core competence. And that didn’t work either, as Microsoft was instead leap-frogged by new developments such as Flashplayer, as promoted through YouTube.

So what about the **interoperability** remedy? Is that structural? Does it involve a divestiture of a business, the most usual structural remedy? No. It is essentially a requirement to provide access to information. Important information; trade secret information, but information none the less. Isn’t that requirement more of a behavioural one then? I will examine this a bit later, but on first blush it seems to be behavioural,

¹ I am grateful for discussions on this topic with Cathryn Ross and Amelia Fletcher, and research assistance of Justine Stefanelli and Floor Rombach. The views are personal.

since it was Microsoft's refusal to provide the information to Sun that provoked the case, and it was continued difficulties in working out what Microsoft needed to do which provoked stern words from Commissioner Neelie Kroes last April (2007).

Indeed it is when we look at her words that we see why Professor Baudenbacher selected our topic. The Commissioner was frustrated by what she felt were years of non-compliance with DG-Competition's order. So even though it was in the middle of an appeal on the merits of the case, she laid down a threat at the Annual ABA Antitrust Section conference: **"It could be reasonable to draw the conclusion that behavioral remedies are ineffective and that a structural remedy is warranted"**.² This news flashed around the world.

Now, Regulation 1/2003 does make "explicit provision for the Commission's power to impose any remedy, whether behavioural or structural, which is necessary to bring the infringement effectively to an end, having regard to the principle of proportionality."³

But the Commissioner's comments seemed to have been about something more than that. There was a sense of frustration in her remarks; something punitive was in the air. But can that really be the case? After all, a remedy is not supposed to be a punishment.

As the Competition Law and Policy Committee of the OECD, to which DG-COMP belongs, has reminded us: "Remedies cure, correct, or prevent unlawful conduct, whereas sanctions penalise or punish it. Typically, a competition law remedy aims to stop the violator's illegal behaviour, its anticompetitive effects, and its recurrence, as well as to restore competition. Sanctions are usually meant to deter unlawful conduct in the future, and in some jurisdictions also to force violators to disgorge their illegal gains and compensate victims."⁴

As for sanctions, the Commission is not able to imprison Bill Gates or Steve Ballmer, but it has made liberal use of its fining powers, so one would think there has been

² <http://arstechnica.com/news.ars/post/20070423-eu-threatens-microsoft-with-structural-remedy-over-antitrust-compliance.html>.

³ Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty [2003] OJ L1, Recital 12.

⁴ JK West, "Remedies and Sanctions in Abuse of Dominance Cases", OECD Working Paper No. 65, 15 May 2007, p 7, available at: <http://ssrn.com/abstract=988053>.

punishment enough in this case. The billion Euro fines are for alleged non-compliance with the Commission order to provide inter-operability information. Microsoft has now provided that information and even more apparently.⁵

So is it the case then that “after *Microsoft*” there is no room for structural remedies in Article 82 cases? They weren’t implemented in the case across the Atlantic either. Indeed, the Court of Appeals overturned Judge Jackson’s divestment order because it was disproportionate and would sacrifice the very efficiencies that benefit consumer welfare. The Court warned that divestiture should only be imposed with ‘great caution’ partly because its ‘long-term efficacy is rarely certain’.⁶

So, given that, and if *Microsoft* is supposedly the most egregious of cases before the Commission, is there any justification for structural remedies in other proceedings under Article 82?. Is our topic exhausted already?

Likely not.

“Effective competitive structure”

Let us look at the Court of First Instance judgment itself. There is the famed paragraph 664, which reads:

“it must be borne in mind that it is settled case law that Article 82 EC covers not only practices which may prejudice consumers directly but also those which indirectly prejudice them by impairing an effective competitive structure. **In this case, Microsoft impaired the effective competitive structure on the work group server operating systems market by acquiring a significant market share on that market.**”⁷

⁵ “Antitrust: Commission imposes € 899 million penalty on Microsoft for non-compliance with March 2004 Decision” IP/08/31, 27 February 2008, [http://europa.eu/rapid/pressReleasesAction.do?reference=IP/08/31&format=HTML&aged=0&language=EN&guiLanguage=en](http://europa.eu/rapid/pressReleasesAction.do?reference=IP/08/31&format=HTML&aged=0&language=EN&guiLanguage=en;); “Microsoft Makes Strategic Changes in Technology and Business Practices to Expand Interoperability”, 21 February 2008, <http://www.microsoft.com/presspass/press/2008/feb08/02-21ExpandInteroperabilityPR.mspx>.

⁶ *United States v Microsoft Corporation*, 253 F3d 34, 80 (US App DC 2001).

⁷ Case T-201/04 *Microsoft Corp v European Commission* judgment of 17 September 2007. Emphasis mine.

Is acquiring market share now an abuse? Some will argue that this paragraph should only be read in context, as a judicial reminder that the Commission need not demonstrate that Microsoft's refusal to provide inter-operability information to its rival Sun prejudiced consumers (see para 660 of the judgment). Is that all that is going on though?

The Court's focus on indirect consumer harm by impairing market structure is an historic ordoliberal concern in Europe. Ordoliberalism promotes the "economic freedom" of competitors, rather than a narrow focus on consumer harm through high prices. While reasonable people can disagree about the propriety of such a focus in global product markets, that is the law in the EC. The European preference is precautionary, and, as such, the Court upheld the Commission's right to intervene if there is a "risk" of impairing that structure of competition, rather than checking if it was likely, or that it might in turn harm consumers. The Court's requirement that dominant firms ensure that their competitors remain "viable" is another worrying tightening of the ordoliberal approach. However, it is the Court's focus on market share that is the most disturbing.

It sounds perilously close to making abuse some sort of structural offence. That is not at all what Article 82 is about. It is the abuse of a dominant position, not the dominance itself, which is at issue. But if the Commission views Article 82 otherwise, and sees Microsoft's acquiring market share as an abuse, isn't it just symmetrical to have a structural remedy as well, one that would address and reduce Microsoft's market share. That is what the remedy was supposed to do in practice, at least according to the Commissioner. On 17 September 2007's judgment day Neelie Kroes said:

"...let us be clear, first of all, that when we observe a situation where one producer has 95% of the market, we are talking about a monopoly ...and that is not acceptable, and that is the point, you cannot expect that a competitor can be interested in entering into such a market, and that is really what we have seen. And we have complaints from those competitors, and so how can you measure whether things are working better. **Well, a market share of much less than 95% would be a way of measuring**

success. Now you cannot draw a line and say, well, exactly 50 is correct, but a significant drop in market share is what we would like to see.”⁸

The Commissioner’s spokesman, Jonathan Todd, was quick to try to clarify that Commissioner Kroes meant that “once the illegal abuse has been removed and competitors are free to compete on the merits, the logical consequence of that would be to expect Microsoft’s market share to fall”.⁹

That is not really the end of the matter, though. It seems we have an insight into how the Commissioner really thinks about this company, and perhaps about all large firms. Mr. Todd’s clarification does not offer any comfort: if Microsoft’s share does not fall as expected, couldn’t the Commission logically conclude that the abuse had not come to an end? Hopefully not!

So we are most certainly in a world where there is a continuing concern with market structure, structural remedies are being threatened, even to the level of talking about reducing sales (i.e. market share), and as we saw recently in E.On, divestments are being offered in 82 cases.¹⁰ The two questions I will try to address are:

- **how appropriate is this development, and**
- **how does this apply in a *Microsoft* scenario, i.e. is it useful to consider the provision of access or of information as structural remedies?**

How appropriate are structural remedies for Article 82 violations?

Of course structural remedies are permissible means of addressing abuses of a dominant position. Regulation 1/2003 makes that clear. *When* they are appropriate is a more relevant issue. Let us remember that Article 82 – in contrast to s. 2 of the Sherman Act – focuses only on behaviour, not on ‘monopolisation’, which arguably

⁸ P Marsden, “Microsoft v Commission: With Great Power Comes Great Responsibility”, Competition Law Insight, 23 October 2007, p4. Emphasis mine.

⁹ *Ibid.*

¹⁰ “Antitrust: Commission welcomes E.ON proposals for structural remedies to increase competition in German electricity market”, MEMO/08/132, 28 February 2008, available at http://ec.europa.eu/comm/competition/index_en.html.

includes structure. Under Article 82, competition is harmed by an abuse of a dominant position, not the dominant position itself. Of course the defendant's place in the structure of the market is a starting point in Europe and an important one. But it should not define the offence, nor the remedy. What is at issue is 'abuse' of that structural position of dominance. And just to be even more trite, let us just remember that being big isn't bad. Indeed, competition law is not about punishing success, which usually arises in a business context in terms of increased sales, and so market share. Success means a bigger, stronger, more profitable company, one that is succeeding presumably because it is providing value for money. So we are not against that, and instead are trying to allow the forces of competition to flourish. What we are very concerned about though is abusive behaviour, which ultimately harms that competition, and which is likely to harm consumers. That is the point of competition policy, and that is why abuse of dominance provisions attempt to address exploitative or exclusionary behavioural problems. They do this - presumably most appropriately and hence most usually - through behavioural remedies.

Structural remedies, on the other hand, may become necessary, according to Regulation 1/2003, when there is no equally effective behavioural remedy, or when such a remedy would be more burdensome than necessary on the defendant company.

The US has a broader remit for such remedies, but helpfully it has also gone further in explaining its rationale. It finds that a structural remedy is appropriate in monopolisation cases, when a behavioural remedy is insufficient to restore competition, and there is a close causal connection between the dominant position and the abusive behaviour.¹¹ The US has also found that structural relief is more appropriate for recidivist companies, by taking away their ability to violate the law. Indeed, it is obviously the most effective remedy: the nuclear option if you will. And with such power, comes fallout, most obviously, the breaking up of the business model in question and any efficiencies it contains.

So how well have structural remedies worked? They are something new and up and coming in the EU for 82, but they have been around as long as there has been merger control. Nevertheless, we saw in the EC's Merger Remedies study, that structural relief

¹¹ OECD Working Paper No. 65, (United States report) *supra* n 4, p 178.

was only successful just over half of the time.¹² And that is with mergers, where divestments are an obvious remedy. No systematic study has been carried out in the EU yet in the 82 area, probably because the relief is still so rare. We need to look again at the US to see how well structural remedies operate in practice.

Fortunately, Professor Robert Crandall has looked at all of the remedies in abuse cases in the US between 1890 and 1996.¹³ It is a masterful study that I recommend highly. What did he find?

Broadly, he examined a range of remedies: from actual divestiture, to mandated access and licensing of intellectual property rights. What is surprising, perhaps, is that structural relief was so common: of the 336 civil monopolisation cases he examined, the remedies imposed in 95 were structural. That's nearly 30%. And of those 95, 63 involved divestiture or dissolution.¹⁴

What was more surprising though was how very rarely they were effective. Crandall found that in most cases, structural relief was not necessary. More often than not the market in question was evolving to a more competitive position anyway. He also found that often such a decree may be ineffective due to changes in customer demand. For example, if demand is not robust, companies will have a lower incentive to enter the market and as a result, the court may have led the rivals to water, but there is not enough for them to drink.

In addition to cases where no remedy was even needed, Crandall also found that in some cases a structural remedy was actually counter productive. It sacrificed economies of scale or scope, and thus efficiency, thus removing important cost savings from the market that would otherwise have been passed on to consumers.

¹² *Merger Remedies Study*, DG COMP, European Commission, October 2005, 133.

¹³ RW Crandall, *The Failure of Structural Remedies in Sherman Act Monopolization Cases*, Joint Center Working Paper (March 2001) available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=286357 or http://www.brookings.edu/papers/2001/03_monopoly_crandall.aspx (last accessed 25 April 2008).

¹⁴ *Ibid* p 7.

He even found that structural change could be price raising, the cure being worse than the disease if a large company was just broken up into smaller regional monopolies, as happened in the *AT&T* case.¹⁵

In other cases involving mandated access, one problem that can arise is that rivals are thereby forced to link up to the dominant firm's costs base, which could mean that the market is, in effect, cartelised for a period.

Nevertheless, despite his fairly damning conclusions, Crandall does not appear to be against structural remedies *in principle*. Instead, their limitations themselves can offer us some guidance:

First, if a structural remedy is to be contemplated, then it should obviously be necessary, in other words it should be clear that there is an anti-competitive problem to remedy, but also that the market itself is not going to correct this problem in the medium term.

A second guiding principle that I would draw from Crandall's study would be that structural relief should not sacrifice net efficiencies, in other words, that any sacrifice to static short run efficiencies from breaking up economies of scale should be clearly and obviously outweighed by likely benefits to dynamic efficiencies. This also implies that the remedy not harm dynamic efficiency itself, whether that of the defendant company or other market participants.

Also, because the harm to economies of scale through any break-up is so immediate and obvious, this should militate towards a requirement that any benefits to dynamic efficiency from intervention not just be merely speculative or possible, but be probable and offsetting.

My third guiding principle would be that any structural remedy should not itself harm competition, or be likely to do so. Here again, some form of structured rule of reason should be applied to net out the harm and benefits of the remedy itself.

¹⁵ *United States v. AT&T*, 552 F.Supp. 131 (D.D.C. 1982), as discussed in Crandall, *supra* n 13.

Crandall himself suggested that divestitures would be more likely to be effective if the defendant is already organised into distinct business units that themselves can become independent following divestiture. In addition, these new competitors that are created, should not just be fragmented monopolists themselves.¹⁶

Furthermore, while one-off structural remedies are preferable to the uncertainty, costs and possible errors of agencies having to monitor a behavioural remedy, Crandall also noted that some structural remedies can take years to implement and may also involve significant monitoring. This was seen with the *AT&T* divestitures, but is even more likely with access remedies, where the continued success of the remedy is dependent on the defendant's continuing compliance.

One thing that also seems clear is that structural remedies should respond to some market failure. This may sound obvious, but I just wish to make it clear that they should not be used simply because a behavioural remedy is difficult to police. That would be creating a remedy to respond to regulatory failure rather than to a market problem. To say that we need to consider structural remedies because a defendant doesn't seem to be adhering to a behavioural remedy, is to argue that the end justifies the means, which is hardly a policy recommendation for an enlightened competition authority. Of course it is difficult to draw the line between behavioural remedies that are not working, and those that aren't working due to half-hearted compliance. Nevertheless, it is only in the former case that structural relief is appropriate, and never punishment. Similarly, it is only in the latter case of non-compliance that something punitive would be appropriate; never structural relief.

To ensure that there is not such over-reaching, the economic rationale for a structural remedy should be echoed as far as possible – and even bolstered - through legal safeguards. Think of the standard requirements that such a remedy be effective, necessary and in particular, from a legal perspective, proportionate. Recital 12 of Regulation 1/2003 states that structural remedies are only proportionate where substantial risk of a lasting or repeated infringement derives from the very structure of the market. Article 7 makes it clear that even then such remedies are only proportionate if the risk of a lasting and repeated infringement comes from the structure

¹⁶ Both findings were also confirmed by the EC Merger Remedies Study, *supra* n 12.

of the company, as opposed to, one imagines, being from the structure of the market itself, or from the structure of the other competitors.

Are access or informational remedies structural relief under Article 82?

The last point I would like to examine under the topic of Structural Remedies after *Microsoft* is the degree to which access and disclosure remedies can be said to be structural rather than behavioural. Structural remedies are assumed to be mainly about divestitures. Nevertheless, several esteemed bodies have considered IP licensing and access remedies to be structural.¹⁷ One of the most common forms of relief in abuse cases these days involves some form of mandated sharing, whether in the form of access to a network or to information that rivals claim they need to compete. Recall also the comments made by the CFI in the *Microsoft* case, in which a concern with harm to the competitive structure was resolved through, essentially, these sorts of remedies. As such, is it useful to think of these remedies as structural?

I appreciate that this is a controversial area. I also understand those who say it shouldn't matter what category – structural or behavioural – such remedies fall within. Others may decide to place them in some intermediate grey zone, and just call them hybrid or quasi-structural remedies.¹⁸ I'm not comfortable sitting on the fence. Perhaps trying to categorise them may seem an idle academic exercise in hair-splitting. But I respectfully disagree. It is vitally important to understand correctly which type of remedy these are. Of course they share elements of both kinds of relief, but it is much more appropriate - at least in fast moving high technology markets – for some of these remedies to be more closely identified as either behavioural or structural, as such a categorisation itself contains its own narrative, and own requirements.

¹⁷ For example, the European Commission categorizes mandatory IP licensing as structural in nature, OECD Working Paper No. 65, *supra* n 4, p 185, and the OECD itself has listed such licensing as a remedy that is structural in nature. 'because it has the capability to alter market structure by introducing new competitors relatively quickly' and 'may permit follow-on innovation that had been blocked by the dominant firms' refusal to license', OECD Working Paper No. 65, para 4.2.2., p 37.

¹⁸ Competition Bureau, Information Bulletin on Merger Remedies in Canada (Government of Canada: Ottawa, 2006), Part II.B.

Consider the defining features of behavioural and structural remedies: how best do access and information sharing remedies fit within that framework?

Behavioural remedies involve either directly preventing or mandating a certain form of conduct, rather than market structure. They involve a particular activity, rather than a state. The activity and relief is ongoing in nature, and needs to be monitored.¹⁹

Structural remedies on the other hand involve some change to market structure, rather than conduct. They involve a transfer of assets, usually tangible but increasingly intangible. They are one-off and do not usually require ongoing monitoring by the authorities.²⁰

Now how do access and information sharing fit within these boxes, or is it better that they straddle the two in some hybrid manner?

Consider mandated access to a network, for example of energy pipelines, a mobile telephony network, a rail network or a mine or ski lift. This sort of remedy involves the creation of an access point, it is true. But what is actually blocking rivals is some form of behaviour of the dominant firm: in other words, a refusal to deal. This is an activity, not a state. As such, both the conduct and the relief are far closer to the behavioural end of the spectrum. As a form of conduct, the remedy requires and indeed creates an ongoing relationship between the defendant company and the rival. Of necessity, it requires ongoing monitoring.

Information-sharing remedies also seem to stem from a refusal to deal. Does that make them automatically a behavioural remedy? Not really. There is something fundamentally different about what is being provided. Access can be cut off, or taken back. Information can never be taken back. So there may be an act of giving, but once given, it cannot be returned. It is spent, and indeed, creates another form of 'state': where there was ignorance, now there is enlightenment. The secret has been told. To my eyes this seems to be much more akin to structural relief: the information shared is often proprietary, and of value. Indeed, the secrecy itself is often what makes it

¹⁹ OECD Working Paper No. 65, *supra* n 4, p 19.

²⁰ *Ibid.*

valuable, and so once it has been shared, it loses all value. Disclosure, in effect, is divestment. The value – the asset - has been transferred, and this value is lost forever to the defendant and gained forever to the applicant. As such, there does not seem to be much need for continued monitoring of the remedy, unless the underlying technology on which the information is based changes, in which case there is some requirement that the information shared be made on an ongoing basis for some period of time. This is rare though. And even then would involve a repeated exchange of valuable information, or assets.

As such, I can see strong arguments for mandated access being thought of as behavioural, and information or IP disclosure remedies being much more akin to divestiture, and thus structural.²¹

What ramifications flow from this categorisation? I am usually not in favour of formal compartmentalisation and classification. Formalism is rarely helpful. But here, form follows function. If you are going to create an ongoing relationship, which can be adjusted or terminated as needs require, then you will need to supervise it, and thus have less need to be absolutely sure of your reasoning *ex ante*. If you are going to order that something be given away irrevocably, then you should be very careful beforehand, and utterly sure of your rationale.

The stakes are very high in structural relief, and the concerns about harming innovation or chilling creative conduct very great. As such I contend that there should be a higher burden of proof on the complainants and competition authorities when requesting structural relief through information-sharing and IP licensing remedies, particularly since – in contrast to behavioural relief – there is no ‘going back’ once the information is shared.

²¹ Indeed, the European Commission has indicated that although the mandatory granting of an IP license does not change an undertaking’s organisation, it ‘may have the same effect on the market as the divestiture of a business branch’, see European Commission report in OECD Working Paper No. 65, *supra* n 4, p 185. Furthermore, the OECD has also listed mandatory licensing as a remedy that is structural in nature, OECD Working Paper No. 65, para 4.2.2., p 37.