Eu competition law and economics

Discuss the use of terms drawn from economics in the jurisprudence of the European Court of Justice, which relate to the interpretation of Articles 101 and 102 of the Treaty on the Functioning of the European Union. Examine, in particular the role such terms play in the legal argument.

This essay will examine the economic theories, both from a classical point of view and neo-classical to determine the underpinnings of competition law. Through the works of Adam Smith regarding monopolies in the Wealth of Nations[1]and John Stuart Mill through his theories on restraints of trade in ' On Liberty'[2]this will demonstrate some economic objectives in pursuing laws regarding competition law. This will be supplanted with the neo-classical theories that have given more reasons through economic terms for laws regarding competition. This will provide a bedrock for an analysis of Articles 101 and 102 of the Treaty on the Functioning of the European Union (' TFEU'), which have been noted as the two principal Articles dealing with competition law in the European Union (' EU').[3]The fundamental reason for having competition law in the EU is to allow for a flourishing free market and to ensure that corporate enterprises do not have undue influence or dominance in the market or even through political influence.[4]This analysis of Articles 101 and 102 of the TFEU through the cases that have come through the Court of Justice of the European Union (' CJEU') will be looked at through the prism of the economic theories that have been outlined. By looking at it through that prism, it will allow for a determination in terms of whether the role of the economic terms are brought into the legal arguments. It has been suggested that the lawyers and the economics are ' co-pilots' of the competition law aeroplane[5]and this essay will determine

whether that is true by looking at the economic theories and the cases through the EU framework on competition law.

Economic Theory and Competition Law

Prior to delving into how competition law has adopted economic terms and theories, it is imperative to understand how economics operates vis-à-vis competition law. The classical economic theories, as noted by John Stuart Mill state that it is through competition that the political economy can have a scientific basis through which wages, rent and prices can be regulated. Whilst Mill does not provide a definition on what he meant by competition his theory on what laws surrounding competition could achieve were indicative. Smith took this further in ‘ Wealth of Nations’ when he stated it is the right of every man to enter into competition with any other man insofar as it does not violate the laws of justice and the idea of competition was to ensure that those in business bought dearer and sold for cheaper rather than having a monopoly with the opposite occurring. This theory was noted as a statement of perfect competition. This demonstrates the classical theories that exist but as time as gone on there have been neo-classical theories that give more defined responses.

In terms of the neo-classical theories, the USA has seemingly stated that competition law should be interpreted solely through what the theories in economics dictate;[6]however, this is questioned in the EU structures. The competing views in the EU look at the efficiencies as well as other concerns such as the environment and the effect on employment.[7]In terms of taking into account the outcome of having perfect competition, it has been stated

that ‘ allocative’ and ‘ productive’ efficiency is achieved which leads to the maximisation of social welfare.[8]In terms of ‘ allocative efficiency’ this is an economic term that means the resources will be allocated to different goods and services but will be divided insofar as it remains privately profitable to do so.[9]The second is that of ‘ productive efficiency’ which means that goods and services in society will be produced at the lowest cost.[10]In this regard, competition is seen as beneficial for the productive efficiency because if monopolies exist then it is likely that they will be high cost producers and they can pass that on to the consumer.[11]A third efficiency has been put forward that explains the need for competition, that being ‘ dynamic efficiency’ which cannot be accurately proved[12]but states that competition allows for products to be developed and created to gain the custom of consumers. This theory, in all but name, had been put forward by Smith when he stated that competition allows for ‘ new improvements of art’[13]showing that this efficiency has long been spoken of. This has been questioned as monopolies have the money to carry out research[14]and where there are monopolies others will try to intervene to get their custom.[15]On this basis, how the EU and CJEU have dealt with situations where monopolies arise must be examined to determine whether the economic terms have led to the decision that has been made.

Article 101 TFEU

In terms of Article 101 of the TFEU, this is designed to ensure that restrictive practices are deemed incompatible with the common market. The restrictions that are placed on ‘ undertakings’, which cover all entities that are involved in business,[16]have been seen to be circumvented for a

number of reasons. In the case of *Wouters & Others v Algemene Raad van de Nederlandse Orde van Advocaten* [17]it was held that despite a restriction on the legal profession, it was pursuing a legitimate objective in ensuring proper legal practice and therefore was allowed. It has been noted that this idea of a legitimate objective will stay within the competition law of the EU, [18]however, it is what constitutes a legitimate objective that can have implications for economic terms being used in the CJEU. In terms of a finding a legitimate objective, it has been noted that it is not necessary to look at the economic and non-economic objectives as they often go hand in hand. [19]In cases involving professional services such as *Wouters* and other cases such as *Asnef Equifax* [20]it was noted that the CJEU took into account the issue of information asymmetry whereby despite the fact that there is a restriction on competition which could increase the cost the consumer, the quality will go up which is especially prevalent in professional services. [21]These decisions tend to go against the productive efficiency in that the cost will go up by allowing increased restriction on trade in professional services, however, the allocative efficiency would be seen to improve as the quality given to the consumer improves. This demonstrates that Article 101 of the TFEU has taken the economic viewpoint into account in ensuring that the Treaty does not act rigidly vis-à-vis competition law.

The mechanism of Article 101 has not completely followed the economic arguments and this is seen with cases involving ‘ free riders’. This was seen in the case of *Consten and Grundig v Commission* [22]which involved Consten who was to be the exclusive distributor in France of Grundig electrical goods with the effect that free riders, who would wait for Consten

to promote the goods before then selling the Grundig electrical goods at a lower price than Consten.[23]The free rider economic system has been allowed in the United States of America in the case of *Continental TV v GTE Sylvania* [24]on the basis that it was economically sound. However, this was rejected in *Consten* on the basis that the fundamental objective of the EU plan is to have greater integration within the single market and not just to increase consumer protection and welfare.[25]Indeed, in the more recent case this viewpoint was reaffirmed in the case of *GlaxoSmithKline v Commission* [26]where the guidance from the EU was considered and it was noted that companies are not allowed to establish private barriers within the single market of the EU.[27]These decisions from the CJEU demonstrate that whilst the economic considerations have to be taken into account, they are secondary to the fundamental aim of the EU project to have ever closer Union[28]and to ensure that there are no private barriers within the single market. To compare this to the co-pilot analogy at the beginning of this essay, these decisions would suggest that the policy makers of the EU are the pilots and the lawyer and economist are mere passengers.

It must be noted that Article 101 has a defence mechanism at 101(3) which is primarily based on the economic considerations that have been outlined. This defence is for a defendant to prove but all agreements made are eligible to qualify under Article 101(3) if the requirements are met.[29]The requirements state that technical and economic progress must be improved which links with the dynamic efficiency theory of competition law economics. [30]The other requirements involve not eliminating competition on the market as well as ensuring that consumers receive a fair share of the

benefits from the agreement. This ties in with Smith's theory on monopolies and improving the market through competition laws as well as the allocative and productive efficiencies noted in the more neo-classical theories regarding economics and competition law. Indeed, this defence under Article 101(3) has been given a wide interpretation as seen in *CECED* [31]where the economic efficiencies were central to the judgment in declaring that the environmental benefits had to be looked at in terms of their effect on the consumer.[32]As this defence is couched in terms that are readily identifiable with the economic theories, it demonstrates that the economic terms have a huge role in competition law within the EU.

Article 102 TFEU

In terms of Article 102 of the TFEU, its whole basis is in economic terms as it is designed to stop dominance and abuse. The use of the term dominance in economics is deemed to be wider than that of a monopoly[33]and is a position of economic strength that prevents effective competition being maintained.[34]This type of dominance goes beyond just a single entity and the CJEU can look at more than one economic enterprise to see whether there is dominance, with what is known as collective dominance.[35]In this regard, the economic term of collective dominance and dominance generally was indicative in the case of *Italian Flat Case* to show that there was a breach of Article 102.[36]The second economic term alongside dominance in Article 102 is that of abuse, which is where a dominant entity can use its economic strength to obtain more benefits that it would have if it was a smaller entity.[37]The use of economic terms in Article 102 cases can be seen when abuse is discussed. Article 102 makes reference to unfair prices

but the CJEU has looked beyond this to see situations where there has been predatory pricing[38]and excessive pricing that look at economic terms in terms of how undertakings with great economic strength may attempt to price their competitors out of the market.[39]This tends to demonstrate that there are some economic terms that are used not only in Article 102 itself but also by the CJEU in its interpretation of the Article. However, this view has not been completely replicated across the spectrum.

The use of the economic terms in invoking Article 102 has been seen as haphazard[40]and this can be seen through the cases where there has been some reliance on economic terms such as predatory pricing noted above but there are others where it has been based more on the legal concepts such as where there is commission attached for selling a certain brand.[41]In this regard, when Article 102 is looked at solely it can be seen that it is couched in economic terms such as dominance and others have come in through cases such as predatory pricing but when it is compared to its counterpart, Article 101, the effect of economics on its interpretation has not been as widespread.[42]Accordingly, when it comes to the aeroplane analogy with Article 102 it is very much that the lawyer takes the chief pilot’s role whereas the economist operates as a co-pilot that attempts to bolster any legal arguments that have been made.

Conclusion

This essay has examined EU Competition Law to determine whether the role of economics or law is prevailing in its application. The economic theories, both classical and neo-classical, demonstrate that the basis for competition

law is allowing a free market to ensure that the consumers are able to receive products at a low price and other individuals are able to compete with the larger firms. In relation to Article 101 it can be seen through the use of legitimate aim and the defence given in Article 101(3) that the economic terms have a great role to play in how the case would be decided by the CJEU. However, as noted with the free rider cases such as *Consten* it is readily identifiable that the economics will only be taken into account after the fundamental aim of the EU, that being ever closer Union, is dealt with. This shows that the economic terms as well as the legal terms are very much secondary to the fundamental aims of the EU project. When the policy issue is put to one side, it can be seen that the economic terms and the legal terms in deciding a competition law case under Article 101 are co-pilots ensuring that the correct decision is made. In terms of Article 102, the use of economics has not been as prevalent as with Article 101 but this is largely due to the fact that there is a lack of a general theme. Perhaps as the law develops vis-à-vis Article 102, the economic terms will have a greater role to play.

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