Competition law

Telecommunications management & strategy

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The important of competition

- Efficient resource allocation
- Efficiency displaces inefficiency
- Incentives for:
  - productivity
  - innovation
- Improves consumer choice
- Provides value for money

Competition policy

- Varies greatly between countries
- Action to ensure markets are competitive
- A voice to counter special interests resisting change and competition
- National Competition Authority as a champion
- Competition law is an important part of the policy

Competition law

- A series of “horizontal” laws to limit anti-competitive behavior in industries, businesses, and professions dealing with:
  - anti-competitive mergers
  - anti-competitive agreements
  - abuse of dominant market positions
- National in scope, but can be extra-territorial
- International co-operation:
  - UNCTAD Forum
  - International Competition Network
  - OECD Global Competition Forum
  - European Competition Network

Market power

- In an imperfectly competitive industry individual firms have some control over the price of their output
- Market power is the imperfectly competitive firm’s ability to raise prices without losing all demand for its product

Monopolies and cartels

- A pure monopoly is an industry with a single firm that produces a product for which there are no close substitutes and in which significant barriers to entry prevent other firms from entering the industry to compete for profits
- Collusion is the act of working with other producers in an effort to limit competition and increase joint profits
- Tacit collusion occurs when firms interact repeatedly – rather than as a cartel or trust – they maintain higher prices by tacitly understanding that any departure from the collusive behaviour would trigger effective retaliation
- When firms collude, the outcome would be exactly the same as the outcome of a monopoly in the industry

Links to strategy

- Constraints on:
  - current behaviour
  - strategic options
- Significant legal risks
- Potential damage to brand
- Delays and uncertainty while cases are being settled
- Business ought to be pro-competitive
- Same economic theory as strategy

USA – antitrust policy

- Federal antitrust statutes are broadly drafted
- Each presidential administration adopts an enforcement policy for antitrust laws
  - political views of the functioning of markets
  - responding to economic, business, and technological changes
- Antitrust laws are enforced more stringently at some times than at others

A trust is an arrangement in which shareholders of independent firms agree to give up their stock in exchange for trust certificates that entitle them to a share of the trust's common profits . A group of trustees then operates the trust as a monopoly, controlling output and setting prices.

USA – antitrust legislation

- Interstate Commerce Commission (ICC) was created in 1877 to oversee and to correct abuses in the railroad industry
- The Sherman Act (1890) declared every contract or conspiracy to restrain trade illegal; and any attempt at monopoly, successful or not, a misdemeanor
- The "rule of reason" was introduced by the Supreme Court in 1911 to determine whether a particular action was illegal ("unreasonable") or legal ("reasonable") in applying the Sherman Act
- The Clayton Act in 1914 strengthened the Sherman Act and clarified the rule of reason. It outlawed specific monopolistic behaviors such as tying contracts, price discrimination, and unlimited mergers

USA – antitrust enforcement

- The Federal Trade Commission (FTC) was created in 1914:
  - to investigate the structure and behavior of firms engaging in interstate commerce,
  - to determine what constitutes unlawful "unfair" behavior
  - to issue cease-and-desist orders to those found in violation of antitrust law
- In 1938 it was extended to include "deceptive" as well as "unfair" methods of competition
- The Antitrust Division of the Department of Justice acts on violations of the antitrust laws, deciding on prosecutions and criminal charges

USA – enforcement

- Federal antitrust laws provide the following penalties:
  - criminal sanctions
  - civil penalties
  - private civil actions
  - effect of a government judgment
- Consent decrees:
  - formal agreements on remedies between all the parties
  - must be approved by the courts
  - can be signed before, during, or after a trial

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European Union

- Treaty of Rome in 1957
- Articles later renumbered, but today:
  - 81 – mergers and cartels
  - 82 – abuse of dominance
  - 86 – granting of special rights
  - 87 – granting of state aid
- Competition policy:
  - operated by the European Commission
  - Network on national competition authorities
- Significant recent reforms

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EU – Article 81

- The following shall be prohibited as incompatible with the common market: all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market, and in particular those which:
  - (a) directly or indirectly fix purchase or selling prices or any other trading conditions;
  - (b) limit or control production, markets, technical development, or investment;
  - (c) share markets or sources of supply;
  - (d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;
  - (e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts

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EU – Article 82

- Any abuse by one or more undertakings of a dominant position within the common market or in a substantial part of it shall be prohibited as incompatible with the common market in so far as it may affect trade between Member States.
- Such abuse may, in particular, consist in:
  - (a) directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions;
  - (b) limiting production, markets or technical development to the prejudice of consumers;
  - (c) applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;
  - (d) making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts

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EU – Article 86

- "In the case of public undertakings and undertakings to which Member States grant special or exclusive rights, Member States shall neither enact nor maintain in force any measure contrary to the rules contained in this Treaty, in particular to those rules provided for in Article 12 and Articles 81 to 89"
- To limit the capacity of member states to create or to sustain monopolies in the common market
- Power to implement this lies with the European Commission

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EU – Article 87

- "Save as otherwise provided in this Treaty, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the common market."
- Developed to ensure that governments and other public authorities do not give support to one firm that would distort the market
- Transparency on aid
- Strict rules on what is and is not allowed

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Market definition

- Product or service
- Geography
- Substitutability

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Merger approvals

- On a defined market
- Market shares: concentration measures, e.g., HHI
- USA – significant lessening of competition
- EU – "significantly impede effective competition, in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position, shall be declared incompatible with the common market"

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The Microsoft case

Joel Brinkley and Steve Lohr (2001) "US v. Microsoft; the inside story of the landmark case" McGraw-Hill.

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Computer cases

- A long history of cases against IBM
- Accusations it behaved anti-competitively
- Cases often dragged on for years, sometimes companies were out of business
- Now transferred to Microsoft
- Clearly dominant on the operating systems market
- Central issues are whether
  - it is anti-competitive?
  - adding software to Windows to disadvantage rivals?

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Microsoft

- Does Microsoft, through Windows, have market power?
- How does that market power arise?
- Does bundling Internet Explorer with Windows maintain Microsoft's market power over operating systems?
- Does the market power extend to browsers?
- Are consumers harmed?
  - network effects
  - the need for compatibility of software between users
  - switching costs
- relevant market: Intel-compatible PC OS worldwide
- Windows market share 95+%
- applications a barrier to entry for applications
- Windows is dominant

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US versus Microsoft

- 1998 Dept of Justice opened a case, alleging Microsoft:
  - monopolised markets for operating systems and browsers
  - engaged in exclusionary practices including bundling Internet Explorer with the Windows OS
- 2000 District Court judgement required:
  - structural separation
  - behavioural remedies
- 2001 Court of Appeals judgement quashed the break-up
- 2002 US and Microsoft then settled a package of behavioural remedies
- Structural remedies may:
  - solve incentive problems
  - lose economies of scope
- Behavioural remedies may be too vague and weak

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European Commission v. Microsoft

- Complainants were primarily based in USA
- Nonetheless, they conducted significant business in the EU
- Microsoft was dominant on the PC OS market
- There are significant differences in competition law from the USA
- EC has the power to fine up to 10% of turnover
- EC required Microsoft to remove certain parts of its software in order to improve competition
- The case is presently before the European Court of Justice (ECJ)

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United States of America antitrust legislation

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Restraints of trade

- Originally drawn from English common law
- Section 1 of the Sherman Act prohibits contracts, combinations and conspiracies in restraint of trade
- Requires the concerted action of two or more parties
- Requires the restraint to be fail one of two tests:
  - Rule of reason - only “unreasonable” restraints of trade
  - *Per se* rule - restraints of trade considered inherently anticompetitive

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Horizontal restraints of trade

- Occurs when two or more competitors at the same level of distribution enter into a contract, combination, or conspiracy to restrain trade.

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Horizontal restraints include:

- Price-fixing – where competitors in the same line of business agree to set the price of the goods they sell (A *per se* violation)
- Division of markets – where competitors agree that each will serve only a designated portion of the market (A *per se* violation)
- Group boycott – occurs when two or more competitors at one level of distribution agree not to deal with others at another level of distribution:
  - supplier
  - purchaser

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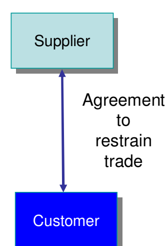
Vertical restraints of trade

- when two or more parties on different levels of distribution enter into a contract, combination, or conspiracy to restrain trade



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Vertical restraints include:

- Resale price maintenance (vertical price-fixing) – occurs when a party at one level of distribution enters into an agreement with a party at another level to adhere to a price schedule that either sets or stabilizes prices (A *per se* violation)
- Non-price vertical restraints – are unlawful under Section 1 of the Sherman Act if their anti-competitive effects outweigh their pro-competitive effects

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Defences

- Unilateral refusal to deal
  - a unilateral choice by one party not to deal with another party
  - does not violate Section 1 of the Sherman Act because there is no concerted action
- Conscious parallelism
  - where two or more firms act in the same way but without concerted action
  - does not violate Section 1 because there has been no concerted action
- Noerr doctrine
  - Two or more parties may petition the government to enact laws or to take other action

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Monopolisation

- Section 2 of the Sherman Act
- Prohibits:
  - the act of monopolisation
  - attempts and conspiracies to monopolise
- Can be violated by the conduct of one firm
- The following elements are necessary to prove a violation:
  - relevant market
  - monopoly power
  - act of monopolising

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Relevant market

- Relevant product or service market – includes substitute products or services that are reasonably interchangeable with the defendant's products or services
- Relevant geographical market – the area in which the defendant and its competitors sell the product or service

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Monopoly

- The power to control prices or to exclude competition
- Measured by the market share of defendant on the relevant market
- Willful act of monopolising:
  - required there to be a violation of Section 2 of the Sherman Act, e.g., predatory pricing
  - mere possession of monopoly power without such an act does not violate Section 2
- Defences to monopolisation:
  - superior business acumen: monopoly that is acquired by superior skill, foresight, or industry
  - natural monopoly: monopoly that is thrust upon the defendant

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Mergers

- Section 7 of the Clayton Act
- Unlawful for a person or business to acquire the stock or assets of another
  "where in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly."
- The following are necessary to prove a violation of Section 7:
  - Line of commerce: the market that will be affected by the merger
  - Section of the country: geographical market that will be affected by the merger
  - Probability of a substantial lessening of competition

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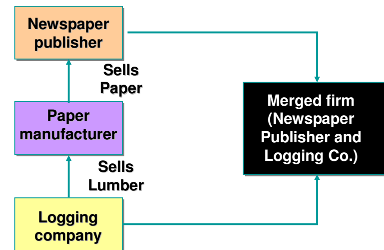
Types of merger

- Horizontal
- Vertical
- Conglomerate
- Market extension

Conglomerate mergers

- Section 7 examines the lawfulness of such mergers under the:
  - unfair advantage theory
  - potential competition theory
  - potential reciprocity theory

Potential reciprocity theory



Defences to Section 7

- The failing company doctrine
- The small company doctrine

Tying arrangements

- A tying arrangement is a restraint of trade where a seller refuses to sell one product to a customer unless the customer agrees to purchase a second product from the seller
- Section 3 of the Clayton Act prohibits tying arrangements involving sales and leases of goods, i.e., tangible personal property
- Section 1 of the Sherman Act prohibits tying arrangements involving goods, services, intangible property, and real property
- A tying arrangement is lawful if there is some justifiable reason for it

Price discrimination

- Sellers often offer favorable terms to their preferred customers
- Price discrimination occurs if the seller does this without just cause

Price discrimination

- Section 2(a) of the Robinson-Patman Act
- Prohibits direct and indirect price discrimination by sellers of a commodity of a like grade and quality where the effect of such discrimination may be to substantially lessen competition or to tend to create a monopoly in any line of commerce
- To prove a violation of Section 2(a), the following must be shown:
  1. The defendant sold commodities of like grade and quality
  2. to two or more purchasers at different prices at approximately the same time, and
  3. the plaintiff suffered injury because of the price discrimination

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Defences to Section 2(a)

- Cost justification
- Changing conditions
- Meeting the competition

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Exemptions from antitrust law

- Statutory exemptions – expressly provided in statutes enacted by the US Congress
- Implied exemptions – implied by the federal courts
- State action exemptions – business activities that are mandated by state law are exempt from federal antitrust laws

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State antitrust laws

- Most of the 50 states have enacted antitrust statutes
- State statutes are usually patterned after the federal antitrust statutes “Baby Sherman Acts”
- State antitrust laws are used to attack anti-competitive activity that occurs in commerce within the state

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European Union competition law

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