# THE ELUSIVE ANTITRUST STANDARD ON BUNDLING IN EUROPE AND IN THE UNITED STATES IN THE AFTERMATH OF THE *MICROSOFT* CASES

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Allegations of anticompetitive tying and bundling were significant parts of the antitrust cases against Microsoft in the United States and the European Union. The facts are well known. Even before its introduction of Windows XP, Microsoft has progressively produced and added to the Windows operating system a number of applications, such as its Web browser, Internet Explorer (which was included in Windows 95 in 1995), and Windows Media Player (WMP), which was integrated to Windows ME in 2000. Microsoft's policy of integrating new functionalities to the Windows operating system has been challenged by both the U.S. and the European antitrust authorities.[1]

Interestingly, the EU case and the U.S. case—which had many similarities in their bundling and tying allegations—had opposite final resolutions. In the United States, the Department of Justice decided not to

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[1] One could also add the procedure at the Korean Fair Trade Commission challenging the integration of Windows Media Server, WMP, and MSN Instant Messenger to the Windows operating system. *See* Press Release, Korea Fair Trade Comm'n, Microsoft Case (July 3, 2008), *available at* http://www.ftc.go.kr/eng.

pursue the bundling aspect of the case (bundling of Windows and Internet Explorer) after the U.S. Court of Appeals for the D.C. Circuit reversed the federal district court's finding of a per se violation for attempted monopolization of the browser market and remanded the issue with instructions that it could be pursued only under a rule of reason standard.[2] By contrast, in the European Union, the Commission found that Microsoft was liable for bundling Windows with WMP and required Microsoft to produce a Windows version without WMP in addition to the bundled version that Microsoft offered on the market.[3] Microsoft was not allowed to offer any technological, commercial, or contractual term or inducement to make the bundled version the more attractive, and a monitoring trustee was required to ensure that the unbundled version of Windows works as well as the bundled version.[4] The Grand Chamber of the Court of First Instance of the European Communities (CFI) confirmed the Commission's decision, although it annulled the part of the Commission's decision that imposed a monitoring mechanism for the implementation of the decision by a monitoring trustee at Microsoft's cost.[5] Microsoft did not appeal the CFI decision to the European Court of Justice (ECJ).[6]

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[2] *See* United States v. Microsoft Corp., 253 F.3d 34 (D.C. Cir. 2001) (The court did uphold liability for monopoly maintenance in the operating system market for integrating the browser with the operating system, commingling the code, and making it difficult to remove the browser.). On the U.S. *Microsoft* case, see, among others, Nicholas Economides, *The* Microsoft *Antitrust Case,* 1 J. INDUS. COMPETITION & TRADE 7 (2001); Nicholas Economides, *The* Microsoft *Antitrust Case: Rejoinder*, 1 J. INDUS. COMPETITION & TRADE 71 (2001); Nicholas Economides, United States v. Microsoft*: A Failure of Antitrust in the New Economy*, 32 UWLA L. REV. 3 (2001); David S. Evans, Albert L. Nichols & Richard Schmalensee, U.S. v. Microsoft*: Did Consumers Win?* (Nat'l Bureau of Econ. Research, Working Paper No. 11727, 2005); Harry First & Andrew I. Gavil, *Re-framing Windows: The Durable Meaning of the* Microsoft *Antitrust Litigation*, 2006 UTAH L. REV. 641; WILLIAM H. PAGE & JOHN E. LOPATKA, THE *MICROSOFT* CASE: ANTITRUST, HIGH TECHNOLOGY, AND CONSUMER WELFARE (2007); A. Douglas Melamed & Daniel L. Rubinfeld, U.S. v. Microsoft*: Lessons Learned and Issues Raised*, *in* ANTITRUST STORIES 287 (Eleanor M. Fox & Daniel A. Crane eds., 2007).

[3] *See* Case COMP/C-3/37.792—Microsoft Corp., Comm'n Decision (Mar. 24, 2004) (summary at 2007 O.J. (L 32) 23) (*Microsoft Comm'n Decision*), *available in full at* http://ec.europa.eu/competition/antitrust/cases/decisions/37792/en.pdf, *aff'd*, Case T-201/04, Microsoft Corp. v. Comm'n, 2007 E.C.R. II-3601 (Ct. First Instance).

[4] *Id.* ¶¶ 1011–1012. On the remedies aspect of the case, see Nicholas Economides & Ioannis Lianos, *The Quest for Appropriate Remedies in the* Microsoft *Antitrust EU Cases: A Comparative Appraisal* (NET Inst., Working Paper No. 09-05, 2009), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1464505.

[5] Case T-201/04, Microsoft Corp. v. Comm'n, 2007 E.C.R. II-3601, ¶ 1278 (Ct. First Instance) (*Microsoft CFI Decision*).

[6] Microsoft withdrew its appeal against the Korean Fair Trade Commission's decision to the High Court, following the decision of the CFI.

This sharp difference in the application of competition law arises out of the different treatment of bundling, tying, single-product and multi-product (loyalty) discounts, and foreclosure in the two jurisdictions. In this article we discuss and contrast the differences in competition policy and enforcement on the subjects of bundling and tying in the United States and the European Union in light of advances in economic analysis.

In its broadest terms, the subject of bundling has been the focus of antitrust scholarship well before the cases brought against Microsoft in the United States and in Europe. The competition issues raised are similar, and one could be tempted to classify them into the same antitrust category.[7] They involve practices that take place in and affect different relevant markets of separate products or services and aim to exclude competitors from the market in which the incumbent firm is active, or from an adjacent market. Bundling can take many different forms (contractual, technological, financial through rebates), which in turn has led competition authorities and courts to develop specific antitrust standards for each category. These different standards can be explained by the need to take into account the risk of enforcement errors and the likelihood of exclusionary effects, which may be different for each form of bundling. It is important, therefore, to develop coherent antitrust standards so that any similarity or difference in the treatment of these practices is adequately explained. Antitrust categories are not clear-cut: it is possible to present the facts of a case as fitting within more than one specific antitrust category. For example, there is a slight conceptual line that may separate the characterization of the facts of the WMP Microsoft case (in the EU) as being a bundled discount rather than a tying case. WMP was offered for free, which may formally correspond to a bundled discount, a practice that entails the offering by the supplier to the distributor of a discount (zero price in this case) for accepting a bundle of different products or services.[8] The fact that the courts analyzed the facts of the case as tying should not mask the importance of developing a coherent conceptual framework for all types of bundling. Accordingly, one should consider whether the practice at issue—and its marketplace effects—are better assessed through a different antitrust category. Doing otherwise would jeopardize the effectiveness of antitrust enforcement.

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[7] For the importance of categorical thinking in antitrust, see Mark A. Lemley & Christopher R. Leslie, *Categorical Analysis in Antitrust Jurisprudence*, 93 IOWA L. REV. 1207 (2008).

[8] *See* Einer Elhauge, *Tying, Bundled Discounts, and the Death of the Single Monopoly Profit Theory*, 123 HARV. L. REV. 397, 450 (2009) (tying is "simply a special case of bundled discounts, where the unbundled price on the linking product is set at infinity.").

Antitrust categories are not just analytical tools. They also reflect the objectives and underlying premises of the entire competition law system. Toward that end, this article adopts a broader perspective, aiming to understand the essence of the different approaches followed in Europe and in the United States with regard to bundling. We identify three important differences. The first relates to the process of antitrust categorization, and in particular the recourse to analogical reasoning in setting the antitrust standards that apply to bundling practices in both jurisdictions. The second relates to the standard of proof for the finding of anticompetitive foreclosure and consumer harm in Sherman Act Section 2 and Article 82 cases,[9] which seems to be lower in Europe than in the United States. The third difference relates to the remedies imposed in the two jurisdictions to preserve consumer choice and benefit, which seems to be the underlying objective of competition law in Europe and in the United States. We advocate a unified test for bundling and tying that would focus on anticompetitive foreclosure and absence of objective justifications. The function of the distinct product element of the tying test should be reconsidered and the separate function of the coercion element of the test should be abandoned.

## I. DIFFERENT ANALOGIES IN THE ANTITRUST STANDARDS APPLIED TO BUNDLING PRACTICES

The analysis of bundling practices and tying under various antitrust standards continues to be a hot topic in competition law, literature, and jurisprudence. The subject of bundled discounts has been, in particular, one of the most controversial in recent competition law enforcement against exclusionary anticompetitive practices of dominant firms.[10]

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[9] As of December 1, 2009, the Treaty of Lisbon became effective and introduced a renumbering of the articles in the Treaty Establishing the European Community. Relevant to the discussion here: Article 81 is now Article 101; Article 82 is now Article 102; and Article 230 is now Article 263. However, for ease of reference, we will continue to use the prior numbering in our discussion. Treaty on the Functioning of the European Union (consolidated version), arts. 101, 102, 263, May 8, 2008, 2008 O.J. (C 115) 47 (effective Dec. 1, 2009).

[10] *See* Michael D. Whinston, *Tying, Foreclosure, and Exclusion*, 80 AM. ECON. REV. 838 (1990); Barry Nalebuff, *Bundling as an Entry Barrier*, 119 Q.J. ECON. 159 (2004); Bruce H. Kobayashi, *Does Economics Provide a Reliable Guide to Regulating Commodity Bundling by Firms? A Survey of the Economic Literature*, 1 J. COMPETITION L. & ECON. 707 (2005); Bruce H. Kobayashi, *The Economics of Loyalty Rebates and Antitrust Law in the United States*, COMPETITION POL'Y INT'L, Autumn 2005, at 115; Thomas A. Lambert, *Evaluating Bundled Discounts*, 89 MINN. L. REV. 1688 (2005); Daniel L. Rubinfeld, *3M's Bundled Rebates: An Economic Perspective*, 72 U. CHI. L. REV. 243 (2005); David Spector, *Loyalty Rebates: An Assessment of Competition Concerns and a Proposed Structured Rule of Reason*, COMPETITION POL'Y INT'L, Autumn 2005, at 89; Daniel A. Crane, *Multiproduct Discounting: A Myth of Nonprice Predation*, 72 U. CHI. L. REV. 27 (2005); Kai-Uwe Kühn et al., *Economic Theories of Bundling and Their Policy Implications in Abuse Cases: An Assessment in Light of the* Microsoft *Case*, 1 EUR. COMPE-

Much of the discussion revolves around choosing the proper analogy for bundled discounts as compared with other conduct that may produce similar exclusionary effects, such as exclusive dealing, predatory pricing, and tying. Although one may consider that this quest for the "right" analogy asks the wrong question—as the real issue arguably should be the effect of the specific practice on consumer welfare[11]—it is clear that the initial choice of differing analogies may explain much of the divergence between the antitrust standards on bundled discounts in the United States and in the European Union. The choice of an adequate analogy for bundled rebates also could have an impact on the antitrust standards applied to tying, where there has been some convergence between the positions of the U.S. and EC antitrust laws. It is, therefore, important to examine what, according to the case law, distinguishes bundling from tying. That characterization will have implications on the antitrust standard that would apply, and it could lead to a different outcome if the case were brought in the European Union or in the United States.

### A. THE U.S. ANTITRUST STANDARD FOR BUNDLED DISCOUNTS

U.S. law focuses on discounts available in a product bundle. Suppose that an array of products bought by the same buyer is offered à la carte. Additionally, assume that buyers are offered a discount if a buyer fulfills a specific requirement contract, for example, if he buys at least 90 percent of his needs for several products from this seller. In economics, this is generally called "mixed bundling." A firm dominant in one market

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TITION J. 85 (2005); Christian Ahlborn & David Bailey, *Discounts, Rebates and Selective Pricing by Dominant Firms: A Trans-Atlantic Comparison*, *in* HANDBOOK OF RESEARCH IN TRANSATLANTIC ANTITRUST 195 (Philip Marsden ed., 2006); Herbert Hovenkamp, *Discounts and Exclusion*, 2006 UTAH L. REV. 841; Robert H. Lande, *Should Predatory Pricing Rules Immunize Exclusionary Discounts?*, 2006 UTAH L. REV. 863; Frank P. Maier-Rigaud, *Article 82 Rebates: Four Common Fallacies*, 2 EUR. COMPETITION J. 85 (2006); Martin Beckenkamp & Frank P. Maier-Rigaud, *An Experimental Investigation of Article 82 Rebate Schemes*, 2 COMPETITION L. REV. No. 2 at 1 (Supp. 2006); John Simpson & Abraham L. Wickelgren, *Bundled Discounts, Leverage Theory, and Downstream Competition*, 9 AM. L. & ECON. REV. 370 (2007); Gregory K. Leonard, *The Competitive Effects of Bundled Discounts*, *in* ECONOMICS OF ANTITRUST: COMPLEX ISSUES IN A DYNAMIC ECONOMY 3 (Laurence Wu ed., 2007); Timothy J. Brennan, *Bundled Rebates as Exclusion Rather than Predation*, 4 J. COMPETITION L. & ECON. 335 (2008); Damien Geradin, *A Proposed Test for Separating Pro-Competitive Conditional Rebates from Anti-Competitive Ones*, 32 WORLD COMPETITION No. 1, at 41 (2009); Patrick Greenlee et al., *An Antitrust Analysis of Bundled Loyalty Discounts* (Econ. Analysis Group, Discussion Paper No. 04-13, 2004), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=600799; Janusz A. Ordover & Greg Shaffer, *Exclusionary Discounts* (Centre for Competition Policy, Working Paper No. 07-13, 2007), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=995426).

[11] ROBERT O'DONOGHUE & A. JORGE PADILLA, THE LAW AND ECONOMICS OF ARTICLE 82 EC 500 (2006).

can use this strategy to leverage its monopoly or dominant position to other products where its market position is weaker. Similarly, this strategy can be used for monopoly maintenance across markets.

In the United States, there are divergent opinions among the circuits of the U.S. Courts of Appeal on the legality of this form of bundling. On one hand, there are circuits that accept mixed bundling as lawful if the effective price charged for one or more products in the bundle is not "predatory" or below some measure of cost.[12] The following test has been suggested: calculate the total dollar discount (across all the products of the bundle) and then apply it all to the competitive product(s). If the resulting hypothetical price for the competitive product of the bundle is above a measure of per-unit cost, then there is no antitrust violation (the "discount allocation safe harbor").[13] There are, of course, questions about whether the right cost measure should be marginal cost, average variable cost, or average total cost, but the basic idea is that unless one can construct a predatory price analogy, there is no antitrust violation. Yet, these courts would not impose the recoupment element of predatory pricing; hence, we call this the "modified predatory pricing rule" approach.

On the other hand, there are circuits that consider that bundled discounts may in some circumstances amount to anticompetitive behavior even when the dominant firm would *not* be liable under the modified predatory pricing rule approach.[14] A central issue in this more enforcement-oriented approach is the possibility that bundled pricing strategies may foreclose or exclude equally efficient rivals or not, even if the dis-

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[12] *See* Cascade Health Solutions v. PeaceHealth, 515 F.3d 883, 894–903 (9th Cir. 2008); Virgin Atl. Airways Ltd. v. British Airways PLC, 257 F.3d 256, 266–69 (2d Cir. 2001); Concord Boat Corp. v. Brunswick Corp., 207 F.3d 1039, 1061–62 (8th Cir. 2000).

[13] See the discussion of these standards in U.S. DEP'T OF JUSTICE, COMPETITION AND MONOPOLY: SINGLE FIRM CONDUCT UNDER SECTION 2 OF THE SHERMAN ACT 99–102 (2008) [hereinafter DOJ SECTION 2 REPORT], *available at* http://www.usdoj.gov/atr/public/reports/236681.pdf. The Report distinguishes between two price/cost screens that have been advanced as safe-harbors for bundled discounts: "the total-bundle predation-based" safe harbor, which essentially examined if the "discounted price of the bundle exceeds an appropriate measure of the aggregate cost of the bundle's constituent products," *id.* at 98; and the "discount-allocation safe harbor," *id.* at 99. Both of these tests build on price predation theory, in the sense that they try to identify the existence of a profit sacrifice for the dominant firm measured by the existence of a negative difference between net revenues and an appropriate measure of costs for the antitrust claim to be examined further. In May 2009, the DOJ severely criticized this report and withdrew it. *See* Press Release, U.S. Dep't of Justice, Justice Department Withdraws Report on Antitrust Monopoly Law (May 11, 2009), *available at* http://www.usdoj.gov//atr/public/press_releases/2009/245710.pdf.

[14] *See* SmithKline Corp. v. Eli Lilly & Co., 575 F.2d 1056 (3d Cir. 1978); LePage's Inc. v. 3M, 324 F.3d 141 (3d Cir. 2003); United States v. Dentsply Int'l, Inc., 399 F.3d 181 (3d Cir. 2005).

count results in prices that are above the dominant firm's costs. Interestingly, these courts make an analogy between bundled discounts and traditional tying, as all these practices may lead to anticompetitive market foreclosure. We call this the "anticompetitive foreclosure approach" to bundling.

### 1. *The Modified Predatory Pricing Rule Approach to Bundling*

In *Cascade Health Solutions v. PeaceHealth*, the Ninth Circuit held that an antitrust plaintiff can prove that a bundled discount was exclusionary or predatory (for the purposes of a claim of monopolization or attempted monopolization under Section 2 of the Sherman Act) *only if* the plaintiff established that "after allocating the discount given by the defendant on the entire bundle of products to the competitive product or products, the defendant sold the competitive product or products below its average variable cost of producing them."[15] The case arose from a challenge by Cascade to the pricing strategies of PeaceHealth, a non-profit provider of hospital care services in a county in which PeaceHealth and Cascade were the only hospital care providers. Cascade offered primary and secondary hospital care but not tertiary hospital services, which involve more complex services. PeaceHealth offered insurance companies, which are the effective purchasers of hospital services on behalf of consumers, discounts on tertiary hospital services if they made PeaceHealth their sole preferred provider for *all* hospital services—primary, secondary, and tertiary. It also offered insurance companies less favorable reimbursement rates if Cascade was added as a preferred provider of primary and secondary services. The jury found PeaceHealth liable for attempted monopolization and PeaceHealth appealed.

The Ninth Circuit focused on the conduct element of the attempted monopolization claim. Remarking that bundled discounts are "a common feature" of the current economic system, as they are used by both large corporations and smaller firms,[16] the court emphasized that they "always provide some immediate consumer benefit in the form of lower prices" and that they also can result in savings for the seller as "it usually costs a firm less to sell multiple products to one customer at the same

[15] *Cascade Health Solutions*, 515 F.3d at 910.

[16] *Id.* at 895 n.5. The court also referred to the "endemic nature of bundled discounts in many spheres of normal economic activity" as a reason to decline to endorse the Third Circuit's anticompetitive foreclosure standard for bundled discounts in *LePage's*. *Id.* at 903. The court noted: "The frequency with which we see bundled discounts in varied contexts does not insulate such discounts from antitrust review, but it heightens the need to ensure that the rule adopted does not expose inventive and legitimate forms of price competition to an overbroad liability standard." *Id.* at 895 n.5.

time than it does to sell the products individually."[17] The pervasive character of mixed bundling and the fact that "price cutting is a practice the antitrust laws aim to promote"[18] led the court to emphasize the risks of false positives in applying Section 2 of the Sherman Act and to advocate a cautious approach that should not discourage legitimate price competition. The court accepted, however, that "it is possible, at least in theory," that a firm uses a bundled discount to exclude an equally or more efficient rival and therefore reduces consumer welfare in the long run.[19] This can be achieved without any sacrifice of short-run profits if the multi-product firm excludes less diversified but more efficient rivals who will not be able to sell their competitive product above their average variable costs.

A test focusing on foreclosure effects and consumer harm would take into account these anticompetitive effects. The court, however, implicitly dismissed this alternative approach based on the risk of false positives. It found instead that "the exclusionary conduct element of a claim arising under Section 2 of the Sherman Act cannot be satisfied by reference to bundled discounts unless the discounts result in prices that are below an appropriate measure of the defendant's costs."[20] The objective in the court's view was clear: the test will filter the meritorious claims (where at least equally efficient rivals are excluded from the market) from unmeritorious claims (where less efficient rivals are excluded, even if this exclusion might have led to higher prices for the consumers), thus creating a safe harbor for monopolists that price their bundles to meet this standard.

As a cost-based rule the court adopted the "discount attribution standard" or "discount allocation standard":[21]

> Under this standard, the full amount of the discounts given by the defendant on the bundle are allocated to the competitive product or products. If the resulting price of the competitive product or products is below the defendant's incremental cost to produce them, the trier of fact may find that the bundled discount is exclusionary for the purpose of § 2. This standard makes the defendant's bundled discounts legal unless the discounts have the potential to exclude a *hypothetical* equally efficient producer of the competitive product.[22]

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[17] *Id.* at 895.

[18] *Id.* at 896.

[19] *Id.*

[20] *Id.* at 903.

[21] *See* Crane, *supra* note 10, at 28.

[22] *Cascade Health Solutions*, 515 F.3d at 906 (emphasis added).

The Ninth Circuit used as an "appropriate measure of the defendant's [incremental] costs," average variable costs, the same as it employs in predatory pricing cases.[23]

The Ninth Circuit adopted a form of predatory pricing test (the attribution test) for bundled discounts for essentially two reasons. First, in its view, the alternative foreclosure standard will create false positives and lacks clarity because it does not provide firms with objective criteria to which they can compare their commercial strategies and determine, ex ante, if these will lead to liability under Section 2 of the Sherman Act.[24] Second, the anticompetitive foreclosure standard may have the effect of protecting a less efficient competitor. The exclusion of a rival that has higher average variable costs will lead to the application of Section 2 of the Sherman Act, if the effect of this exclusion will be to extend or maintain the market power of the firm employing the bundled discount practice.

In reaching this conclusion, the Ninth Circuit relied on what it perceived as significant differences between bundled discounts and traditional tying practices, therefore implying that the attribution test will not apply in tying cases:

> "[O]ne difference between traditional tying by contract and tying via package discounts is that the traditional tying contract typically *forces* the buyer to accept both products, as well as the cost savings." Conversely, "the package discount gives the buyer the choice of accepting the cost savings by purchasing the package, or foregoing the savings by purchasing the products separately." The package discount thus does *not constrain the buyer's choice as much as the traditional tie*. For that reason, the late-Professor Areeda, and Professor Hovenkamp, suggest that "[a] variation of the requirement that prices be 'below cost' is essential for the plaintiff to establish one particular element of unlawful discounting—namely, that there was actually 'tying'—that is, that the purchaser was actually '*coerced*' (in this case, by lower prices) into taking the tied-up package."[25]

The court noted that Areeda and Hovenkamp take the view that bundled discounts are a specific form of tying, but they also advocate a stricter standard to establish coercion under bundled discounts—i.e., a requirement that the attributed prices are below some measure of

[23] *Id.* at 903, 910.

[24] *See id.* at 903 ("[W]e think the course safer for consumers and our competitive economy to hold that bundled discounts may not be considered exclusionary conduct within the meaning of § 2 of the Sherman Act unless the discounts resemble the behavior that the Supreme Court . . . identified as predatory.").

[25] *Id.* at 900–01 (emphases added) (quoting 3 PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶ 749b2, at 331–32 (Supp. 2006)).

cost—than the standard used under the traditional tying test. This is not similar to the claim that bundled discounts should be analyzed under the predatory pricing test. Predatory pricing provides an immediate benefit to consumers that is objectively measured by reference to the costs of the undertaking.[26] The terminology of bundled "discounts" may induce the erroneous assumption that bundled discounts reduce prices to buyers, although it simply means that the defendant charges lower prices to the clients that conform with the bundling condition than to those that do not.[27] The defendant is free to set the prices above the levels that would have prevailed but for the bundling and therefore, as Einer Elhauge rightly observes, "There is no warrant for presuming that noncompliant prices equal but-for prices, and thus no justifiable grounds for assuming that 'discounts' from noncompliant prices reflect a true discount from but-for levels."[28] The Ninth Circuit did not hesitate, however, to establish an analogy between bundled discounts and predatory pricing and to refer to Supreme Court precedents on pricing abuses,[29] notwithstanding the fact that no specific argument other than the one previously mentioned was made to support this analogy.

Based on Supreme Court precedent on pricing abuses, the Ninth Circuit derived the proposition that "antitrust laws do not punish economic behavior that benefits consumers and will not cause long-run injury to the competitive process."[30] The benefits to consumers are immediate, "because the discounts allow the buyer to get more for less."[31] Yet, as we have explained, this is based on the incorrect assumption that bundled discounts are true discounts.

The Ninth Circuit also relied on the fact that the Antitrust Modernization Commission (AMC) suggested a predatory pricing standard for bundled discounts. This standard requires the plaintiff to prove that the defendant (after attribution of the bundled discount) priced below incremental costs for the competitive product (attribution test), that the

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[26] Professor Hovenkamp seems to support even stricter requirements than the test adopted in *Cascade Health* for bundled discounts. *See* Herbert J. Hovenkamp & Erik N. Hovenkamp, *Exclusionary Bundled Discounts and the Antitrust Modernization Commission* (Univ. of Iowa, Legal Studies Research Paper Series, Research Paper No. 08-13, 2008), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1126723.

[27] *See* Elhauge, *supra* note 8, at 450.

[28] *Id.*

[29] Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 414 (2004) ("[A]bove-cost predatory pricing schemes, [are] 'beyond the practical ability of a judicial tribunal to control.'" (citation omitted)); Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co., 549 U.S. 312, 325 (2007) (same).

[30] Cascade Health Solutions v. PeaceHealth, 515 F.3d 883, 903 (9th Cir. 2008).

[31] *Id.* at 895.

defendant is likely to recoup these short-term losses (recoupment test), and that the bundled discount or rebate program has had or is likely to have an adverse effect on competition (evidence of a likely adverse anticompetitive effect test).[32] However, when it came to the definition of the different steps of the analysis for bundled discounts, the Ninth Circuit omitted the additional elements of the test advocated by the AMC, other than the attribution test. First, it refused to integrate the recoupment test of predatory pricing in the test applied to bundled discounts, asserting that the bundled discounter may not lose any profits by bundling.[33] Second, it found redundant the third prong of the test suggested by the AMC, holding it "no different than the general requirement of 'antitrust injury' that a plaintiff must prove in any private antitrust action."[34]

### 2. *The Anticompetitive Foreclosure Approach to Bundling*

At the opposite end of the spectrum, some courts have ruled that bundled discounts may in some circumstances amount to anticompetitive behavior even when the dominant firm would not be liable under the modified predatory pricing test. Interestingly, these courts make a more direct analogy between bundled discounts and tying, as all these practices lead to anticompetitive market foreclosure (the anticompetitive foreclosure approach).

In *LePage's*, the Third Circuit made explicit the analogy between bundled rebates and tying, and it adopted an abbreviated rule of reason approach. 3M, a dominant supplier of transparent tape, bundled rebates relating to the purchase of its private-label tape, which was a product for which it faced important competition from LePage's, with a requirement that customers purchase other products from 3M's different product lines that LePage's did not offer. LePage's argued that 3M's behavior constituted monopolization under Section 2 of the Sherman Act because, by bundling its rebates, 3M had created a de facto exclusivity as the bundled rebates induced many of LePage's major customers to eliminate or reduce their purchases of tape from LePage's. 3M argued that its conduct was legal as it never priced its transparent tape below its

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[32] ANTITRUST MODERNIZATION COMM'N, REPORT AND RECOMMENDATIONS 94–98 (2007) [hereinafter AMC REPORT], *available at* http://govinfo.library.unt.edu/amc/report_recommendation/amc_final_report.pdf.

[33] *See Cascade Health Solutions*, 515 F.3d at 910 n.21 ("We do not believe that the recoupment requirement from single product cases translates to multi-product discounting cases. Single-product predatory pricing, unlike bundling, necessarily involves a loss for the defendant. . . . By contrast, as discussed above, exclusionary bundling does not necessarily involve any loss of profits for the bundled discounter.").

[34] *Id.*

cost. The court did not examine whether 3M's price of transparent tape was below a certain measure of its cost. It applied instead an anticompetitive foreclosure test: "[T]he principal anticompetitive effect of bundled rebates . . . is that when offered by a monopolist they may foreclose portions of the market to a potential competitor who does not manufacture an equally diverse group of products and who therefore cannot make a comparable offer."[35]

The Third Circuit found that foreclosure of LePage's, which was a significant competitor, could lead to higher prices and reduced output. 3M could have later recouped the profits it had forsaken with the discount scheme by selling higher priced Scotch-brand tape. This was a possible strategy in view of evidence indicating that "'significant entry barriers'" prevented competitors from entering the tape market in the United States.[36] According to the court, 3M's practice had "long-term" anticompetitive effects, without 3M offering any adequate business justification for its practices.[37] The Supreme Court refused the petition for a writ of certiorari.[38]

The decision has been controversial, in particular, because the anticompetitive foreclosure test applied by the court could lead to the application of Section 2 of the Sherman Act even if the excluded competitor was not as efficient as the defendant. As Judge Greenberg remarked in his dissenting opinion, "LePage's is not as efficient a tape producer as 3M."[39] The introduction of the requirement that Section 2 of the Sherman Act should only apply if the plaintiff brings evidence that the defendant priced below its average variable costs, therefore, aims to take into account the possible false positives that could follow from the full application of the anticompetitive foreclosure approach.

The adoption of a price/cost test and the contrary position of the Third Circuit in *LePage's* have been a matter of controversy in U.S. antitrust law.[40] The *DOJ Section 2 Report*, published by the George W. Bush administration, embraced a cost-based safe harbor.[41] Where bundle-to-

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[35] LePage's Inc. v. 3M, 324 F.3d 141, 155 (3d Cir. 2003).

[36] *Id.* at 163 (citation omitted).

[37] *Id.*

[38] 3M Co. v. LePage's Inc., 542 U.S. 953 (2004) (mem.). The decision followed a brief from the Solicitor General suggesting that "[t]here is insufficient experience with bundled discounts to this point to make a firm judgment about the relative prevalence of exclusionary versus procompetitive bundled discounts." Brief for the United States as Amicus Curiae, *3M Co.*, 542 U.S. 953 (No. 02-1865), 2004 WL 1205191, at *12.

[39] *LePage's*, 324 F.3d at 177 (Greenberg, J., dissenting).

[40] See the discussion in DOJ SECTION 2 REPORT, *supra* note 13, ch. 6.

[41] *Id.*

bundle competition was not possible, the DOJ suggested a discount allocation safe harbor that would compare the dominant firm's cost for the competitive product in the bundle to the "imputed" price of that product, i.e., the price after allocating to the competitive product all discounts and rebates attributable to the entire bundle. The bundling scheme could fall within the scope of Section 2 only if the plaintiff showed that the defendant sold the competitive product at an imputed price that was below the product's incremental costs.[42] In contrast, in its *Transition Report* the American Antitrust Institute, a liberal think tank advancing a more active antitrust enforcement agenda for Section 2, rejected a cost-based safe harbor for bundled rebates and supported a structured rule of reason that would allow plaintiffs to establish that such discounts are prima facie exclusionary under certain conditions.[43] Recently, early in the Obama administration the DOJ Antitrust Division has withdrawn the *DOJ Section 2 Report* and expressed its disagreement with the reasoning and the conclusions of the report.[44] The position of the new administration with regard to the price/cost-based test is still unclear.

### B. THE STANDARD FOR BUNDLED DISCOUNTS IN EC COMPETITION LAW

In the following discussion we explore the differences between the case law of the European Courts (ECJ and CFI), which apply to bundled discounts a foreclosure-based approach, and the European Commission, which has recently adopted a price/cost-based approach.

#### 1. *The Foreclosure Standard of the European Courts*

The case law of the ECJ and the CFI does not draw a distinction between single-product rebates and bundled discounts. The case law distinguishes between volume (quantity discounts), which are legal per se, and loyalty rebates, which are illegal in most circumstances. The European judiciary adopts a foreclosure test that does not require evidence that the discount on the competitive product was below an appropriate measure of the defendant's cost.

A dominant firm can grant quantity discounts without infringing Article 82 of the EC Treaty if these are offered on equal terms to all custom-

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[42] *Id.* at 101–02. The *AMC Report* provides for an additional condition, as it requires the plaintiff to prove that the defendant is likely to recoup these short-term losses. AMC REPORT, *supra* note 32, at 99.

[43] AMERICAN ANTITRUST INSTITUTE, TRANSITION REPORT ON COMPETITION POLICY TO THE 44TH PRESIDENT OF THE UNITED STATES 71 (2008), *available at* http://www.antitrustinstitute.org/archives/transitionreport.ashx.

[44] *See* Press Release, *supra* note 13.

ers of the firm. Discounts also should reflect efficiency gains (economies of scale in production, cost savings, etc.). By contrast, loyalty rebates rewarding exclusivity or strongly encouraging the customer to stay with the supplier may in certain circumstances be considered illegal under Article 82.[45]

A system whereby the rebate is conditional on purchasing mainly or exclusively from the dominant undertaking is abusive in principle.[46] Dominant firms may not enter into exclusive purchasing agreements and may not operate rebate schemes that have the same adverse effect as an exclusive purchasing agreement. For example, in *Hoffmann-La Roche v. Commission*, the discounts were conditioned on the customer's obtaining from the dominant defendant firm all or most of its requirements on sometimes different vitamins, which were part of different relevant markets. The court found that these conditional rebates foreclosed the access of rival producers in the market,[47] and it observed that such rebates amounted to an unlawful tie-in, infringing Article 82(d).[48]

Recent case law has focused on targeted (individualized) retroactive discounts producing an exclusionary and loyalty effect.[49] These are generally found to infringe Article 82 when they are capable of producing an exclusionary effect by causing, without any objective economic justification, the entry of competitors into the market to be more difficult, or impossible.[50] Somewhat analogous to the *LePage's* decision in the United States, the excluded rival may be a less efficient firm than the defendant, but this is not an element that is taken into account in the application of Article 82 to rebates.

In *Michelin II*, the CFI found that discounts based on standardized sales targets over a relatively long reference period (almost a year) were abusive under Article 82. The rebates applied retroactively to the entire turnover achieved with Michelin (thus including many different products) if the dealer achieved a pre-determined turnover target in the ref-

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[45] *See, e.g.*, Case 85/76, Hoffmann-La Roche & Co. v. Comm'n, 1979 E.C.R. 461 (Eur. Ct. Justice); Case T-65/89, BPB Indus. Plc v. Comm'n, 1993 E.C.R. II-389 (Ct. First Instance).

[46] *Hoffmann-LaRoche*, 1979 E.C.R. 461, ¶ 89.

[47] *See id.* ¶ 90.

[48] *See id.* ¶¶ 110–111.

[49] *See* Case 322/81, NV Nederlandsche Banden-Industrie Michelin v. Comm'n (*Michelin I*), 1983 E.C.R. 3461 (Eur. Ct. Justice); Case T-203/01, Manufacture Française des Pneumatiques Michelin v. Comm'n (*Michelin II*), 2003 E.C.R. II-4071 (Ct. First Instance); Case T-219/99, British Airways plc v. Comm'n, 2003 E.C.R. II-5917 (Ct. First Instance); Case C-95/04, British Airways plc v. Comm'n, 2007 E.C.R. I-2331 (Eur. Ct. Justice).

[50] *See British Airways*, 2007 E.C.R. I-2331, ¶¶ 68–69.

erence period from a number of targets set according to a grid. It was difficult for the dealers to determine the actual unit purchase price of the tires before making the last orders of the year. This uncertainty induced them to purchase wholly or mainly from Michelin. The variations in the final steps of the grid calculation created a weighted effect, as this affected the dealers' profit margins for the entire year, thus creating additional pressure to buy Michelin tires. Michelin's competitors not only had to offer a price on a customer's marginal requirements that matched Michelin's price for that quantity, but also had to propose a price so low as to offset the loss that the dealer would have made on all his purchases from Michelin during the reference period.

The purpose of the system was effectively to tie dealers to Michelin. The CFI found irrelevant the fact that the market shares and sales of Michelin fell during the period in question; the fall would have been greater had Michelin not adopted the specific rebate scheme.[51] The court emphasized the need for multi-product dominant firms to compete on the merits with their rivals and to grant discounts only if economically justified—for example, because the specific dealers bring an important volume of business, which in turn provides economies of scale to the producer that passes them to the dealers in the form of discounts. It is a central element of the decision that "[n]ot all competition on price can be regarded as legitimate."[52] In this respect, *Michelin II* seems to depart from the generally positive view of this type of "price" competition, highlighting a strong contrast between EU and U.S. treatment of dominant firms or monopolies.

For example, in *Cascade Health Solutions v. PeaceHealth*, the Ninth Circuit relied on the fact that bundled discounts are a "pervasive practice" employed by both large and small corporations to substantiate the need for a more lenient approach under U.S. antitrust law.[53] This assumption does not apply in EC competition law: dominant firms do not have the same freedom of action as non-dominant firms. This approach may be explained by the specific structure and the purpose of Article 82.

In comparison, Section 2 of the Sherman Act prohibits monopolization. Therefore, in the view of the Ninth Circuit, a practice that also is used by non-dominant firms strongly undermines the likelihood that the conduct in question was intended to expand monopoly power. Article 82, however, enshrines a regulatory approach: it is "less concerned about the creation of dominant positions and more focused on reg-

[51] *Michelin II*, 2003 E.C.R. II-4071, ¶ 245.
[52] *Id.* ¶ 97.
[53] Cascade Health Solutions v. PeaceHealth, 515 F.3d 883, 895 & n.5 (9th Cir. 2008).

ulating their behavior once dominance has been achieved."[54] The fact that a practice is pervasive in the economy will not be a relevant factor in the enforcement of Article 82, as dominant firms in the European Union have a special responsibility to preserve competition in the marketplace.[55]

It follows that the scope of Article 82 is broader than the scope of Section 2 of the Sherman Act, if an undertaking has a dominant position. First, Article 82 reaches significantly lower market shares: a dominant position may be found with a market share as low as 40 percent.[56] Second, the fact that non-dominant firms also use the same practice is irrelevant, as the purpose of Article 82 is to impose specific responsibilities on dominant undertakings. The CFI thus found in *Michelin II* that "discounts granted by an undertaking in a dominant position *must* be based on a countervailing advantage which may be economically justified."[57] In comparison, non-dominant undertakings are able to grant discounts even if these are not based on the economic justifications envisioned by the court, such as economies of scale, and even if the result of these discounts will be the acquisition of a dominant position. Nevertheless, once the threshold of dominance has been reached, the undertaking will not be able to maintain these rebates, unless they provide an economic justification for "the discount rates chosen for the va-

[54] Herbert J. Hovenkamp, *The Legal Periphery of Dominant Firm Conduct* 4 (Univ. of Iowa, Legal Studies Research Paper Series, Research Paper No. 07-21, 2007), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1014426.

[55] *Michelin I*, 1983 E.C.R. 3461, ¶ 57; *Microsoft CFI Decision*, *supra* note 5, ¶ 775; *Michelin II*, 2003 E.C.R. II-4071, ¶ 97; *see also British Airways*, 2007 E.C.R. I-2331, ¶ 23. In *British Airways* Advocate General Kokott wrote:

> Within the scope of the application of Article 82 EC, a dominant undertaking is subject to certain limitations that do not apply to other undertakings in the same form. Because of the presence of the dominant undertaking, competition on the market in question is weakened. Therefore—whatever the causes of its dominant position—that undertaking has a particular responsibility to ensure that its conduct does not undermine effective and undistorted competition in the common market. A practice which would be unobjectionable under normal circumstances can be an abuse if applied by an undertaking in a dominant position.

*British Airways*, 2007 E.C.R. I-2331, ¶ 23 (footnotes omitted). This constitutes one of the main factors explaining the "divide" between Article 82 and Section 2 of the Sherman Act. *See* Eleanor M. Fox, *Monopolization, Abuse of Dominance, and the Indeterminacy of Economics: The U.S./E.U. Divide*, 2006 UTAH L. REV. 725, 728.

[56] Case T-219/99 found that British Airways had a dominant position with a market share of 39.7 percent, which was moreover declining. Case T-219/99, British Airways plc v. Comm'n, 2003 E.C.R. II-5917, ¶¶ 183, 225 (Ct. First Instance). However, this case should be put in the context of the liberalization of the airways sector in the UK and the need to protect a new entrant, Virgin, from the incumbent monopolist, which was previously state owned. *See* GIORGIO MONTI, EC COMPETITION LAW 169 (2007).

[57] *Michelin II*, 2003 E.C.R. II-4071, ¶ 100 (emphasis added).

rious steps in the rebate system in question" (quantity discounts).[58] The position of the *Michelin II* court seems to indicate that all loyalty-inducing discounts by dominant firms in the European Union are anticompetitive by their object or, in the context of Article 82, practically illegal per se.[59]

The restrictive position of the *Michelin II* court was slightly reformulated in *British Airways v. Commission*,[60] where the ECJ adopted an approach that balances the anticompetitive foreclosure effect[61] of the rebate system against the advantages it provided to consumers.[62] Both the CFI and the ECJ upheld the decision of the Commission to condemn British Airways' reward system with travel agents because of the powerful loyalty-inducing effect of the system: (1) the reward schemes were drawn up by reference to individual sales objectives; and (2) the rewards extended to the whole of the turnover made by the agents during the period under consideration and not just on the incremental sales above the target. The Court found no possible economic justification for the system of rebates. However, the ECJ's language was more explicit than the CFI's in *Michelin II* on the possibility of being able to "counterbalance" or "outweigh" the exclusionary effects by "advantages in terms of efficiency which also benefit the consumer."[63]

The position of the court in *British Airways* is remarkable not only because the court applied an anticompetitive foreclosure test, but also because in a quite similar case involving the same parties the U.S. Second Circuit rejected Virgin's attempted monopolization claim based on British Airways' bundling of its ticket sales for corporate customers on routes between the United Kingdom and the United States.[64] The plain-

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[58] *Id.* ¶ 109.

[59] *See* John Kallaugher & Brian Sher, *Rebates Revisited: Anti-Competitive Effects and Exclusionary Abuse Under Article 82*, 25 EUR. COMPETITION L. REV. 263, 266 (2004); Denis Waelbroeck, Michelin II*: A Per Se Rule Against Rebates by Dominant Companies?*, 1 J. COMPETITION L. & ECON. 149 (2005); RICHARD WHISH, COMPETITION LAW 196 (6th ed. 2009) (noting that there is no need to prove the anticompetitive effects of the conduct but that these are inferred by the existence of a loyalty-inducing rebate system).

[60] *British Airways*, 2003 E.C.R. II-5917 (Ct. First Instance); *British Airways*, 2007 E.C.R. I-2331 (Eur. Ct. Justice); *see also* Kelyn Bacon, *European Court of Justice Upholds Judgment of the Court of First Instance in the* British Airways/Virgin *Saga*, COMPETITION POL'Y INT'L, Autumn 2007, at 227; Okeoghene Odudu, British Airways plc v. Comm'n, 44 COMMON MKT. L. REV. 1781 (2007).

[61] This standard is similar to the standard applied to exclusive dealing in U.S. antitrust law. *See* Jonathan M. Jacobson, *Exclusive Dealing, "Foreclosure," and Consumer Harm*, 70 ANTITRUST L.J. 311, 322 (2002).

[62] *British Airways*, 2007 E.C.R. I-2331, ¶ 86.

[63] *Id.*

[64] *See* Virgin Atl. Airways Ltd. v. British Airways plc, 257 F.3d 256 (2d Cir. 2001).

tiff's expert advanced a "predatory foreclosure" theory, according to which British Airways had priced below its *own* costs in certain routes by adding additional flights to deter or delay its rival Virgin's expansion and the costs incurred by British Airways were immediately recouped by setting prices substantially above costs on other routes.[65]

Highlighting once again the differences between the EU and U.S. approaches, the Second Circuit found that Virgin failed to bring evidence of below-cost pricing because, inter alia, the correct measure of costs was average avoidable costs (AAC) calculated on all of the British Airways routes in the geographical market (and not only an incremental sales test as was argued by Virgin's expert).[66] The Second Circuit also refused to find that there was recoupment, as Virgin did not indicate how much above its costs British Airways priced the non-competitive routes.[67] Thus, the court adopted a predatory standard test, noting that "low prices are a positive aspect of a competitive marketplace and are encouraged by antitrust laws," and it considered that, "[a]s long as low prices remain above predatory levels, they neither threaten competition nor give rise to an antitrust injury."[68] Indeed, this test imposes an even higher standard of proof on the plaintiff than the Ninth Circuit's modified predatory pricing test. In the latter case, the plaintiff must prove that the monopolist's prices are below its average variable costs in the competitive segment of the market.

A comparison of the antitrust standards used in the United States and the European Union for bundled discounts shows that there is an important divergence in the analogy employed for these practices. Whereas some U.S. courts examine these practices from the perspective of a modified version of a predatory pricing test, these practices are examined in Europe under the anticompetitive foreclosure standard. The European courts acknowledge that bundled discounts may, in some circumstances, have an equivalent effect to tying.[69] The European Commission has recently, however, initiated a different approach for mixed bundling.

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[65] *Id.* at 266.

[66] *Id.* at 267–69. The incremental sales test examines if the incremental revenue exceeds or not incremental cost. If this is the case, the bundled discount is found to be legal.

[67] *Id.* at 271–72.

[68] *Id.* at 269.

[69] *Microsoft CFI Decision*, *supra* note 5, ¶ 908. Although the court does not indicate if it will apply the same standard as that for tying, the language used indicates that the CFI embraces the tying analogy.

### 2. *The Commission's Approach: The Rise of the Price/Cost Test*

In this section, we will examine the approach suggested in the Commission's staff *Discussion Paper*, which was finally adopted in the *Guidance*.[70]

#### a. Analysis of Rebate Practices

The Commission's staff *Discussion Paper* rejected the distinctions among quantity, loyalty, and target rebates that were previously employed.[71] Instead, it divided rebate practices into two categories. First, it focused on single-product rebate systems of dominant firms that have effects in the dominated market; these were considered a form of price-abuse and were mainly examined under a price/cost standard. The *Discussion Paper* suggested a predatory pricing test for these practices. This was an important shift from the current approach of the CFI and the ECJ on rebates, which employs the anticompetitive foreclosure standard and does not provide for a safe harbor for discount practices. Second, the *Discussion Paper* separately categorized mixed bundling practices or bundled discounts that produce effects on *other* markets or on different products of the same market; these were analyzed in the section of the *Discussion Paper* devoted to tying practices,[72] although the Commission also classified them as a pricing abuse.[73]

Concerning bundled discounts (mixed bundling), the *Discussion Paper* acknowledged that these may have effects on competition similar to tying and that the distinction between mixed bundling and pure bundling is not "necessarily clear-cut" as mixed bundling may come close to pure bundling when the prices charged for the individual offerings are

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[70] European Comm'n, *DG Competition Discussion Paper on the Application of Article 82 of the Treaty to Exclusionary Abuses* (2005) [hereinafter *Discussion Paper*], *available at* http://ec.europa.eu/competition/antitrust/art82/discpaper2005.pdf. The *Discussion Paper* is a consultation document, prepared by the staff of DG Competition. It has not been published in the *Official Journal of the European Communities* and therefore does not have any legal effect. The Commission has recently adopted guidance on its enforcement priorities. European Comm'n, *Guidance on the Commission's Enforcement Priorities in Applying Article 82 of the EC Treaty to Abusive Exclusionary Conduct by Dominant Undertakings*, COM (2009) 864 final (Feb. 9, 2009) [hereinafter *Guidance*], *available at* http://ec.europa.eu/competition/antitrust/art82/guidance_en.pdf.

[71] On the position of the European Commission to bundled discounts and rebates having a tying effect prior to the *Discussion Paper*, see WHISH, *supra* note 59, at 727–29; JONATHAN FAULL & ALI NIKPAY, THE EC LAW OF COMPETITION §§ 4.317, 4.330–4.331 (2d ed. 2007). The Commission applied a foreclosure test, and the practices were found to be either discriminatory or equivalent to tying practices.

[72] *Discussion Paper*, *supra* note 70, ¶ 142.

[73] *Id.* ¶¶ 142–176.

high.[74] The Commission officials referred in some parts of the *Discussion Paper* to mixed bundling as "commercial tying."[75] Yet, in other parts of the *Discussion Paper*, the DG Competition staff remarked that there is a difference between these two practices in the sense that, in mixed bundling, none of the products is "'tied' in the traditional sense."[76] Nonetheless, the *Discussion Paper* recognized that both practices have similar foreclosure effects: mixed bundling constitutes an indirect measure to achieve the same result as contractual tying "by *inducing* customers to purchase the tied product through granting bonuses, rebates, discounts or any other commercial advantage."[77] In this sense, the *Discussion Paper* seemed to recognize that coercion and inducement may produce the same effects on customer choice. However, the *Discussion Paper* differentiated between commercial tying and contractual tying when it examined the existence of a market-distorting foreclosure effect. It is only if the discount was so large that "efficient competitors offering only some but not all of the components, cannot compete against the discounted bundle" that a bundled discount was found to infringe Article 82.[78]

The Commission's *Guidance* follows a similar approach by including "multi-product rebates" within the tying/bundling category.[79] This does not imply, however, that both practices are subject to a similar antitrust regime. In this case, the distinction is not between commercial and contractual tying but between price-based and non-price-based exclusionary conduct. For price-related conduct, the exclusion of competitors at least as efficient as the dominant firm is an important factor "in the general assessment of anticompetitive foreclosure."[80] The Commission recognizes that "in certain circumstances a less efficient competitor may also exert a constraint which should be taken into account when considering whether a particular price-based conduct leads to anticompetitive foreclosure,"[81] but this possibility is given less weight than in the staff *Discussion Paper*.[82] The Commission applies a price/cost test, which identifies

[74] *Id.* ¶ 177 n.112.

[75] *Id.* ¶ 182.

[76] *Id.* ¶ 181 n.113.

[77] *Id.* ¶ 182 (emphasis added).

[78] *Id.* ¶ 189.

[79] *Guidance*, *supra* note 70, ¶¶ 59–61.

[80] *Id.* ¶ 27.

[81] *Id.* ¶ 24.

[82] *See Discussion Paper*, *supra* note 70, ¶ 67. The *Discussion Paper* included it as a possible exception to the operation of the cost-based test and accepted that "it may be possible to show that the rival was actually excluded or marginalised following the bundling by the dominant company" and then leave to the dominant undertaking "the possibility to rebut the findings by using its own incremental costs." *Id.* ¶ 191.

the competitors "worthy" of competition law protection, before moving to the examination of the existence of an anticompetitive foreclosure.

The price/cost test operates, therefore, as an efficiency filter, mainly for administrability reasons. The exclusion of less-efficient competitors remains nevertheless an important concern for non-price based exclusionary conduct, such as tying. Indeed, the *Guidance* does not exclude further analysis of the practice to detect anticompetitive foreclosure once the other two conditions for the application of Article 82 are fulfilled, which are (i) the undertaking is dominant in the tying market, and (ii) the tying and the tied product are distinct products.[83]

It is important here to be precise in distinguishing between different types of rebates. These may first take the form of conditional rebates, which are "rebates granted to customers to reward them for a particular form of purchasing behaviour."[84] Conditional rebates provide the customer a rebate if her purchases over a defined reference period exceed a certain threshold. This could be a turnover threshold covering several products. According to the Commission's *Guidance*, these rebates have effects similar to exclusive purchasing obligations. They should be distinguished from multi-product rebates (or mixed bundling), where two distinct products are made available together at a lower price than the sum of their prices when made available separately. These rebates have effects similar to tying.[85] Second, there are unconditional rebates, which were mentioned in the *Discussion Paper* but were not examined by the *Guidance*, as they do not produce anticompetitive effects.

According to the Commission's *Guidance*, multi-product rebates are anticompetitive if they are so large that "equally efficient competitors offering only some of the components cannot compete against the discounted bundle."[86] For unconditional multi-product rebates the Commission takes into account the incremental price that customers pay for each of the dominant undertaking's products in the bundle and assesses whether this price remains above the Long Run Average Incremental Costs (LRAIC) of the dominant undertaking when this product is in-

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[83] *Guidance*, *supra* note 70, ¶¶ 52–58.

[84] *Id.* ¶ 37.

[85] *Id.* ¶¶ 59–61. In contrast, the recent OECD report on rebates does not make this distinction and groups all forms of bundled rebates and loyalty-inducing single-product rebates under the category of "conditional discounting." *See* OECD, POLICY ROUNDTABLES: FIDELITY AND BUNDLED REBATES AND DISCOUNTS 2008 at 7 (2008), *available at* http://www.oecd.org/dataoecd/41/22/41772877.pdf; *see also id.* at 121 (submission of the UK).

[86] *Guidance*, *supra* note 70, ¶ 59.

cluded in the bundle.[87] If this is the case, the Commission will not intervene "since an equally efficient competitor with only one product should in principle be able to compete profitably against the bundle."[88]

The Commission's *Guidance* also advances a safe harbor for "conditional rebates," when the "effective price" over the "relevant range" (which could be either the incremental purchases for incremental rebates or the contestable share (portion) for retroactive rebates) remains consistently above the LRAIC of the dominant undertaking.[89] This would normally allow an equally efficient competitor profitably to compete notwithstanding the rebate. If the effective price is between AAC and LRAIC, the Commission will proceed to a more detailed competition law assessment and examine the existence of an anticompetitive foreclosure. Of particular importance in this case will be the existence of "realistic and effective counterstrategies" at the disposal of the dominant firm's competitors.[90] If the effective price is below AAC, which is the cost benchmark for predatory pricing,[91] there is a presumption of anticompetitive foreclosure.[92]

The Commission's *Guidance* paper adopts a variation of the attribution test that closes the gap between EC competition law and the positions adopted in *Cascade Health Solutions* but with some important differences still remaining. The test attributes the discounts only to the contestable share of the non-monopolized product sold by the competitor[93] and not to all units sold, as is the case in the *Cascade Health Solutions* and the AMC test[94] and it employs LRAIC as the relevant cost bench-

[87] *Id.* ¶ 60. The Commission's *Guidance* modified the cost standard applicable to single product rebates to align it with the cost standard the staff *Discussion Paper* advocated for multi-product rebates (LRAIC).

[88] *Id.*

[89] *Id.* ¶ 43.

[90] *Id.* ¶ 44. According to the Commission, this could include, for instance, "their capacity to also use a 'noncontestable' portion of their buyers' demand as leverage to decrease the price for the relevant range." *Id.* However, "[w]here competitors do not have such counterstrategies at their disposal, the Commission will consider that the rebate scheme is capable of foreclosing equally efficient competitors." *Id.*

[91] *Id.* ¶ 64.

[92] *Id.* ¶¶ 23–26, 40–43.

[93] This is established for existing competitors by looking to the specific market context: "how much of a customer's purchase requirements can realistically be switched to a [rival]." *Id.* ¶ 42. For potential competitors, the Commission will assess "the scale at which a new entrant would realistically be able to enter." *Id.* This will be done by taking into account "the historical growth pattern of new entrants in the same or in similar markets." *Id.*

[94] It does not therefore include the portion of the monopolist's sales that are not contested and would have remained with the monopolist in the absence of the conditional discount. The discount is thus applied to a relatively small number of units while the *AMC*

mark (and not AAC as in U.S. antitrust law). It is therefore easier for the plaintiff to prove that the discount is an antitrust infringement in EC competition law, although the Commission's *Guidance* standard is more restrictive than the test applied by the Third Circuit in *3M*.[95]

However, the Commission adopts the lower predatory standard (prices below AAC) as the threshold for bundled rebates—if the dominant undertaking's competitors are selling identical bundles or could do so in a timely way without being deterred by possible additional costs—which is also similar to the standard suggested by the *DOJ Section 2 Report*.[96]

The Commission has recently applied the price/cost test in the decision fining *Intel* a record €1.06 billion on the grounds that it had abused its dominant position in the Central Processing Unit (CPU) market by granting conditional rebates and payments to a number of Original Equipment Manufacturers (OEMs), and by making payments to OEMs in order to delay and restrict the commercialization of specific products based on its rival AMD's technology.[97] In addition, the Commission found that Intel offered conditional rebates and funding to a large retailer of consumer electronics, which purchased assembled desktop and mobile PCs from OEMs for end customers on the condition that it sold exclusively Intel-based PCs. While the Commission conducted an "efficient competitor test" to determine whether the pricing regime was capable of foreclosing competition, it also noted that the Guidance Paper did not apply in this case, as it was published after the proceedings against Intel were initiated.[98]

The Commission's decision's frequent references to the case law of the European Court of Justice and the Court of First Instance create uncertainty about the application of the price/cost test in future cases. Indeed, the Commission observed in the *Intel* decision that "[a]lthough not indispensable for finding an infringement under Article 82 of the Treaty according to the case law," the efficient competitor analysis is

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and *Cascade Health Solutions* standards apply the discounts to all units, with the consequence that fewer antitrust violations are discovered. For an analysis and example, see Nicholas Economides, *Loyalty/Requirement Rebates and the Antitrust Modernization Commission: What is the Appropriate Liability Standard?*, 54 ANTITRUST BULL. 259, 274–75 (2009).

[95] LePage's Inc. v. 3M, 324 F.3d 141 (3d Cir. 2003) (adopting a rule of reason approach without any price/cost-based test).

[96] *Guidance*, *supra* note 70, ¶ 60 & n.38; DOJ SECTION 2 REPORT, *supra* note 13, at 101.

[97] *See* Case COMP/C-3/37.990—Intel, Comm'n Decision (May 13, 2009) (summary at 2009 O.J. (C 227) 13) (*Intel Comm'n Decision*), *available in full* at http://ec.europa.eu/competition/antitrust/cases/decisions/37990/provisional_decision_en.pdf.

[98] *Id.* ¶ 916.

only "one possible way of showing whether Intel's rebates and payments were capable of causing or likely to cause anticompetitive foreclosure,"[99] thus indicating that the "efficient competitor" filter does not immunize rebates from antitrust challenges based on the foreclosure test developed in the case law of the European Court of Justice and the Court of First Instance.

Subsequent to the EU *Intel* decision, the Attorney General of New York (AGNY) sued Intel on November 3, 2009, making similar allegations.[100] The AGNY alleged that Intel used its monopoly power to foreclose its competitor AMD from the market. The allegations include (i) Intel providing payments to a buyer (Dell) if it sells only Intel PCs, as well as various threats if it did not do so;[101] (ii) Intel retaliating against Dell when it started selling some AMD-based PCs;[102] (iii) a loyalty-requirement contract that required HP to sell at least 95 percent of business desktop PCs based on Intel chips with payments if the requirement was met and significant punishments if it was not;[103] and (iv) various threats to IBM not to sell high-performance AMD servers.[104]

#### b. Criticism of the Commission's Test for Bundled Rebates

One could criticize the test introduced by the Commission's *Guidance* for the following reasons: First, the underlying principle of the price/cost standard is that price-related abuses should be dealt with more leniently than non-price related abuses: the "efficient competitor" filter does not apply to non-price restraints. However, from an economic perspective there is no explanation for such a distinction. Some authors have advanced the view that enforcing Article 82 to price-related behavior leads to a high risk of false positives, while prohibiting exclusionary contracts does not have the same effect: "unlike low prices, exclusionary contracts do not always benefit consumers in the short term, regardless of their long-term effect on competition."[105] This assumption is questionable. Competition based on quality (Q) or variety (V) that increases investment is equally important.

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[99] *Id.* ¶ 925.

[100] *See* Complaint, New York v. Intel Corp., No. 09-887 (D. Del. filed Nov. 3, 2009), *available at* http://www.oag.state.ny.us/media_center/2009/nov/NYAG_v_Intel_COMPLAINT_FINAL.pdf.

[101] *Id.* at 26–44.

[102] *Id.* at 45–47.

[103] *Id.* at 2, 14, 48–63.

[104] *Id.* at 64–75.

[105] M. Laurence Popofsky, *Drawing a Line Between Bundling and Contractual Exclusion Under the Sherman Act*, GLOBAL COMPETITION POL'Y, June 2008, at 5–6.

The importance of this type of competition has been recognized by the ECJ in *Metro*.[106] It may have also justified the more lenient antitrust regime for vertical restraints, which could be viewed as contract enforcement mechanisms that ensure the quality of distribution services provided to consumers, even if this also reduces intra-brand price competition.[107] There is no specific reason advanced by the Commission to explain why price competition is more important as an antitrust concern than QV investment competition. Administrability concerns constitute generally the main explanation for this price/non-price dichotomy, such as that the courts are unable to assess complex pricing schemes, or the risk of error would be too high and could affect the incentives of dominant firms to provide better pricing deals to their customers.[108]

One could, however, raise several objections to these concerns over the administrability of a rule of reason analysis for price-related exclusionary practices. The "risk of private litigation" may explain the need to establish efficiency and "worthy of antitrust protection" filters in the context of U.S. antitrust law but it omits the fact that public enforcement by regulatory agencies covers the most important part of the enforcement of Article 82.[109] One could also devise a system that would separate the issue of liability (is there a violation of Article 82?) from the issue of remedies (what is the adequate remedy to address this violation?) and also one in which courts could delegate to competition or regulatory authorities the enactment and supervision of the remedial phase. If courts are generally found able to adopt decisions that fix royalties in other contexts, such as intellectual property law infringement and damages actions, there is no reason why, with some additional support and resources, they would not be able to perform the same task in competition law.[110]

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[106] Case 26/76, Metro SB-Groβmärkte GmbH & Co. KG v. Comm'n, 1977 E.C.R. 1875, ¶ 21 (Eur. Ct. Justice).

[107] Benjamin Klein & Kevin Murphy, *Vertical Restraints as Contract Enforcement Mechanisms*, 31 J.L. & ECON. 265 (1988).

[108] For a similar argument see DOJ SECTION 2 REPORT, *supra* note 13, at 46. The DOJ wanted to develop different tests for different types of conduct, "depending upon, among other things, the scope of harm implicated by the practice; the relative costs of false positives, false negatives, and enforcement; the ease of application; and other administrability concerns." *Id.*

[109] The relatively short history of private litigation in Europe and the filtering role of the European Commission in the context of public enforcement show that this risk is far lesser in Europe.

[110] In the U.S. context, see, for example, the *Georgia-Pacific* valuation factors case law, *Georgia-Pacific Corp. v. U.S. Plywood Corp.*, 318 F. Supp. 1116 (S.D.N.Y. 1970), under the U.S. Patent Act, 35 U.S.C. § 284 (damages for patent infringements). For a useful introduction, see WESTON ANSON, DONNA SUCHY & CHAITALI AHY, FUNDAMENTALS OF INTELLECTUAL PROPERTY VALUATION: A PRIMER FOR IDENTIFYING AND DETERMINING VALUE (2005).

Second, one could further understand the adoption of a cost-based test for pricing abuses as compensation for the asymmetrical standard of proof in EC competition law for efficiency gains.[111] In the absence of a price/cost test, dominant undertakings would have had to substantiate the efficiency gains for every rebate/discount that could have produced an exclusionary effect—a "mission impossible" in terms of litigation costs. This would have also seriously affected incentives to provide discounts that may benefit consumers. This constitutes, however, a second-best solution in comparison to a cost benefit analysis approach that would impose a symmetrical standard of proof for anticompetitive effects and possible justifications.

Third, the link between the classification of price and non-price related conduct and the interpretation of the concept of consumer harm (which is the reference point to measure anticompetitive effects) is missing. The Commission defines the concept of consumer harm broadly as covering not only restraints that affect competition through lower prices, but also those affecting the possibility for consumers to benefit from better quality products and wider choice of new or improved goods and services.[112] The underlying objectives of Article 82, in particular its emphasis on preserving consumer choice, may explain the relatively strict antitrust standards that apply to technical tying, in comparison to contractual tying.[113] It is clear that the Commission does not establish a hierarchy between these different aspects of consumer harm.

Fourth, the introduction of the price/non-price dichotomy in EC competition law is also at odds with recent developments in U.S. antitrust law. In *Pacific Bell v. linkLine*, the U.S. Supreme Court made clear that "there is no reason to distinguish between price and nonprice components of a transaction" and consequently found that its reasoning in *Trinko* (involving an insufficient assistance claim by a competitor) applied "with equal force to price-squeeze claims."[114] What counts is the effect of the specific conduct on consumers, not the price or non-price label attached to it by the plaintiff/claimant or the defendant.

Fifth, as we have previously observed, the Commission's *Guidance* does not take seriously into consideration that even an inefficient competitor

[111] On this asymmetry see our discussion *infra* Part II.A.

[112] *Guidance*, *supra* note 70, ¶ 5.

[113] *Id.* ¶ 53. The main justifications provided for this classification are that technical tying is costly to reverse and that it also reduces the opportunities for resale of individual components.

[114] Pacific Bell Tel. Co. v. linkLine Commc'ns, Inc., 129 S. Ct. 1109, 1119 (2009).

can constrain a dominant firm's pricing and thereby increase consumer surplus. The test, therefore, runs the high risk of being under-inclusive.[115] This is certainly not a concern for those advancing the need for a safe harbor for bundling because they focus primarily or entirely on productive efficiency.[116] However, this is certainly neither the case in EC competition law[117] nor in U.S. antitrust law.[118]

Sixth, in the presence of product differentiation (either in variety or in quality) the *Guidance*'s test makes little sense. Because a rival to the dominant firm does not offer the same products, why should courts use the dominant firm's costs to evaluate the survival of the rival's products that differ in quality and variety from those of the dominant firm?[119] Moreover, when the products are differentiated, consumers may gain

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[115] See the analysis in Economides, *supra* note 94, at 268–69, 278.

[116] *See* Dennis W. Carlton, *Does Antitrust Need to Be Modernized?* 2 (Econ. Analysis Group, Discussion Paper No. 07-3, 2007), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=956930; Dennis W. Carlton & Michael Waldman, *Safe Harbors for Quantity Discounts and Bundling* (Econ. Analysis Group, Discussion Paper No. 08-1, 2008), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1089202; Dennis W. Carlton & Ken Heyer, *Appropriate Antitrust Policy Towards Single-Firm Conduct* (Econ. Analysis Group, Discussion Paper No. 08-2, 2008), *available* at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1111665.

[117] Case T-168/01, GlaxoSmithKline Servs. Unlimited v. Comm'n, 2006 E.C.R. II-2969, ¶ 118 (Ct. First Instance) (the protection of the welfare of final consumers constitutes the objective of Article 81(1)); *But see* Joined Cases C-501, 513, 515 & 519/06, GlaxoSmithKline Servs. Unlimited v. Comm'n, ¶ 63 (Eur. Ct. Justice, Oct. 6, 2009) (on Article 81: "[T]here is nothing in that provision to indicate that only those agreements which deprive consumers of certain advantages may have an anti-competitive object. Secondly, it must be borne in mind that the Court has held that, like other competition rules laid down in the Treaty, Article 81 EC aims to protect not only the interests of competitors or of consumers, but also the structure of the market and, in so doing, competition as such. Consequently, for a finding that an agreement has an anti-competitive object, it is not necessary that final consumers be deprived of the advantages of effective competition in terms of supply or price"), *available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:62006J0501:EN:HTML. This case law is not incompatible with emphasis on long term consumer interest: *See* Joined Cases C-468/06 to C-478/06, Sot. Lélos kai Sia EE v. GlaxoSmithKline AEVE Farmakeftikon Proionton, ¶ 66 (Eur. Ct. Justice, Sept. 16, 2008) (*Sot. Lélos kai Sia*) (noting that "there can be no escape from the prohibition laid down in Article 82 EC for the practices of an undertaking in a dominant position which are aimed at avoiding all parallel exports from a Member State to other Member States, practices which, by partitioning the national markets, neutralise the benefits of effective competition in terms of the supply and the prices that those exports would obtain *for final consumers* in the other Member States.") (emphasis added), *available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:62006J0468:EN:HTML. This focus on consumer interest also explains the strict pass-on requirement to consumers for any efficiency gains that the defendant advances as a justification for anticompetitive effects. Commission Notice on the Guidelines on the Application of Article 81(3) of the Treaty, 2004 O.J. (C 101) 97, ¶¶ 85–86. The same principle applies in the context of Article 82. *See Guidance*, *supra* note 70, ¶ 30.

[118] See the analysis in Elhauge, *supra* note 435–39, at 37–41.

[119] See the analysis in Economides, *supra* note 94, at 269.

from the presence of additional varieties and qualities offered by the rival even if the rival prices higher than the dominant firm.[120] The protection of variety and quality are important objectives of EC competition law, according to the Commission's *Guidance*.[121]

Finally, the *Guidance*'s test is based on a mistaken distinction between contractual/technological tying and bundled discounts, which, as previously explained, is not compatible with the objectives of EC competition law and leads to the application of different standards, although both practices may produce similar anticompetitive effects. The test suggested in the Commission's *Guidance* does not make clear how mixed bundling is different from tying. This is an important consideration, as the equally efficient competitor test does not apply to tying, while it would apply to mixed bundling. This raises the issue of the existence of an effective and practical tool to distinguish between the two practices. It would make no sense to have a price/cost test for mixed bundling if the same practice also could be analyzed under the anticompetitive foreclosure approach of tying.

As will become clear from the analysis in the following section, U.S. and EC competition law employ two criteria to distinguish between tying and single-product discount practices and between tying and mixed bundling—respectively, the requirements of the existence of distinct products and that of coercion.

### C. The Case for an Anticompetitive Foreclosure Test: A Unified Standard for Bundled Discounts and Tying

There are a number of economic and legal arguments that, in our view, shift the balance in favor of an anticompetitive foreclosure test for all bundling practices. The economic arguments relate to the anticompetitive harm of bundled discounts and to the need for inclusive antitrust standards. The legal arguments relate essentially to the difficulty of distinguishing between bundled discounts and tying, which is an argument in favor of a unified approach to these practices.

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[120] *See* Steven C. Salop, *Question: What Is the Real and Proper Antitrust Welfare Standard? Answer: The* True *Consumer Welfare Standard* (Nov. 4, 2005) (statement to the AMC), *available at* http://govinfo.library.unt.edu/amc/public_studies_fr28902/exclus_conduct_pdf/051104_Salop_Mergers.pdf; Steven C. Salop, *Exclusionary Conduct, Effect on Consumers, and the Flawed Profit-Sacrifice Standard*, 73 ANTITRUST L.J. 311 (2006); Nicholas Economides, *Quality Variations in the Circular Model of Variety-Differentiated Products*, 23 REGIONAL SCI. & URB. ECON. 235 (1993).

[121] *Guidance*, *supra* note 70, ¶¶ 5–6.

### 1. *The Case for an Anticompetitive Foreclosure Test from an Economic Perspective*

As a matter of economics, the modified predatory pricing test of the Ninth Circuit can result in a finding of no liability even when there are anticompetitive effects. First, even if one believes that bundling will be anticompetitive only when allocating the discount from all products to the competitive product(s) results in an effective price below some measure of unit cost, average variable cost is not the appropriate measure of cost. Firms need to cover their fixed costs as well to stay in business. Thus, the appropriate measure of cost should be average total cost, which includes a per-unit (average) allocation of fixed cost. For example, to say an action is not anticompetitive when a firm prices above average variable cost but below average total cost makes no sense because a firm will not be able to survive in business in the long run under this pricing. Such pricing involves a short-run profit sacrifice, is not part of normal firm behavior, and is highly suspect as to its anticompetitive motive. An antitrust standard should not condone a dominant firm's behavior that imposes pricing on equally efficient competitors that does not allow them to survive in the long run.

Second, an entrant may have higher unit costs because foreclosure as a result of bundling reduced its scale of operations. Thus, specifying a test that relies on the unit costs of the dominant firm (given the higher scale of its operations) can easily result in an incorrect finding of no liability and false negatives.

Third, attention should be paid to the effects of the bundling strategies on consumer surplus. Use of bundling strategies can lead to the exclusion of one or more competitors. In turn, this can decrease consumer surplus, even when the excluded entrant is less efficient than the incumbent. Entry constrains pricing, and even entry by less efficient entrants can lead to lower prices.[122] Thus, excluding entrants on the grounds of productive inefficiency (or creating tests that would exclude less efficient entrants out of hand) can reduce consumer surplus and increase allocative inefficiency (divergence of prices from costs).[123]

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[122] *See, e.g.*, Jonathan B. Baker, *Predatory Pricing After* Brooke Group: *An Economic Perspective*, 62 ANTITRUST L.J. 585, 591 (1994) ("A firm can deter aggressive competition with a low price, even if the low price exceeds the price-cutter's average cost, so long as the price is sufficiently low relative to its rivals' cost. Hence, it is possible that competition can be harmed by low prices even if those prices are not below the price-cutter's cost." (footnote omitted)).

[123] This can be true in a variety of situations. For example, the "Efficient Components Pricing Rule" (ECPR) that determines prices for components in systems was proposed as a way to keep inefficient entrants out of the market. *See* William J. Baumol, *Some Subtle*

Fourth, even starting from monopoly in one product and competition or oligopoly in a second product (or in more products), the introduction of mixed bundling strategies—where products are offered undiscounted à la carte as well as at a discounted price only to a customer committing to buy at least x percent of his needs in all the bundled products from the same firm—can lead to a reduction in consumer surplus.[124] The monopolist can set an à la carte price above the monopoly price and charge approximately the monopoly price for the monopolized good under the bundle/requirements contract. The introduction of the bundle can make consumers worse off even where they have the choice of whether or not to accept the terms of the bundle. Even where, after the introduction of the bundle, each consumer is better off buying the bundle rather than buying at the à la carte prices available in the presence of the bundle, the aggregate effect of these decisions to buy the bundle allows the monopolist to set pricing so that it extracts more surplus than in unbundled monopoly.[125]

Fifth, bundling also can be used to create threats of higher à la carte prices, even if all consumers buy under the bundle and therefore the

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*Pricing Issues in Railroad Regulation*, 10 INT'L J. TRANSPORT ECON. 341 (1983); Robert D. Willig, *The Theory of Network Access Pricing*, *in* ISSUES IN PUBLIC UTILITY REGULATION 109 (Harry M. Trebing ed., 1979). However, it has been shown that allowing even (moderately) inefficient entrants to enter the market increases consumers' surplus because it decreases prices and reduces the allocative inefficiency of monopoly. *See* Nicholas Economides & Lawrence J. White, *Access and Interconnection Pricing: How Efficient Is the "Efficient Component Pricing Rule"?*, 40 ANTITRUST BULL. 557 (1995); Nicholas Economides & Lawrence J. White, *The Inefficiency of the ECPR Yet Again: A Reply to Larson*, 43 ANTITRUST BULL. 429 (1998); Nicholas Economides, *The Tragic Inefficiency of M-ECPR*, *in* DOWN TO THE WIRE: STUDIES IN THE DIFFUSION AND REGULATION OF TELECOMMUNICATIONS TECHNOLOGIES 142 (Allan L. Shampine ed., 2003).

[124] *See, e.g.*, Greenlee et al., *supra* note 10. This paper shows how a monopolist can extend its monopoly in the first market to the second market through offering a bundling scheme with a requirement that all or almost all purchases are made from the monopolist, and simultaneously increase the price of the monopolized product when it is offered on a stand-alone basis. Greenlee et al. show in Theorem 2 (*id.* at 11) that the application of this bundling scheme reduces consumers' welfare. They show that consumers can be made worse off even when they have the choice of whether or not to take the bundle. Moreover, Greenlee et al. devise a test to ascertain if there are consumer losses: "[I]f the firm maximizes profits and the standalone price of A exceeds the initial price of A, then we can infer that the bundled rebate reduces consumer welfare." *Id.* at 32; *see also* Barry J. Nalebuff, *Bundling as a Way to Leverage Monopoly* 14–15 (Yale Sch. of Mgmt., Research Paper Series, Working Paper No. ES-36, 2004), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=586648.

[125] Because the prices for some bundles under the commitment contract are better than the à la carte ones, it is individually rational for some consumers to buy under the bundle. However, collectively these actions of consumers strengthen the monopolist and allow it to increase both the à la carte and bundle prices.

threat of buying at higher à la carte prices is not enforced at equilibrium.[126]

Sixth, the "discount" in the price of the bundle can be illusory as the à la carte price can be increased simultaneously with the offer of the bundle by more than the discount so that, in the end, the consumer who buys the bundle pays more than before the bundle was offered.[127] This strategy results in consumers buying the competitive good from the monopolist (of the first good) under the bundle, leading to (i) lower consumer surplus; and (ii) foreclosure of competitors in the "competitive" good(s). The fact that some buyers may agree to buy under the bundling contract does not contradict the illusory nature of the discount or that consumers may be worse off after the introduction of the bundling scheme. A buyer faced with an à la carte price and an effectively lower price for some bundles under the requirement contract may choose to buy under the bundling/requirement contract. As more buyers buy under the bundling/requirement contract, the market power of the dominant firm increases. As a result, the dominant firm is able to increase price above the ex ante pre-bundling price (even if that price was the original monopoly price) so that buyers buying under the bundling contract pay more than before the bundling scheme was introduced, and therefore the "discount" offered by the bundle is illusory. Buyers who do not buy under the bundling contract are even worse off.[128]

From the point of view of the buyers, this is similar to the classic "prisoner's dilemma," in which each of two prisoners is offered a chance to talk about the other prisoner's crimes in exchange for a lighter sentence. No matter what the other prisoner does, each prisoner would like to talk to make his sentence lighter. However, if both prisoners talk, they end up with heavier sentences than if they had both stayed silent. Here, a buyer offered the bundling/requirement scheme may be willing to accept it because he gets a lower price for some bundles compared to à

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[126] *See, e.g.*, Barry Nalebuff, *Tried and True Exclusion: Comment on Jean Tirole's "The Analysis of Tying Cases,"* COMPETITION POL'Y INT'L, Spring 2005, at 41.

[127] Daniel Rubinfeld calls such a discount a "'sham' discount." Rubinfeld, *supra* note 10, at 252.

[128] When a buyer buys more than one unit, he has positive consumer surplus left even at monopoly pricing. The bundling/requirement contract allows the dominant firm to take away from consumers some of this surplus. This fact was missed by the Chicago School analysis, which advanced that a firm with a monopoly in one product cannot increase its monopoly profit by leveraging through bundling/tying its monopoly into a second monopoly in another product (*see* Aaron Director & Edward H. Levi, *Law and the Future: Trade Regulation*, 51 NW. U. L. REV. 281, 290–92 (1956); Ward S. Bowman, Jr., *Tying Arrangements and the Leverage Problem*, 67 YALE L.J. 19, 20–23 (1957); ROBERT H. BORK, THE ANTITRUST PARADOX 372–75, 380–81 (1978); RICHARD A. POSNER, ANTITRUST LAW 198–99 (2d ed. 2001)) because it typically assumed single-unit purchasers.

la carte from the dominant seller—this is akin to the prisoner talking to reduce his sentence. However, as more buyers accept the bundling/requirement scheme, the dominant firm's market power increases. As a result, it is able to charge even higher prices. Like the prisoners, the buyers are worse off after more of them accept the deal.

Seventh, the bundling strategy will tend to foreclose competitors in the second (non-monopolized) market, so that in the long run they are eliminated from the second market, and, to the extent that re-entry is not easy, the monopolist will have a free rein to set an even higher price in the second market in the future. Thus, foreclosure of competitors can further reduce consumer surplus in the medium and long run.

Eighth, bundling may be used as an entry-deterring device by making it economically unprofitable for an entrant to enter one market without simultaneously entering the second market.[129]

As a matter of principle, a major implication of what we refer to here as a predatory bundling analogy for all bundling practices would be to allow for a safe harbor test for dominant firms based on an "equally efficient" principle and make it more difficult for the plaintiff to bring a case. The significant part of the debate is about allocating the burden of proof that the defendant is at least as efficient a producer as the plaintiff and that therefore the exclusion of the latter is the consequence of business acumen and superior efficiency. One could consider that an anticompetitive foreclosure test assumes that this is the case: if the defendant were as efficient as the plaintiff in the market of the competitive product, then there is no need to bundle the sale of this product with discounts in lines of products that are not within the plaintiff's product range. The defendant could have simply offered, as a least restrictive to competition alternative, single product discounts for the competitive product that could match or even be lower than the price charged by his rival.

Certainly, there may be efficiency reasons that could explain the decision of a firm to bundle products, such as cost savings in production (e.g., joint costs), distribution, or price discrimination.[130] Tying is a common practice in competitive markets as firms often compete with bundles of products and consumers are offered discounts if they buy the products that are part of the bundle. Evidence from the pervasive use of

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[129] *See, e.g.*, Nalebuff, *supra* note 10; Rubinfeld, *supra* note 10, at 257; Aaron S. Edlin & Daniel L. Rubinfeld, *Exclusion or Efficient Pricing? The "Big Deal" Bundling of Academic Journals*, 72 ANTITRUST L.J. 119 (2004).

[130] David S. Evans & Michael Salinger, *Why Do Firms Bundle and Tie? Evidence from Competitive Markets and Implications for Tying Law*, 22 YALE J. ON REG. 37, 41–42 (2005).

bundling in competitive markets would thus require the competition authorities or courts to adopt prima facie a positive view of such practices, unless they are used by firms with a dominant position and may exclude competitors that cannot offer the same bundle of items. The analysis of the practice under a rule of reason that would balance procompetitive and anticompetitive effects would thus be an adequate antitrust standard.[131] This is the position taken by the Third Circuit in *LePage's*.

Some authors nevertheless have advanced the view that the application of the rule of reason anticompetitive foreclosure test to bundled discounts could still lead to false positives, in view of the difficulty of documenting efficiencies.[132] They suggest the adoption of a cost-based standard that would operate as a safe harbor for bundled discounts.[133] It is only if a rival as efficient as the dominant firm would be excluded from the market that the necessary costs of an extensive rule of reason inquiry should be incurred.[134] The underlying assumption is that firms should be free in defining their pricing strategies. It also is based on the belief that pricing restraints should be subject to the more restrictive (for plaintiffs) antitrust analysis for predatory pricing. The inquiry would be whether the incremental price for the tied product (that is, price under the bundle reduced by the allocation of the total discount for the whole bundle to the tied product) is below the defendant's average variable cost of producing the tied product.[135] The assumption is that lower prices indicate superior efficiency and that they will presumptively benefit consumers. Such an assumption is more difficult to substantiate in contractual restraints, such as exclusive dealing or tying.[136] It is worth noting, however, that most of these bundled rebates are offered to distributors, not to the final consumer.[137] There is no reason to presume that distributors will not increase their margins instead of reducing the prices to the final consumer, in the absence of potential or actual competition in the downstream market. Furthermore, in practically all the cases on bundled rebates the discount was granted only

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[131] In this case, the legal burden of proof will rest on the plaintiff, while the defendant will bear the evidentiary burden of substantiating the procompetitive efficiency justifications for the bundled discount, after the plaintiff brought evidence of an anticompetitive foreclosure effect.

[132] *See, e.g.*, Evans & Salinger, *supra* note 130, at 83.

[133] *See, e.g.*, Hovenkamp, *supra* note 10, at 854.

[134] Cascade Health Solutions v. PeaceHealth, 515 F.3d 883, 909 (9th Cir. 2008).

[135] *Id.* at 912–13.

[136] *See* Popofsky, *supra* note 105.

[137] *See* Benjamin Klein, *Bundled Discounts as Competition for Distribution*, GLOBAL COMPETITION POL'Y, June 2008, http://www.globalcompetitionpolicy.org.

through a commitment to buy a certain market share from the dominant supplier, which was done by contract.

Critics also assert that a predatory bundling test does not take into account the fact that bundled discounts may be a way for a dominant firm to impair the efficiency of its rivals because rivals that have a long run cost curve that is as low as the defendant's (and therefore are equally efficient in the long run) would be "unable to achieve a price as low as the defendant's [average] total costs precisely because the foreclosure has relegated them to the high cost portion of their cost curve."[138]

Furthermore, they impose on the plaintiff an important hurdle, as cost data of rivals may be hard to find. Indeed, one of the implications of a price/cost test is to reverse the allocation of the burden of proof for efficiencies. In the anticompetitive foreclosure test, the defendant should establish efficiency gains after the plaintiff has substantiated consumer harm. In the modified predatory price test, the plaintiff should prove from the outset that the excluded rival is at least as efficient as the dominant firm. Is this second screen necessary? It is generally argued that the cost/price test increases the predictability of antitrust rules for business.[139] This is certainly a valid argument, which can be extended to any type of antitrust violation examined under the rule of reason.[140] Does this mean that we should introduce a cost/price test for all rule of reason antitrust cases? We do not think so.

Finally, we question the position that antitrust concerns should be limited to practices that exclude equally efficient firms. Excluding less efficient rivals may also produce a negative consumer welfare effect if it removes a competitive constraint on the market power of the defendant and thus allows the defendant to raise prices and reduce consumer surplus while the effects on total surplus are ambiguous, as discussed earlier.[141] Indeed, the protection of the final consumer from wealth transfers may be the primary objective of antitrust law,[142] imposing a strict pass-on requirement for any efficiency gains that the defendant advances as a justification for the adoption of a specific practice.

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[138] EINER ELHAUGE & DAMIEN GERADIN, GLOBAL COMPETITION LAW AND ECONOMICS 576 (2007).

[139] *See* DOJ SECTION 2 REPORT, *supra* note 13, at 97.

[140] *See* Maurice E. Stucke, *Does the Rule of Reason Violate the Rule of Law?*, 42 U.C. DAVIS L. REV. 1375 (2009).

[141] *See* Elhauge, *supra* note 8; Einer Elhauge, *Defining Better Monopolization Standards*, 56 STAN. L. REV. 253, 320–23 (2003).

[142] *See* Robert H. Lande, *Wealth Transfers as the Original and Primary Concern of Antitrust: The Efficiency Interpretation Challenged*, 34 HASTINGS L.J. 65 (1982).

### 2. *The Case for an Anticompetitive Foreclosure Test from a Legal Perspective*

The analysis of bundled discounts under a predatory pricing standard in the United States and the Commission's *Guidance* paper's use of a cost/price standard for rebates are in sharp contrast to the foreclosure test applied to tying practices in the United States and Europe. This confirms that the threshold process of characterization of the specific facts—as constituting tying or multi-product rebates (mixed bundling)—should precede the step of examining the anticompetitive effects of the practice under either the foreclosure or the cost/price based test. One, however, could advocate a common standard for all bundling practices, whether or not traditionally characterized as tying. Jean Tirole suggests a predation test for tying practices that would include the analysis of the likelihood of tying to reduce competition in the tied market (step 1), the likelihood of tying to hurt consumers (step 2), as well as a recoupment test (step 3).[143] According to this view, tying is a tool for non-price predation, which is defined as "a voluntary and temporary loss in profit that can be rationalized only through a contemplated and substantial increase in the rival's probability of exit and the subsequent ability to recoup losses."[144] This proposal is not, however, clear as to which criterion should be used to measure loss (and the adequate measure of costs) in this circumstance.

Interestingly, both the European Commission and the U.S. courts that advocate a cost/price-based standard for bundled discounts continue to employ a specific anticompetitive foreclosure standard for tying. Although this may be driven by prior case law, analytically, from a consumer welfare perspective, it seems to be an inconsistent approach; if a predatory cost/price test should be the standard for bundled discounts, there is no reason why the same should also not be true for tying.[145] The application of a predation test to tying practices would, of course, likely be controversial as it would lead to under-enforcement and false nega-

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[143] Jean Tirole, *The Analysis of Tying Cases: A Primer*, COMPETITION POL'Y INT'L, Autumn 2005, at 1.

[144] *Id.* at 20. For a different definition of non-price predation that emphasizes the probability of raising rivals' costs strategies even in the absence of a profit sacrifice in the short run, see Thomas G. Krattenmaker & Steven C. Salop, *Anticompetitive Exclusion: Raising Rivals' Costs to Achieve Power over Price*, 96 YALE L.J. 209, 224 (1986).

[145] Although the *DOJ Section 2 Report* stated that "The Department believes that the potential competitive harm of bundled discounting more closely resembles that from tying than that from predatory pricing" when bundle-to-bundle competition is not reasonably possible "because of the inability of any substantial competitor or group of competitors to provide a similar range of items," it advocated an anticompetitive foreclosure approach for tying, without suggesting any additional safe harbor. No clear explanation is given for this conceptual inconsistency. DOJ SECTION 2 REPORT, *supra* note 13, at 101; *see also id.* at 90 (tying).

tives, and it would conflict with well-established case law of the U.S. Supreme Court and the European Courts. Such a test has not yet been suggested by either the EU or the U.S. antitrust authorities.

With the uniform foreclosure standard we are proposing for assessing both bundling and tying, several of the historical tying elements take a different meaning or become superfluous. For example, under our proposed uniform foreclosure standard approach, the distinct/separate product rule, which is the first step of the antitrust analysis of tying cases in the European Union and the United States, would operate as a distinguishing criterion between bundling and single-product rebates, should the latter be subject to a different antitrust standard. Likewise, a careful consideration of the coercion test, which has traditionally been the third step of an antitrust claim in both jurisdictions, shows that it is redundant and should not form a separate step in the competition assessment of tying but rather be integrated in the analysis of the existence of an anticompetitive foreclosure, as we will argue in our last section.

### 3. *The Rationale of the Separate Products Test: Establishing the Boundaries of the Bundling Antitrust Category*

The judicial test for tying practices in Europe follows similar steps to that for tying in the United States. There is anticompetitive tying if (i) the tying and the tied products are two separate (distinct) products; (ii) the undertaking concerned is dominant (or has market power) in the market for the tying product (there is market power in the market for the tying product);[146] (iii) the practice (an agreement or technological integration) does not give customers a choice to obtain the tying product without the tied product (coercion); and (iv) the practice in question forecloses competition (there are anticompetitive effects in the tied market). The CFI also accepted in *Microsoft* that the Commission correctly examined the objective justifications of the conduct that were ad-

[146] Although the CFI and the U.S. courts consider that the requirement of two distinct products constitutes the first step of the competition assessment of tying, the *Discussion Paper, supra* note 70, reverses the order and requires first evidence of a dominant position before moving to the separate products requirement. The CFI's approach in *Microsoft* has the benefit of unifying the standard for tying for Article 81 and Article 82 cases because the existence of market power in the tying product market also constitutes a prerequisite for the application of Article 81 since the adoption of the Guidelines on Vertical Restraints. *See* Commission Notice on the Guidelines on Vertical Restraints, 2000 O.J. (C 291) 1, ¶¶ 219–220. Furthermore, it makes more sense to determine if the alleged tying and tied products are distinct before analyzing the existence of a dominant position or market power on the tying-product market.

vanced by Microsoft[147] and referred to this condition as the fifth step of the analysis.[148]

The separate/distinct product test fulfills two objectives: first, it is a proxy for efficiency gains, thus excluding from further antitrust assessment practices that have an obvious efficiency justification that benefits consumers; and second, it sets the boundaries of the bundling antitrust category, as opposed to practices involving a single product. While the first reason may still be valid, if the antitrust standards for bundled rebates are similar to those applying to single-product rebates, the second rationale for the distinct product test may be questioned in this case.

As concerns the utility of the coercion requirement, its function is merely to distinguish between different forms of bundling practices, such as technological tying, contractual tying, and mixed bundling (commercial tying). We argue that the coercion criterion should be abandoned because it offers little information in terms of anticompetitive effects and consumer harm, in particular if one rejects, as we do, the assumption that price competition is more valuable to consumers than non-price competition. .

#### a. The Separate Products Test in EC Competition Law

The separate products test is the first step of the analysis of anticompetitive tying for the purposes of Articles 81 and 82. It also is a requirement in U.S. antitrust law for tying arrangements. This derives from *Jefferson Parish*, a Section 1 Sherman Act case, although the case law does not seem to require a separate products test for non-contractual tying under Section 2 of the Sherman Act.[149] This approach presents important advantages, as our analysis will demonstrate.

The main function of the two distinct products requirement is to serve as a screening device to take into account apparent efficiency gains that follow from the bundling of two separate products. Two items may be considered to be a single product for the purposes of the law of tying when they are subject to certain economies of joint production or distribution that can be achieved only if all customers can be forced to take

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[147] *Microsoft CFI Decision*, *supra* note 5, ¶ 858.

[148] *Id.* ¶ 869; *see also Guidance*, *supra* note 70, ¶ 62.

[149] *See* HERBERT HOVENKAMP, FEDERAL ANTITRUST POLICY 306 & n.25 (3d ed. 2005) ("[T]he § 2 decisions on forced bundling generally do not discuss the 'separate product' requirement in tying cases, because they do not follow the tying logic at all; rather they go straight to the question whether the practice is exclusionary under the circumstances.").

the entire package.[150] In *Tetra Pak II*, the ECJ observed that "even where tied sales of two products are in accordance with commercial usage or there is a natural link between the two products in question [therefore they are single products in the sense of consumer demand], such sales may still constitute abuse within the meaning of Article [82] unless they are objectively justified."[151] This arguably suggests that even if the two items are considered to be a single product for the purposes of tying, it is still possible that Article 82 will apply if the other conditions of anticompetitive tying are fulfilled. This interpretation finds support in *Microsoft*, where the CFI remarked that it is difficult to speak of "commercial usage or practice in an industry that is 95% controlled by Microsoft."[152] The condition of the existence of two separate products will become devoid of purpose if the commercial usage is defined by the practice of a dominant firm in the market. It seems, therefore, that if this requirement also applies for the application of Article 82 in situations of "super dominant position,"[153] such as in *Microsoft,* it is because it fulfills an additional objective other than simply being a screening device for the efficiency of the bundling practice.

The definition of what constitutes a distinct product may shed light on the real objective of this element. The Commission officials advanced the position in the *Discussion Paper*, as well as in the Commission's *Microsoft* decision, that "products are distinct if, in the absence of tying or bundling, from the customers' perspective, the products are or would be purchased separately."[154] The distinct product test does not necessarily constitute a relevant market test.[155] In the *Discussion Paper*, the Commission's staff relied on direct evidence of consumer demand for this requirement, such as the fact that the consumers purchase the products separately when given a choice, or indirect evidence, such as the fact that firms in competitive markets tend to tie the products together. The Commission's *Guidance* also relies on direct evidence of the distinctiveness of the products, such as "when given a choice, customers

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[150] *See* Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 40–41 (1984) (O'Connor, J., concurring); Jack Walters & Sons Corp. v. Morton Bldg., Inc., 737 F.2d 698, 703 (7th Cir. 1984).

[151] Case C-333/94, Tetra Pak Int'l SA v. Comm'n, 1996 E.C.R. I-5951, ¶ 37 (Eur. Ct. Justice).

[152] *Microsoft CFI Decision*, *supra* note 5, ¶ 910.

[153] The expression refers to a situation of a firm benefiting from an overwhelming dominant position in the market. *See* Case C-395/96, Compagnie Maritime Belge Transports SA v. Comm'n, 2000 E.C.R. I-1365, ¶¶ 114–120 (Eur. Ct. Justice).

[154] *Discussion Paper*, *supra* note 70, ¶ 185; *Microsoft Comm'n Decision*, *supra* note 3, ¶ 803.

[155] *Id.* ("It is, however, not necessary that the two products belong to two separate product markets. In a market with differentiated products, two products may be sufficiently differentiated that a company can be said to tie or bundle two distinct products.").

purchase the tying and the tied products separately from different sources of supply."[156] According to the CFI in *Microsoft*, the distinctness of products for the purpose of applying Article 82 "has to be assessed by reference to customer demand," and "in the absence of independent demand for the allegedly tied product, there can be no question of separate products and no abusive tying."[157]

Nevertheless, in *Microsoft*, the Commission did not focus only on customer demand but accorded at least equal importance to the supply side of the tied product's market:

> The distinctness of products for the purposes of an analysis under Article 82 therefore has to be assessed with a view to consumer demand. If there is no independent demand for an allegedly "tied" product, then the products at issue are not distinct and a tying charge will be to no avail.
>
> *The fact that the market provides media players separately is evidence for separate consumer demand for media players, distinguishable from the demand for client PC operating systems.* There is, therefore, a separate market for these products. There are vendors who develop and supply media players on a stand-alone basis, separate from PC operating systems.[158]

The CFI refused Microsoft's argument that the Commission should have examined instead if the tying product was regularly offered without the tied product or whether customers wanted Windows without media functionality. If this were the case, complementary products could not constitute separate products for the purposes of Article 82.[159] The court noted that "it is quite possible that customers will wish to obtain the products together, *but from different sources*."[160] The existence of different sources of supply and, in particular, of competing suppliers of the alleged tied product were influential factors in concluding that the products were distinct.[161] The CFI followed previous case law of the ECJ holding that the presence in the market of independent companies specializing in the manufacture and sale of the tied product constitutes serious evidence of the existence of a separate market for that product.[162] In

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[156] *Guidance*, *supra* note 70, ¶ 51.
[157] *Microsoft CFI Decision*, *supra* note 5, ¶¶ 917–918.
[158] *Microsoft Comm'n Decision*, *supra* note 3, ¶¶ 803–804 (footnote omitted) (emphasis added).
[159] *Microsoft CFI Decision*, *supra* note 5, ¶ 921.
[160] *Id.* ¶ 922 (emphasis added).
[161] Although the CFI also noted that "a not insignificant number of customers continue to acquire media players from Microsoft's competitors, separately from their client PC operating system, which shows that they regard the two products as separate." *Id.* ¶ 932.
[162] *See* Case C-333/94, Tetra Pak Int'l SA v. Comm'n, 1996 E.C.R. I-5951, ¶ 36 (Eur. Ct. Justice).

contrast, the *Discussion Paper* embraced a demand-oriented test: although the existence of independent suppliers constituted indirect evidence of a separate consumer demand, this factor did not in itself play a decisive role in the inquiry on the existence of a distinct product.[163] The Commission's *Guidance* retreats from this more demand-oriented test and emphasizes again the supply side: "Two products are distinct if, in the absence of tying or bundling, a substantial number of customers would purchase or would have purchased the tying product without also buying the tied product from the same supplier, *thereby allowing stand-alone production for both the tying and the tied product.*"[164] Again, the presence of undertakings specialized in the manufacture and sale of the tied product without the tying product constitutes indirect evidence of the distinctness of the products.

The approach of the CFI makes sense if one considers this element in light of the interpretation by the court of the fourth condition of tying: foreclosure of competition. The court assumed that the foreclosure of competitors in the specific circumstances of this case led to consumer detriment, in the sense that consumers' choice and innovation were restricted. A focus on consumer demand—at least as this concept is perceived in defining a relevant market—simply does not address this type of anticompetitive harm as it generally centers on cross-price elasticity of demand.

The CFI also noted that IT and communications industries develop rapidly and, over time, separate products might become unified.[165] This did not impede the court from assessing the existence of distinct products "by reference to the factual and technical situation that existed at the time when . . . the impugned conduct became harmful."[166] The supply-oriented character of the distinct product test is directly related to the emphasis the court put on the exclusion of rival suppliers of streaming media players, and it constitutes one of the main points of difference with the interpretation of this test in U.S. antitrust law.

b. A Comparison with the Distinct Product Test in U.S. Antitrust Law

In U.S. antitrust law, the tying and tied products are separate if "the tying item is commonly sold separately from the tied item in a well func-

[163] *Discussion Paper*, *supra* note 70, ¶ 186.

[164] *Guidance*, *supra* note 70, ¶ 51 (emphasis added).

[165] *Microsoft CFI Decision*, *supra* note 5, ¶ 913. The court accepted that "consumers want to find a media player pre-installed on their computers." *Id.* ¶ 904.

[166] *Id.* ¶ 914.

tioning market."[167] The test is whether there is sufficient consumer demand in the marketplace to support independent markets despite any efficiencies tying may bring. The D.C. Circuit mentioned in *United States v. Microsoft* that "perceptible separate demand is inversely proportional to net efficiencies."[168] Separate demand for the tied product indicates that the efficiencies provided by the bundling practice to consumers are limited. However, the existence in the market of independent companies specializing in the manufacture and sale of the tied product does not by itself constitute adequate evidence of a distinct product under U.S. antitrust law, as is the case in Europe. Bundling can be efficiency enhancing if the tying and the tied products are used in fixed proportions and have no separate utility, as the dominant firm has the incentive to tie into the competitive market only if the combination is more efficient.[169] By contrast, tying with variable proportions may be a vehicle for price discrimination and thus lead to a reduction of consumer surplus by profitably extracting consumer surplus from individual buyers.[170]

This explains why in *United States v. Microsoft*, where Internet Explorer and Windows were used in fixed proportions, the D.C. Circuit found merit in Microsoft's argument that, in the circumstances of the case, an abstract consumer demand test would chill innovation to the detriment of consumers by preventing firms from integrating into their products some new functionality that was previously provided by stand-alone products—and hence, by definition, subject to separate consumer demand. In a frequently cited passage, the D.C. Circuit found the *Jefferson Parish* separate products test to be inappropriate:

> The per se rule's direct consumer demand and indirect industry custom inquiries are, as a general matter, backward-looking and therefore systematically poor proxies for overall efficiency in the presence of new and innovative integration. The direct consumer demand test focuses on historic consumer behavior, likely before integration, and the indirect industry custom test looks at firms that, unlike the defendant, may not have integrated the tying and tied goods. Both tests compare incomparables—the defendant's decision to bundle in the presence of integration, on the one hand, and consumer and competitor calcula-

[167] HOVENKAMP, *supra* note 149, at 415 (emphasis omitted).

[168] United States v. Microsoft Corp., 253 F.3d 34, 87–88 (D.C. Cir. 2001) (*Microsoft D.C. Circuit 2001*).

[169] This should not however exclude antitrust liability if the objective of tying is to maintain or protect the degree of tying market power. *See* Elhauge, *supra* note 8, at 446 (citing *Microsoft Corp. v. Commission* as an example of tying with fixed proportions and no separate utility that could help to preserve tying market power). In this case, the distinct product rule should not constitute a filter avoiding a more detailed competition law assessment under the rule of reason.

[170] *See* Bowman, Jr., *supra* note 128, at 20–23.

> tions in its absence, on the other. . . . Because one cannot be sure beneficial integration will be protected by the other elements of the per se rule, simple application of that rule's separate-products test may make consumers worse off.[171]

In contrast to the U.S. view, the position of the CFI in *Microsoft* can hardly be explained by the objective to protect market innovation through product integration. If this were the case, the CFI should have balanced the benefits, from the point of view of the consumers, of having a new integrated product and the costs of the immediate reduction of consumer choice that the bundling of the alleged "distinct products" would have brought. This test could essentially be performed under the step of the analysis of anticompetitive effects (foreclosure of competition). The negative effects on consumers should be balanced against efficiency gains that could be passed on to consumers in the form of new products or better quality. The existence of a full rule of reason test for technological tying in the United States makes possible the full consideration of these efficiencies without necessarily applying the distinct products test. The D.C. Circuit did not refer to the distinct product test in *United States v. Microsoft.* The decision to abandon this condition was intrinsically related to the adoption of a rule of reason instead of a per se approach. The separate product test is transformed to an obvious and significant efficiency inquiry, a position defended by Justice O'Connor in her concurring opinion in *Jefferson Parish*[172] and by the Seventh Circuit.[173]

If the CFI adopted a supply-oriented definition of the distinct product test in *Microsoft,* it is because the main focus of the enquiry was to establish if competitors could viably (profitably) operate in the tied product market. This is relatively easy to prove as the presence in the tied product market of companies that offer only the tied product indicates that there is sufficient consumer demand for the tied product (without the tying product) and therefore that the two products are distinct. It is also clear that a quasi-per se illegality test applies for tying practices in EC competition law. Indeed there is no point in having a distinct product test if the benefits of the single product for the consumers would in any

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[171] *Microsoft D.C. Circuit 2001,* 253 F.3d at 89 (citations omitted).

[172] Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 40 n.8 (1984) (O'Connor, J., concurring) ("When the economic advantages of joint packaging are substantial the package is not appropriately viewed as two products, and that should be the end of the tying inquiry.").

[173] Jack Walters & Sons Corp. v. Morton Bldg., Inc., 737 F.2d 698, 703 (7th Cir. 1984) ("[I]f there are not separate markets, this is evidence that the economies of joint provision are overwhelming.").

case be examined in the next step of the analysis under a rule of reason standard.[174]

A bundling/tying standard that discards the distinct product inquiry certainly would have its detractors. One might argue, for example, that this approach is not an optimal allocation of the burden of proof between the plaintiff and the defendant, which typically would require that the former brings evidence of the absence of any obvious efficiency in bundling the products as well as of an anticompetitive effect before the burden of proof shifts to the dominant firm. But this interpretation is valid only if one considers that the distinct product test focuses on consumer demand and operates as a proxy for examining the obvious and significant efficiencies that the single product would bring to consumers. This interpretation does not fit well, however, with the CFI's assumption that the presence of independent suppliers of the alleged tied product indicates the existence of two distinct products. In this sense, the presence of rivals in the tied market constitutes a proxy for potential anticompetitive foreclosure. This explains why the CFI did not focus only on identifying an independent consumer demand for the tied product but instead looked for evidence that the market included independent companies specializing in the manufacture and sale of the tied product that could have been marginalized or excluded with the tying practice. The distinct product test is therefore intrinsically linked to the CFI's specific approach in interpreting the requirement of anticompetitive foreclosure (an issue we examine in the following section). It follows that although the distinct product test in Europe operates as a proxy for anticompetitive effects, the similar test in the United States indicates the presence of efficiency gains.

#### c. The Distinct Product Test and the Boundaries of the Bundling Antitrust Category

This is not the only function of the distinct product inquiry. The Commission's staff *Discussion Paper* employed the requirement of distinct products to distinguish single branding obligations from bundled discounts and mixed bundling strategies.[175] Rebates that were applied by a dominant company for a particular product and had their possible

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[174] *See Microsoft D.C. Circuit 2001*, 253 F.3d at 96 ("Because courts applying the rule of reason are free to look at both direct and indirect evidence of efficiencies from a tie, there is no need for a screening device as such . . . .").

[175] *Discussion Paper*, *supra* note 70, ¶ 185 n.118 ("Practices involving two or more units of the same product, such as imposing minimum purchasing requirements and giving loyalty rebates, may also be abusive; such practices are analyzed in section 7 on single branding and rebates.").

negative effects *in the market where the firm was dominant* were considered under the rubric of "single branding and rebates" and were subject to a variety of tests, including a predatory cost/price standard for certain types of unconditional rebates. By contrast, single branding obligations and rebates that had effects in *other markets* were considered to be a form of tying/bundling. This implied, as we previously mentioned, that the existence of distinct products would lead to the analysis of the practice under the tying/bundling rubric rather than under the single branding one.[176] The Commission's recent *Guidance* also classifies multi-product rebates as a form of tying/bundling, and the distinct products test constitutes the first step of the analysis under Article 82.[177] The *Guidance* does not, however, distinguish between single branding and multi-product rebates, as was the case in the *Discussion Paper*, probably because the *Guidance* focuses on conditional rebates and ignores single-product unconditional rebates that produce merely exploitative effects. The *Guidance* only refers to two broad categories of exclusionary practices: exclusive dealing and tying/bundling.

This is also the approach followed by the D.C. Circuit in *United States v. Microsoft*, when it examined the price bundling claim of Windows and Internet Explorer.[178] According to the D.C. Circuit, to establish a valid claim for illegal price bundling,[179] the plaintiffs must demonstrate that

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[176] The distinction suggested by the *DOJ Section 2 Report* between situations where bundle-to-bundle competition is reasonably possible (subject to a predatory-pricing safe harbor) and those where bundle-to-bundle competition is not reasonably possible because of the inability of any substantial competitor or group of competitors to provide a similar range of items (subject to the discount-allocation standard) seems to be inspired by the same principle. Contrary to the separate products test of the European Courts, the distinction focuses, however, on the existence of different sources of supply for the tying good (and not the tied good) as an indication of a possibility of bundle-to-bundle competition. The more lenient, for the defendant, predatory pricing standard will apply in this case. The possibility of bundle-to-bundle competition will indicate the existence of a single product. If, however, bundle-to-bundle competition is not reasonably possible, "the discounting more closely resembles that from tying than that from predatory pricing," which indicates the existence of two separate products. Another notable difference with the European supply-oriented separate product test is that it considers that a group of competitors may provide a similar range of items, thus including within the scope of the predatory pricing standard situations where only the dominant firm offers the different items and it faces competition from firms that are present either in the tying or the tied product market, but not both markets. The European separate product test would have in this case identified two separate products and would have applied the tying standard. *See* DOJ SECTION 2 REPORT, *supra* note 13, at 101–02. The current administration has withdrawn the *DOJ Section 2 Report*. *See supra* note 13 and accompanying text.

[177] *Guidance*, *supra* note 70, ¶¶ 50–51.

[178] *Microsoft D.C. Circuit 2001*, 253 F.3d at 96–97.

[179] The allegation of such a claim will depend on evidence that Microsoft charged a price increment for Internet Explorer in Windows. The inquiry is if the price charged for

> the anti-competitive effects of Microsoft's price bundling outweigh any procompetitive justifications the company provides for it. In striking this balance, the District Court should consider, among other things, indirect evidence of efficiency provided by the "competitive fringe." Although this inquiry may overlap with the separate-products screen under the per se rule, that is not its role here. . . . [T]hus, *the separate-products inquiry serves merely to classify arrangements as subject to tying law, as opposed to, say liability for exclusive dealing*.[180]

The main function of the distinct products test in mixed bundling cases is therefore to establish the frontiers of the bundling antitrust category, as opposed to other antitrust categories. In examining the anticompetitive effect of the price bundling, the court affirmed that "there is no claim of price predation," thus indicating that price predation is a separate claim from "price bundling."[181] The distinct products rule thus could indicate the applicable antitrust standard if single product pricing and multi-product rebates or bundling were subject to different standards of antitrust liability: a predatory pricing standard versus an anticompetitive foreclosure standard. The utility of the distinct products requirement would, however, be limited if similar antitrust standards applied to both of these practices.

From a consumer welfare perspective, it makes sense to apply the same antitrust standard for discounts on loyalty/requirement practices irrespective of whether it is a single-product or multi-product case. In the former case, the demand is divided between an uncontested part that is always purchased from the dominant firm and a contested part where the customer may buy from any firm. In both the multi- and single-product cases, the dominant firm leverages its monopoly or dominant position to obtain higher sales in the remaining market. The only difference is that in the multi-product case, sales in market A are leveraged to obtain higher sales in market B, while in the single-product case, the uncontested sales in market A are leveraged to obtain the contested sales also in market A. Both practices reward consumers. Conditional product rebates may produce anticompetitive effects even if the discounted and rival prices are above cost, as they can raise rivals' costs above but-for levels and may discourage price cutting by the firms that use them and their rivals.[182] The most appropriate standard for both

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Windows and Internet Explorer was higher than what would have been the price for Windows alone.

[180] *Id.* (emphasis added) (citation omitted).

[181] *Id.* at 96. It follows that there is no need to bring evidence that the price of the bundle is lower than a specific measure of costs to bring a "price bundling" claim.

[182] *See* Einer Elhauge, *How Loyalty Discounts Can Perversely Discourage Discounting*, 5 J. COMPETITION L. & ECON. 189 (2009).

practices is a structured rule of reason that would look at a number of variables to ascertain whether a loyalty/requirement program violates antitrust law, with the central question being whether the introduction of the loyalty/requirement program reduces consumer surplus.[183] The distinct product rule would in this case be superfluous.

One could nonetheless maintain the distinct products rule as an indication of possible anticompetitive effects (or absence of significant efficiency gains) that would require further analysis under a rule of reason standard. As it is clear from the position of the D.C. Circuit on price bundling, the success of such a claim requires evidence that competing suppliers of the alleged tying product do not sell the bundled (tying and tied) product "*exclusively* at a bundled price."[184] Indeed, if the firms at the competitive fringe were able to offer an unbundled version of the tying product at a lower price than the bundled version, this would indicate that the two products could profitably be offered separately (to the benefit of consumers) and that "at least" for these rivals, the efficiency gains from bundling would "be outweighed by those from separate choice."[185] That finding also would indicate that offering a bundled version is a direct impediment to consumer choice.[186] The court does not explain though if this (more supply-oriented) separate products test obviates the need to prove coercion, which is a requirement for bringing a tying claim, and how the rule of reason would apply in that circumstance.

#### 4. *The "Coercion" Test: Blurring the Lines Between Tying and Mixed Bundling?*

It is a common feature in both EC and U.S. antitrust law that bundling of two distinct products does not constitute tying unless there has been an effective limitation of the consumers' choice (or coercion) to purchase the products separately. The main function of the coercion test is to distinguish between the different forms of bundling (by contract, by technological integration, or by financial incentives) and their effects on consumers.[187] It is however contended by the authors that the

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[183] *See* Economides, *supra* note 94, at 276–77.

[184] *Microsoft D.C. Circuit 2001*, 253 F.3d at 97.

[185] *Id.*

[186] For an analysis of Microsoft's procompetitive justifications in employing a zero-price bundling of Internet Explorer with Windows, see Benjamin Klein, *Microsoft's Use of Zero Price Bundling to Fight the "Browser Wars," in* COMPETITION, INNOVATION AND THE MICROSOFT MONOPOLY: ANTITRUST IN THE DIGITAL MARKETPLACE 217 (Jeffrey A. Eisenach & Thomas M. Lenard eds., 1999).

[187] The terms "technological" and "technical" tying and bundling are used interchangeably. The European Commission refers to "technical tying" (*see Guidance*, *supra* note 70,

test is redundant if the standard for all forms of bundling is similar and should form part of the assessment of the anticompetitive foreclosure element of the tying/bundling abuse under Article 82.

#### a. The Coercion Test in EC Competition Law

In EC competition law, there is a tying violation if the undertaking concerned does not give customers a choice to obtain the tying product without the tied product. Coercion may arise from the refusal of the dominant firm to sell the tying product without the tied one (either as a contractual clause or de facto), from the unavailability of the products separately, from pressure exerted on the customer through the promise of favorable treatment to customers who take both products or threats to those who do not, or from pricing incentives that may be so powerful that no rational customer would choose to buy the products separately.[188] In *Microsoft* the CFI took the view that the analysis of whether the dominant undertaking does not give customers a choice to obtain the tying product without the tied product is "merely expressing in different words the concept that bundling assumes that consumers are compelled, directly or indirectly, to accept 'supplementary obligations,' such as those referred to in Article 82(d) EC."[189] It also held that the test in Article 82 is not exhaustive and that the Commission was therefore right to rely in its decision on Article 82 in its entirety and not exclusively on Article 82(d).[190]

For the CFI, Microsoft had contractually and technically coerced the OEMs. First, it was not possible for the OEMs to obtain a license on the Windows operating system without WMP. Second, it was not technically possible for the OEMs to uninstall WMP. The CFI also noted that coercion of OEMs indirectly restricted the choice of the end consumers.[191] Although Microsoft alleged that customers were not required to pay anything extra for WMP, the court rejected this argument noting that the price of WMP was included in this case in the total price of the Windows client PC operating system. This argument seems paradoxical because the court had already accepted that the two products were distinct, and it should have therefore examined Microsoft's arguments from that perspective. That also would have been consistent with the position of the

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¶ 48), while the U.S. courts most frequently use the term "technological bundling" (*see Microsoft D.C. Circuit 2001*, 253 F.3d at 84).

[188] *See* HOVENKAMP, *supra* note 149, at 410–15.

[189] *Microsoft CFI Decision*, *supra* note 5, ¶ 864.

[190] *Id.* ¶ 861.

[191] *Id.* ¶ 965.

CFI with regard to bundled discounts (in this case a discount of 100 percent on media players).

The CFI adopted a broad definition of coercion, stating that "neither Article 82(d) EC nor the case law on bundling requires that consumers must be forced to use the tied product or prevented from using the same product supplied by a competitor of the dominant undertaking."[192] The theoretical possibility that consumers were not prevented from installing and using other media players instead of WMP was not sufficient to conclude that there was no coercion as the end consumers had a strong incentive to use WMP.[193] The court seems to consider that the alternative offered to consumers to install media players other than WMP should be equivalent with regard to its effectiveness to the pre-installation of media players by the OEMs, which implies a rather strict standard for dominant firms.

It is noteworthy that the requirement of coercion was not mentioned in the *Discussion Paper* for bundling/tying practices.[194] One reason for omitting the coercion test is that the Commission examined together mixed bundling and tying practices and considered mixed bundling as a form of "commercial" tying. The main difference between tying and mixed bundling was therefore the form of restricting the choice for consumers to obtain the tying product without the tied product. In contractual and technical tying, coercion takes a direct form, while for mixed bundling, coercion is indirect and often takes the form of an inducement of the customers to purchase the tied product through granting bonuses, rebates, discounts or any other commercial advantage. (However, the Commission distinguished the two forms of bundling when it examined the foreclosure effect of these practices, as it advocated, wrongly in our view, a cost/price measure for mixed bundling practices.)

The recent Commission *Guidance* also does not mention the element of coercion,[195] although it implicitly internalizes this condition when it treats technical tying more restrictively than contractual tying, by considering that the risk of anticompetitive foreclosure is expected to be

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[192] *Id.* ¶ 970.

[193] *Id.* ¶ 1042 (referring to the Commission's analysis).

[194] *Discussion Paper*, *supra* note 70, ¶ 183 (footnote omitted): The Commission's staff retained instead the following four criteria for the application of the bundling test: "(i) the company concerned is dominant in the tying market; (ii) the tying and tied goods are two distinct products; (iii) the tying practice is likely to have a market distorting foreclosure effect; (iv) the tying practice is not justified objectively or by efficiencies."

[195] *See Guidance*, *supra* note 70, ¶ 50.

greater in this case.[196] In contrast, "technological" tying is subject to the rule of reason in U.S. law, whereas contractual tying falls under the quasi-per se rule of *Jefferson Parish*.[197] The position of the European Commission cannot be explained by the case law of the CFI, which does not establish such a distinction between contractual and technical tying. It is not also compatible with consumer welfare, as in most cases technical tying bundles products in fixed proportions and is thus more likely to be motivated by efficiency gains rather than by an anticompetitive aim. Overall, the European approach for bundling/tying seems inconsistent. The Commission adopts different standards for the various forms of bundling (contractual, technological, and commercial (bundled rebates), strict standards for contractual tying, stricter standards for technological tying, and lenient standards for bundled rebates (by introducing a price/cost test), all without clearly explaining how these fit with the overall objectives and aims of Article 82.

b. A Comparison with the Coercion Test in U.S. Antitrust Law

The requirement of coercion also is present in U.S. antitrust law on tying. The buyer must somehow be forced to accept the tied product. According to Herbert Hovenkamp,

> This coercion should result from (1) an absolute refusal to sell the tying product without the tied product; (2) a discount, rebate or other financial incentive given to buyers who also take the tied product; (3) technological design that makes it impossible to sell the tying product without the tied product.[198]

It follows that coercion does not cover only contractual or technological tying, but also situations of commercial tying.

This does not fit well with the recent Ninth Circuit's decision in *Cascade Health Solutions v. PeaceHealth*, where the court distinguished bundled discounts from tying practices by requiring evidence of coercion for tying but *not* for bundled discounts:

> "One difference between traditional tying by contract and tying via package discounts is that the traditional tying contract typically forces the buyer to accept both products, as well as the cost savings." Conversely, "the package discount gives the buyer the choice of accepting

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[196] *Id.* ¶ 53. The recent challenge by the European Commission of the bundling of Microsoft's Internet Explorer with Windows seems to have been inspired by this principle. *See* Press Release, European Comm'n, Antitrust: Commission Confirms Sending a Statement of Objections to Microsoft on the Tying of Internet Explorer to Windows (Jan. 17, 2009) (Memo/09/15).

[197] Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2 (1984).

[198] HOVENKAMP, *supra* note 149, at 410.

> the cost savings by purchasing the package, or foregoing the savings by purchasing the products separately." The package discount thus does not constrain the buyer's choice as much as the traditional tie. For that reason . . . "[a] variation of the requirement that prices be 'below cost' is essential for the plaintiff to establish one particular element of unlawful bundled discounting—namely, that *there was actually 'tying'*—that is, that the purchaser was actually *'coerced' (in this case by lower prices)* into taking the tied-up package."[199]

When the Ninth Circuit examined the same facts under the tying claim, the court included financial incentives as a form of coercion that could be qualified as unlawful tying, if their effect was to coerce the customers to buy the tying and the tied product.

Persuasion by financial incentives and coercion have similar effects and the Ninth Circuit was quick to find that PeaceHealth's practice of giving a larger discount to insurers who dealt with it as an exclusive preferred provider "may have *coerced* some insurers to purchase primary and secondary services from PeaceHealth rather than from [its rival,] McKenzie."[200] Indeed, "the fact that a customer would end up paying higher prices to purchase the tied products separately does not necessarily create a fact issue on coercion" and "additional evidence of economic coercion" is required.[201] Although "not dispositive evidence of an illegal tie," the fact that McKenzie's prices for primary and secondary services were lower than PeaceHealth's prices on those services was considered by the court as constituting a "permissible inference that a rational customer would not purchase PeaceHealth's allegedly overpriced product in the absence of a tie" and therefore that if customers agreed on an exclusive relationship with PeaceHealth, it is because they were coerced by the latter.[202]

If coercion can also be established by evidence of economic incentives, which have the potential to induce a rational consumer to buy the tying and the tied product together, there is little difference between a tying and a bundled discount claim. The Ninth Circuit recognized the problem when it accepted that economic coercion through inducement could be an alternative theory for McKenzie to present its tying claim:

> [S]uch a claim might raise the question of whether, to establish the coercion element of a tying claim through a bundled discount, McKen-

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[199] Cascade Health Solutions v. PeaceHealth, 515 F.3d 883, 900–01 (9th Cir. 2008) (emphasis added) (quoting AREEDA & HOVENKAMP, *supra* note 25, ¶ 749b2, at 331–32). *See* Virgin Atl. Airways Ltd. v. British Airways plc, 257 F.3d 256, 270 (2d Cir. 2001).

[200] *Cascade Health Solutions*, 515 F.3d at 914 (emphasis added).

[201] *Id.* at 915.

[202] *Id.*

> zie must prove that PeaceHealth priced below a relevant measure of its costs. Some commentators would require a plaintiff alleging that a bundled discount amounts to an illegal tie to prove below-cost prices. . . . It is unclear whether the AMC intended its three-part test to apply when a plaintiff alleging an illegal tying arrangement asserts that the defendant's pricing practices coerced unwanted purchases of the tied product. . . . The parties have not briefed this issue to us, and the parties did not raise the issue before the district court. We therefore leave it to the district court, if necessary, to decide the issue in the first instance on remand.[203]

This demonstrates the internal contradiction of the court's decision: how is it possible to think that coercion distinguishes tying from bundled discounts while considering, at the same time, that bundled discounts may constitute a form of coercion? Furthermore, should financial coercion be interpreted as covering only situations where the "pricing structure makes purchase of the tying and tied products together the only viable economic option" or is this standard "too extreme"?[204]

The Ninth Circuit's espousal of a different antitrust standard for bundled discounts than for tying practices is thus based on shaky grounds, both in terms of law and policy. Adopting the modified predatory cost/price standard for bundled discounts would imply the abandonment of the anticompetitive foreclosure test for all exclusionary practices—tying, exclusive dealing, etc.—in favor of a cost/price predation test or, in other words, of an "as efficient as competitor" test. Legal precedent, economic analysis, and policy choices, however, are all obstacles to this prospect.[205]

The generalization of the approach followed by the Ninth Circuit in *Cascade Health Solutions* for non-price restraints also could lead to an important divergence with EC competition law. The choice between the two analogies—price predation versus anticompetitive foreclosure—is an issue that is not only linked to the apparent need, or not, to build safe harbors for "efficient" pricing practices of dominant firms and also

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[203] *Id.* at 916 n.27.

[204] Ortho Diagnostic Sys., Inc. v. Abbott Labs., Inc., 920 F. Supp. 455, 471 & n.23 (S.D.N.Y. 1996) (citing 10 PHILLIP AREEDA & DONALD F. TURNER, ANTITRUST LAW ¶ 1758b, at 345–46 (1978)).

[205] Although the D.C. Circuit acknowledged in *United States v. Microsoft Corp.*, 253 F.3d 34 (D.C. Cir. 2001), that, except for situations of predatory pricing, "antitrust laws do not condemn even a monopolist for offering its product at an attractive price," *id.* at 68, it did not apply the predatory pricing test or a modified version of it for the nonprice exclusionary practices and bundling, in general, *id.* at 96–97. *See* PAGE & LOPATKA, *supra* note 2, at 66.

is related to the theory of competition that underscores the enforcement of Section 2 of the Sherman Act and Article 82. The interpretation of the concept of anticompetitive foreclosure in both jurisdictions illustrates the different theoretical foundations of U.S. antitrust law and EC competition law.

## II. THE DIFFERENT MEANING OF ANTICOMPETITIVE FORECLOSURE IN U.S. ANTITRUST AND EC COMPETITION LAW

The competitive assessment of bundling practices requires analysis of the foreclosure of competition in the tying or tied market (depending on the theory of anticompetitive harm) in both EC and U.S. antitrust law. The meaning of the concept of anticompetitive foreclosure has been, and still is, one of the most controversial issues in antitrust law enforcement, not only for bundling but also for all types of exclusionary practices. An important aspect of this debate has been the definition of a limiting principle for antitrust law enforcement: whether anticompetitive foreclosure should be perceived as requiring something more than foreclosure or the exclusion of a rival. For bundling practices, the debate over the adequate standard of foreclosure has focused on the following two questions: (i) should the foreclosure effect be presumed from the nature of the bundling practice and/or the existence of tying market power (dominant position); and (ii) in which circumstances does the foreclosure of a competitor from the tied product market harm consumers?

### A. Foreclosure and the Nature of Bundling: A Quasi-Per Se Rule or a More Flexible Standard?

Framing effective (neither overinclusive, nor underinclusive) and workable (easily administrable) competition law standards for bundling practices is not an easy exercise. It is more usual to contrast *effects*-based approaches to *form*-based approaches: the former require the examination of the effects of a practice before concluding that it is anticompetitive, while the latter focus on the nature of the practice before arriving at any conclusion with regard to its anticompetitive effects. A form-based approach is not necessarily incompatible with the analysis of the anticompetitive effects of a practice. Nevertheless, instead of analyzing the effects of the specific practice within the specific market context (an ex post and concrete analysis[206]), the competition authority or the judge

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[206] Such an analysis does not necessarily require evidence of actual effects of anticompetitive foreclosure. See discussion *infra* Part II.B.

characterizes the practice as falling within an ex ante pre-defined category of practices that are generally deemed—from previous practical experience or because of their opposition to a fundamental aim of competition law— to produce anticompetitive effects (abstract/categorical analysis).

The U.S. and EC competition law on tying and bundling practices illustrate the evolution of antitrust standards towards a more effects-based approach. Although judicial decisions were often developed without much concern for analyzing anticompetitive effects, the more recent case law in the United States requires the examination of the anticompetitive effects of the practice before concluding whether there is illegal tying. In *Jefferson Parish,* the Supreme Court adopted a modified per se test for contractual tying.[207] There was a presumption of anticompetitive effects whenever a firm with market power employed bundling practices that had the effect of foreclosing rivals from significant market shares in the tied product market,[208] of extracting consumer surplus,[209] or of raising barriers to entry in both the tying and the tied markets.[210] In *United States v. Microsoft*, the D.C. Circuit moved to a rule of reason test for software bundles that requires plaintiffs to demonstrate that the benefits of the tying practice are outweighed by the harms in the tied product market.[211] This essentially is a cost/benefit analysis test that takes fully into account the efficiency gains to the benefit of consumers and allocates the legal burden of proof to the plaintiff: the plaintiff "must demonstrate that the anticompetitive harm of the conduct outweighs the procompetitive benefit."[212] If the plaintiff successfully establishes a prima facie case by demonstrating anticompetitive effects, it is on the defendant monopolist to "proffer a 'procompetitive justification' for its conduct" (evidentiary burden of proof for efficiency justifications).[213] The burden then shifts back to the plaintiff to rebut that claim and to prove that "the anticompetitive harm of the conduct outweighs the procompetitive benefit."[214] This cost/benefit analysis test, and at-

[207] Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 12–18 (1984).

[208] Fortner Enters. v. U.S. Steel Corp., 394 U.S. 495 (1969).

[209] *Jefferson Parish*, 466 U.S. at 14–15 (market power in the tying market is employed to "impair competition on the merits in another market," thus "increasing monopoly profits over what they would be absent the tie").

[210] Eastman Kodak Co. v. Image Technical Servs., Inc., 504 U.S. 451 (1992).

[211] United States v. Microsoft Corp., 253 F.3d 34, 95–97 (D.C. Cir. 2001). Procompetitive justifications for tying were also considered in *Illinois Tool Works v. Independent Ink*, 547 U.S. 28, 36 (2006).

[212] *Microsoft D.C. Circuit 2001*, 253 F.3d at 59.

[213] *Id.*

[214] *Id.*

tendant burden shifting, also applies to bundled discounts.[215] In essence, the anticompetitive foreclosure test in the United States looks to the anticompetitive effects of the practice and concludes that there is anticompetitive foreclosure only when the benefits of a practice do not outweigh its costs, from the point of view of the consumers.

The position of EC competition law was initially quite hostile to any form of tying.[216] In *Hilti* and *Tetra Pak II* the ECJ applied a quasi-per se test and found that by imposing on their customers numerous obligations that had no link with the purpose of the contracts, the dominant firms in question had restricted the market access of their competitors and had deprived consumers of any freedom to make their own choices.[217] Consequently, if there are independent producers in the tied product market, it is required that dominant undertakings abstain from any conduct, such as contractual tying, that would have the effect of restricting the freedom of these independent producers to compete in the tied market.

Dominant undertakings may argue the existence of an objective justification for their conduct. Early case law has, however, restrictively interpreted this concept as not including any efficiency defense, but only broad non-economic public policy concerns, such as safety or health factors related to the dangerous nature of the product in question.[218] The CFI's 2007 *Microsoft* decision and the Commission's *Guidance* constitute, in this respect, an interesting evolution.

The two steps in the abuse control test of Article 82 are as follows:

> Article [82] covers practices which are *likely* to affect the structure of a market where, as a direct result of the presence of the undertaking in question, competition has already been weakened and which, through recourse to methods different from those governing normal competition in products or services based on traders' performance, have the

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[215] LePage's Inc. v. 3M, 324 F.3d 141, 163–64 (3d Cir. 2003).

[216] VALENTINE KORAH, AN INTRODUCTORY GUIDE TO EC COMPETITION LAW AND PRACTICE 142 (8th ed. 2004).

[217] *See* Case IV/30.787 and 31.488—Eurofix-Bauco v. Hilti, Comm'n Decision, 1988 O.J. (L 65) 19, ¶ 75; Case T-83/91, Tetra Pak Int'l SA v. Comm'n, 1994 E.C.R. II-755, ¶ 140 (Ct. First Instance); Case C-333/94, Tetra Pak Int'l SA v. Comm'n, 1996 E.C.R. I-5951, ¶ 36 (Eur. Ct. Justice).

[218] For an analysis, see Ekaterina Rousseva, *Abuse of Dominant Position Defenses—Objective Justification and Article 82 EC in the Era of Modernization*, *in* EC COMPETITION LAW—A CRITICAL ASSESSMENT 377–431 (Giuliano Amato & Claus-Dieter Ehlermann eds., 2007); Albertina Albors-Llorens, *The Role of Objective Justifications and Efficiencies in the Application of Article 82 EC*, 44 COMMON MKT. L. REV. 1727 (2007).

> effect of hindering the maintenance or development of the level of competition still existing on the market.[219]

As a first step, the abuse test involves assessing whether the conduct is of a type "likely" or "such as" to affect the structure of an otherwise concentrated market and which constitutes a (business) method "different from those governing normal competition in products or services based on traders' performance" (abstract/categorical analysis) that would initially require the classification of the practice into a specific antitrust category. In the second step, the competition authority or judge will examine the anticompetitive effects of the specific practice (fact-based analysis).[220] The first prong of this abuse test, abstract/categorical analysis, implies that for certain practices there is a prima facie presumption of anticompetitive or procompetitive effect when the firm has a dominant position.

The case law of the European Courts is ambiguous as to which practices are presumptively anticompetitive in the abstract/categorical analysis part of the abuse test. Certain forms of practices, such as tying, loyalty rebates, predatory prices, and exclusive dealing obligations imposed by dominant firms, were often analyzed as being anticompetitive and therefore infringing Article 82 by their nature and effect.[221] It is true that the case law does not always require the examination of the existence of actual anticompetitive effects, as these follow from the qualification of the conduct as being tying, a loyalty rebate, or predatory pricing.[222] This

[219] Case 322/81, NV Nederlandsche Banden Industrie Michelin v. Comm'n (*Michelin I*), 1983 E.C.R. 3461, ¶ 70 (Eur. Ct. Justice) (emphasis added). Compare with the terminology used by the ECJ in Case 85/76, *Hoffman-LaRoche & Co. v. Commission*, 1979 E.C.R. 461, ¶ 91 (Eur. Ct. Justice), and Case C-95/04, *British Airways plc v. Commission*, 2007 E.C.R. I-2331, ¶ 66 (Eur. Ct. Justice): Article 82 "refers to conduct *which is such as to influence the structure of a market* where, as a result of the very presence of the undertaking in question, the degree of competition is already weakened." *British Airways*, 2007 E.C.R. I-2331, ¶ 66 (emphasis added). The difference between "likely to affect" and "conduct which is such as to influence" may indicate a difference in the degree of probability of the occurrence of the outcome ("affect" or "influence" the structure of the market) as a result of the specific conduct.

[220] *See* MONTI, *supra* note 56, at 171.

[221] *Sot. Lélos kai Sia*, *supra* note 117, ¶ 50; Case T-203/01, Manufacture Française des Pneumatiques Michelin v. Comm'n (*Michelin II*), 2003 E.C.R. II-4071, ¶ 241 (Ct. First Instance) ("[F]or the purposes of applying Article 82 EC, establishing the anti-competitive object and the anti-competitive effect are one and the same thing. If it is shown that the object pursued by the conduct of an undertaking in a dominant position is to limit competition, that conduct will also be liable to have such an effect." (citation omitted)); *Intel Comm'n Decision*, *supra* note 97, ¶ 923 ("a violation of Article 82 may also result from the anticompetitive object of the practices pursued by a dominant undertaking").

[222] *Michelin II*, *supra* note 21, ¶ 239 (loyalty rebates); Case T-340/03, France Télécom SA v. Comm'n, 2007 E.C.R. II-107, ¶¶ 195, 197 (Ct. First Instance) (predatory pricing); *Microsoft CFI Decision*, *supra* note 5, ¶ 1035 (tying).

classification or characterization process that precedes the assessment of the anticompetitive effects of the conduct plays an important role.

It is not clear, however, what the European Court of Justice meant by "methods different from those governing normal competition in products or services based on traders' performance" ("abnormal" practices). Would that mean that EC competition law prohibits certain commercial practices, such as tying and loyalty discounts, per se? The Commission's *Guidance* refers to certain circumstances where it would not be necessary to carry out a detailed assessment before concluding that the conduct in question is likely to result in consumer harm.[223] It is true that the Commission considers that the anticompetitive effect will be inferred in this case, as that type of conduct can only raise obstacles to competition without adding any efficiency gain. One could argue, however, that this paragraph of the *Guidance* does not affect the theoretical possibility for dominant undertakings to invoke efficiencies, in particular as it remains possible for conduct leading to anticompetitive foreclosure to be justified by the objective necessity defense and efficiencies, before finding the existence of an abuse of a dominant position. The Commission does not explicitly exclude these practices from Section D of the *Guidance* on objective necessity and efficiencies, although, in practice, it seems unlikely that the alleged efficiencies will be accepted for failure to comply at least with the first two cumulative conditions of the efficiency defense under EC competition law.

In *Sot. Lélos kai Sia*, a case involving the refusal to supply by a dominant undertaking with the aim of avoiding all parallel exports from a Member State to other Members States, the ECJ implicitly recognized that certain types of conduct, such as a restriction of parallel trade, may create a presumption of negative effects on consumers and therefore shift the burden of proof to the defendant, without it being necessary for the claimant to bring additional evidence on the causal link between the specific conduct and consumer harm.[224] Despite, however, the language employed, the Court immediately recognized that this does not amount to an absolute presumption of consumer harm or a per se prohibition. The presumption of anticompetitive effects may still be rebutted by the defendant in limited circumstances: a company must be "in a position to take steps that are reasonable and in proportion to the need

[223] *Guidance*, *supra* note 70, ¶ 22. The Commission provides some non-exhaustive examples, such as conduct through which the dominant undertaking prevents its customers from testing the products of competitors or pays a distributor or a customer to delay the introduction of a competitor's product.

[224] *Sot. Lélos kai Sia*, *supra* note 117, ¶¶ 56–57.

to protect its own commercial interests."[225] The first prong of the abuse test, abstract/categorical analysis, does not therefore establish a per se prohibition of certain commercial practices, including tying or bundling.

One also could interpret the first prong of the test as covering all practices that are likely to (not just may potentially) exclude rivals from the market, a test that would require more than just establishing the mere probability of exclusion and would resemble a balance of probabilities test.[226] Nevertheless, distinguishing the practices that, on a balance of probabilities following an abstract/categorical analysis, are likely to produce such an effect from those that are not likely to achieve exclusion is still an unclear test.

Furthermore, the case law on tying and loyalty rebates might seem to be in conflict with the more flexible position on refusals to deal adopted by the ECJ in *Bronner*. The court took a restrictive view in this case of the obligation of a dominant undertaking to grant competitors access to its facilities.[227] Bronner, a publisher of a newspaper in Austria, had refused access to a competing newspaper to the nationwide home-delivery scheme it had established. The court stressed that the refusal must "be likely to eliminate all competition" on the part of the competitor requesting access, that access should be indispensable and not only make it harder for the requesting undertaking to compete, and that it should not be capable of being objectively justified.[228] With regard to the indispensability condition, the court held that access would have been indispensable only if it was not economically viable to create a home-delivery system for a newspaper with a comparable circulation to the dominant firm's.[229]

One could argue that the conditions in *Bronner* set the outer boundaries of the special responsibility of a dominant firm and consequently of the corresponding duty, under Article 82, to abstain from any action that would be likely to exclude rivals from the market. The excluded rival would be granted access only if it would be impossible for an undertaking with a comparable output to the dominant firm to develop

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[225] *Id.* ¶ 69.

[226] On the terminology (e.g., likely, capable or tend to restrict competition) used by the different cases of the CFI and the ECJ in the context of a multilingual legal system, see Klaus Pfeiffer, *Reflections on* British Airways v. Comm'n, 28 EUR. COMPETITION L. REV. 597, 599 (2007).

[227] Case C-7/97, Oscar Bronner GmbH & Co. KG v. Mediaprint Zeiturgs-und Zeitschriftenverlag GmbH & Co., KG, 1998 E.C.R. I-7791 (Eur. Ct. Justice).

[228] *Id.* ¶ 41.

[229] *Id.* ¶¶ 45–46.

such facility—that is, the facility should be indispensable. The indispensability test laid down by the ECJ and Advocate General Jacobs in *Bronner* requires the plaintiff to prove that it would not be economically viable for a competitor with a comparable turnover to create the facilities/input to which his rivals are requesting access. The test integrates a (not yet) equally efficient competitor test, as it is only if the input or facility would not be economically viable,[230] "in the sense that it would not generate enough revenue to cover its costs"[231] that a duty to deal may be imposed under Article 82. The test involves comparing relevant costs and revenues. The dominant firm's costs in running the upstream facility are employed as the basis for comparison for the evaluation of the costs; hence the implicit introduction of an equally efficient competitor test.

Drawing on this case law, Jean-Yves Art and Gregory McCurdy argue that the *Microsoft* bundling case could fit in the refusal to supply category and that it should be examined under the limiting principles of *Bronner*.[232] They assert that the main issue involved in the bundling part of the case was that by offering to OEMs only a bundled version of Windows and WMP, Microsoft had effectively denied its rivals in the media player market access to the appropriate "distribution services" of the OEMs. The OEMs would operate in this case as intermediaries between the market players in the tied product market and the final consumers. Art and McCurdy's argument is that the application of the *Bronner* principles in the factual situation of Microsoft would not have led to an infringement of Article 82 because distribution of the player in Windows was not indispensable and that Internet downloading was a feasible and only "less advantageous" distribution channel.

There are at least two problems with this conclusion. First, even if the *Bronner* conditions applied in this case, it is not clear that they would not have led to the finding of an infringement. Indispensability of access is measured with reference to the possibility of creating an economically viable distribution channel. It remains to be seen if Internet downloading is an economically viable alternative to access to the OEMs to bring the product to the attention of the final consumers. Second, in *Bronner*, the dominant firm was refusing access to a facility it owned, which was

[230] *Id.* ¶¶ 43–46; *id.* ¶ 68 (opinion of Advocate General Jacobs).

[231] *Discussion Paper*, *supra* note 70, ¶ 229.

[232] Jean-Yves Art & Gregory V.S. McCurdy, *The European Commission's Media Player Remedy in Its* Microsoft *Decision: Compulsory Code Removal Despite the Absence of Tying or Foreclosure*, 25 EUR. COMPETITION L. REV. 694, 703–07 (2004).

the product of its own investment and efforts.[233] The refusal of access was therefore a legitimate exercise of the undertaking's property rights. Thus, if we follow Art and McCurdy's arguments, Microsoft's refusal to supply to its rivals access to the distribution services of the OEMs could not be considered as the legitimate exercise of a property right for the simple reason that the OEMs were not owned by Microsoft and there was no exclusive contract that linked the OEMs to Microsoft.[234] But how is it possible to explain the fact that for refusals to deal there is no presumption of anticompetitive effects, under the first prong of the abuse of dominance test, while there is one for bundling or loyalty rebates?

It is possible to understand the EC abuse test by referring to two important factors: first, the idea that dominant firms have a special responsibility in preserving competition;[235] and second, but closely linked to the first factor, the importance of the objective of consumer sovereignty in EC competition law.

The concept of special responsibility means that dominant firms' commercial freedom is restricted in comparison to non-dominant undertakings. The latter remain free to use commercial practices that are different from those governing normal competition. The focus of the test seems to be the protection of "free competition" or "complete competition" and "open markets."[236] The underlying theoretical assumption is that rivalry brings variety in the marketplace, in the sense that entre-

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[233] *See also* Case C-552/03, Unilever Bestfoods (Ireland) Ltd. v. Comm'n, 2006 E.C.R. I-9091, ¶ 137 (Eur. Ct. Justice) (favoring this interpretation of *Bronner*, 1998 E.C.R. I-7791).

[234] The result would not have been different in EC competition law if Microsoft decided to integrate vertically (and to own OEMs). This situation could have been analyzed as a case of refusal to supply to existing customers (in the sense that competing media players would not have access to OEMs that would have been open to them otherwise) and judged under the strict standards of *Commercial Solvents*. *See* Joined Cases 6 & 7/73, Instituto Chemioterapico Italiano Spa & Commercial Solvents Corp. v. Comm'n, 1974 E.C.R. 223 (Eur. Ct. Justice).

[235] Or this may be seen as the "system of variable thresholds" *("System beweglicher Schranken,"* i.e., the concept that behavior which may be unproblematic for competition law purposes in the hands of a firm in a competitive market need not be harmless in the hands of a dominant firm). *See* Wernhard Möschel, *Art. 82 EGV*, *in* WETTBEWERBSRECHT EG TEIL I 534, ¶ 120 (Ulrich Immenga & Ernst-Joachim Mestmäcker eds., 4th ed. 2007); Wernhard Möschel, *GWB § 19*, *in* WETTBEWERBSRECHT EG TEIL I, *supra. But see* VOLKER EMMERICH, KARTELLRECHT § 27, ¶ 63 (10th ed. 2006).

[236] Walter Eucken, *Die Wettbewerbsordnung und ihre Verwirklichung [The Competitive Order and Its Implementation]*, 2 ORDO, JAHRBUCH FÜR DIE ORDNUNG VON WIRTSCHAFT UND GESELLSHEFT 1–99 (1949), *translated in* Walter Eucken, *The Competitive Order and Its Implementation*, COMPETITION POL'Y INT'L, Autumn 2006, at 219. More recently, see Jürgen Basedow, *Konsumentenwohlfahrt und Effizienz—Neue Leitbilder der Wettbewerbspolitik?*, 57 WIRTSCHAFT UND WETTBEWERB 712 (2007); C. Christian von Weizsäcker, *Konsumentenwohlfahrt und Wettbewerbsfreiheit: Über den tieferen Sinn des "Economic Approach,"* 57 WIRTSCHAFT UND WETTBEWERB 1078 (2007).

preneurs test a certain number of hypotheses on the parameters of the "product" (price, quality, service, and so on) that they think will satisfy consumers' demands; variety ultimately preserves the choice of the consumers and their ability to test the solutions adopted by the entrepreneurs.[237] The variety of "products" (or solutions suggested by the entrepreneurs) therefore are not the outcome of the "natural" selection process of the marketplace but result from a process of "artificial selection" by formal and informal institutions that "channel the competitive process and give it a certain direction" and select "at the same time, artificially, which entrepreneurial hypotheses will survive."[238] Dominant firms are in a position to influence directly the market activities of other economic agents and therefore may constitute an informal institution that can indirectly affect the ultimate choice of the consumers.[239] Their freedom of action is restricted to "performance competition," offering better terms to consumers, and does not extend to "impediment competition," where commercial practices, such as loyalty rebates or predatory pricing, hinder the ability of rivals to compete; in other words, to offer their own set of solutions to the essential problem of productive activity: what "products" do the consumers prefer?[240]

The concept of special responsibility of dominant firms may be explained by the emphasis of EC competition law on consumer sovereignty, rather than on the concept of consumer welfare as such.

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[237] CHRIS MANTZAVINOS, INDIVIDUALS, INSTITUTIONS, AND MARKETS 193–203 (2001). This conception of competition as a process of rivalry rather than as a market equilibrium (neoclassical theory) is not very different from that developed by the Old-Institutionalist School in the United States and that of John M. Clark. *See* J.M. Clark, *Competition and the Objectives of Government Policy*, *in* MONOPOLY AND COMPETITION AND THEIR REGULATION 317, 326 (Edward H. Chamberlin ed., 1954). However, although these concepts of competition are different from "perfect competition," they are not unrelated. *See* John Vickers, *Concepts of Competition*, 47 OXFORD ECON. PAPERS 1, 5, 6–7 (1995).

[238] MANTZAVINOS, *supra* note 237, at 174.

[239] See recent literature on market manipulation, providing evidence that firms take advantage of the specific characteristics of consumers and manipulate their cognitive biases. *See, e.g.*, Jon D. Hanson & Douglas A. Kysar, *Taking Behavioralism Seriously: Some Evidence of Market Manipulation*, 112 HARV. L. REV. 1420 (1999).

[240] The distinction between "performance competition" and "impediment competition" was suggested as an element distinguishing abusive from non-abusive practices by professor Peter Ulmer of the University of Heidelberg and was influential in the enforcement of the German Act Against Restraints of Competition (GWB). DAVID J. GERBER, LAW AND COMPETITION IN TWENTIETH CENTURY EUROPE: PROTECTING PROMETHEUS 313 (1998) (citing PETER ULMER, SCHRANKEN ZULÄSSIGEN WETTTBEWERBS MARKTBEHERRSCHENDER UNTERNEHMEN (1977)); *see also* Kallaugher & Sher, *supra* note 59, at 269; Liza Lovdahl Gormsen, *Article 82 EC: Where Are We Coming from and Where Are We Going to?*, 2 COMPETITION L. REV., Mar. 2006, at 5, 25 For a criticism from other ordo-liberals of the "impediment competition" concept, see Erich Hoppmann, *Behinderungsmissbrauch und Nichtleistungswettbewerb*, 30 WIRTSCHAFT UND WETTBEWERB 811 (1980); Möschel, GWB § 19, *supra* note 235, ¶¶ 102–105; EMMERICH, *supra* note 235, § 27, ¶ 68.

Consumer sovereignty can be preserved by the ability of consumers to influence price, quality, variety, and subsequently the competitive (or innovation) process according to their own preferences.[241] The emphasis on the special responsibility of dominant firms to protect the competitive process should therefore be understood as a proxy for consumer sovereignty: open and contestable markets are a prerequisite for the empowerment of consumers.

This doctrine is not antithetical to modern economic thinking. It may not always be compatible with mainstream neoclassical economic theory, but one should not forget that economic theory is in constant evolution. What was considered as mainstream in the past may well be marginalized in the future, especially in light of recent economic turmoil and the causes attributed to it. Recent economic thinking has cast doubt on several assumptions and the analytical framework of neoclassical price theory. Behavioral law and economics challenges the premise of perfect rationality that permeates much of neoclassical economic analysis. This has profound implications for antitrust policy and doctrine.[242] Behavioral economists' emphasis on bounded rationality may explain much of this behavior and could lead to different prescriptions for public policy, even, in some circumstances, to more active antitrust enforcement.

Recent evolutionary thinking on the theory of consumer behavior has also challenged the neoclassical price theory assumption that consumers act upon exogenously given preferences. Consumers are influenced in their decisions by "the context of choice, defined by the set of options under consideration. In particular, the addition and removal of options from the offered set can influence people's preferences among options that were available all along."[243] The firms with their marketing activities may, for example, shape endogenously consumer preferences by establishing an artificial selection process.

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[241] For another formulation of this principle, see Neil W. Averitt & Robert H. Lande, *Consumer Sovereignty: A Unified Theory of Antitrust and Consumer Protection Law*, 65 ANTITRUST L.J. 713, 715 (1997) ("[C]onsumer sovereignty is . . . the set of societal arrangements that causes that economy to act primarily in response to the aggregate signals of consumer demand, rather than in response to government directives or the preferences of individual businesses.").

[242] *See* Maurice E. Stucke, *Behavioral Economists at the Gate: Antitrust in the Twenty-First Century*, 38 LOY. U. CHI. L.J. 513 (2007); Avishalom Tor, *Illuminating a Behaviorally Informed Approach to Antitrust Law: The Case of Predatory Pricing*, ANTITRUST, Fall 2003, at 52.

[243] Eldar Shafir, Itamar Simonson & Amos Tversky, *Reason-based Choice*, 49 COGNITION 11, 21 (1993).

Neoclassical economic theory operates on the assumption that preferences are revealed by market behavior[244] and ignores the psychological aspect of the formation of these preferences. Recent studies have challenged this assumption: "preferences are actually constructed—not merely revealed."[245] A greater focus on consumer sovereignty may, in some cases, lead to more intensive competition law intervention to establish the parameters of independent consumer choice[246] and specific presumptions against commercial practices that deny the sovereignty of consumer choice.

It follows that certain commercial practices (that we will call "coercive abuses") are more likely than others to affect the competitive process by interfering with the sovereign decision of the consumer in the choice of the bundle of the parameters of a product. This category regroups practices, such as bundling (tying, multi-product rebates) and conditional rebates, which interfere with an established consumption trend and tend to influence it to the benefit of the dominant firm. By employing these practices, the dominant firms aim to exclude rivals by increasing their costs or by denying them the necessary economies of scale in the distribution of their products. They do not compete on the merits by offering better quality parameters of the specific product bundle and they attempt to interfere with the consumers' final choice of the entrepreneurial hypothesis that will survive. In other words, the dominant company will not respond to consumer preferences on the parameters of the bundle of a product and/or service but will attempt to reduce consumer sovereignty by coercing or inducing the intermediaries to reject competing bundles of products and/or services, therefore denying the final consumers the opportunity to influence the market selection process according to their own preferences. This implies that the conduct would require at least the passive assistance or participation of intermediaries to achieve its effects.[247] The antitrust standard/test applicable in this case should be consistent with the standard applied in the context of Article 81 for vertical restraints that affect interbrand competition, as it is generally difficult to distinguish between these two

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[244] Paul A. Samuelson, *Consumption Theory in Terms of Revealed Preference*, 15 ECONOMICA 243, 243 (1948).

[245] Shafir et al., *supra* note 243, at 34.

[246] For a recent setting of the theoretical foundation of state intervention to protect consumer choice, see Cass R. Sunstein & Richard H. Thaler, *Libertarian Paternalism Is Not an Oxymoron*, 70 U. CHI. L. REV. 1159 (2003), and Cass R. Sunstein & Richard H. Thaler, *Libertarian Paternalism*, 93 AM. ECON. REV. 175 (2003).

[247] If the assistance is active that will amount to an agreement not a unilateral practice. *See* Ioannis Lianos, *Collusion in Vertical Relations Under Article 81 EC*, 45 COMMON MKT. L. REV. 1027 (2008).

forms of coercive practice in terms of anticompetitive effects. Hence, the courts should not apply in this case a predatory or equally efficient competitor test, since the conduct of the dominant undertaking is of the nature to limit consumer sovereignty. The risk of false negatives is, in this instance, reduced as there is a clear indication that the dominant undertaking's conduct affects the competitive process.

There is, however, an important ambiguity underlying this entire approach: the identification of the practices that are deemed "abnormal" or coercive, if we employ this terminology. In theory, many commercial practices may have the effect of excluding rivals from the market or substantially to hinder their ability to compete.[248] The test is unworkable without a limiting principle that could provide dominant undertakings the ability to identify, ex ante, if their commercial practices would be considered illegal. This is where recourse to an effects-based approach makes a difference.

In an effects-based approach, the identification of a specific practice as coercive or abnormal should not lead to a presumption of anticompetitive effects and consumer harm. It only indicates that the fact finder should examine the existence of consumer harm according to a different decision procedure than non-coercive purely unilateral abuses, such as refusals to deal.[249] The latter are subject to a test of indispensability (as access is provided only if the resource is considered indispensable

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[248] *See* Case C-95/04, British Airways plc v. Comm'n, 2007 E.C.R. I-2331, ¶ 68 (Eur. Ct. Justice) (To determine if there is exclusionary effect one should determine whether the dominant firm's conduct/practices are "capable, first, of making market entry very difficult or impossible for competitors of the undertaking in a dominant position and, secondly, of making it more difficult or impossible for its co-contractors to choose between various sources of supply or commercial partners"). This seems to set the standard of proof too high. Compare, however, the French version of the decision: "*[I]l convient, d'abord, de vérifier si ces rabais ou primes peuvent produire un effet d'éviction, c'est-à-dire s'ils sont à même, d'une part, de rendre plus difficile, voire impossible*, l'accès au marché pour les concurrents de l'entreprise en position dominante et, d'autre part, *de rendre plus difficile, voire impossible*, pour ses cocontractants, le choix entre plusieurs sources d'approvisionnement ou partenaires commerciaux." *Id.* (emphasis added), *available at* http://curia.europa.eu/jurisp/cgi-bin/form.pl?lang=fr (search by case number under "*Numéro d'affaire*") (summary translation: It is sufficient for Article 82 to apply that market access for the competitors became more difficult or [in certain cases] impossible.).

[249] There is no doubt that the risk of false positives is higher if antitrust law intervenes in the unilateral decisions of dominant firms to lower the prices of a product, such as unconditional single product discounts/rebates, or to set other dimensions of a product transaction (quality, quantity of products sold, their commercial partner) or finally to pursue legal proceedings against a competitor. These are practices that are purely unilateral in their form and essence, as they do not require for their success the assistance or contribution of other market players situated in the downstream or upstream market. The assumption is that, absent evidence of the contrary, the dominant undertaking engages in this conduct without having the objective or intent to affect the principle of consumer sovereignty.

for the continuation of the activity of the excluded undertaking)[250] or of a price/cost test measuring the relative efficiency of the excluded or marginalized undertaking as a filter for a more detailed competition law assessment. There is no such filter for coercive abuses, as in this case there is a greater likelihood that consumer sovereignty is affected. However, it is only if there is an identifiable consumer detriment, either direct (empirically verified) or indirect (involving a plausible theory of consumer harm), that the practice will be found contrary to Article 82. Identifiable efficiency gains, such as lower costs or better quality inputs that are likely to be passed on to final consumers, should be able to mitigate the anticompetitive effects. This balancing test (cost/benefit analysis) will ensure that practices that could enhance consumer sovereignty in the long run are not prohibited under Article 82, without a more careful analysis of their effects on final consumers.

The comparative analysis of the *Michelin II* and the *British Airways* rebates cases may provide an example of how a form-based approach could be different from a more effects-based test. In *Michelin II*, the CFI spent a number of paragraphs examining whether the specific target rebate scheme could be characterized as loyalty inducing, which did not require the court to analyze the concrete effects of the specific scheme on consumers. The CFI conducted instead an abstract/categorical analysis of the facts of the case to find out if the quantity rebate system, put in place by Michelin, fit the characterization of "loyalty inducing" rebates.[251] The CFI considered that quantity rebates that are justified by a "countervailing advantage" that is "economically justified" do not constitute in general loyalty inducing rebates and therefore would escape the prohibition of Article 82.[252] The court subjected this economic justification of the rebate to a high standard of proof,[253] and, in the absence of an objective justification, the CFI concluded that the rebate system was loyalty inducing.[254] As a result of its loyalty-inducing character, the quantity rebate scheme "limited the dealers' choice of supplier and made access to the market more difficult for competitors."[255] The anticompetitive effect of this practice was thus presumed from the simple characterization of the rebate scheme as loyalty inducing without any analysis of

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[250] *See supra* text accompanying notes 230–231.

[251] Case T-203/01, Manufacture Française des Pneumatiques Michelin v. Comm'n (*Michelin II*), 2003 E.C.R. II-4071, ¶ 95 (Ct. First Instance). The court concluded that the rebate scheme offered by Michelin "has the characteristics of a loyalty-inducing discount system."

[252] *Id.* ¶ 100.

[253] *Id.* ¶¶ 108–109.

[254] *Id.* ¶ 113.

[255] *Id.* ¶¶ 110, 240.

anticompetitive effects and possible consumer detriment. One could compare this approach to a quasi-per se illegality test for loyalty-inducing rebates.

The position of the CFI, confirmed by the ECJ, seems to have slightly evolved in *British Airways* towards a more flexible approach in the form-based/effects-based continuum. First, the court found that even if the specific schemes had a "fidelity-building" effect, they could escape the application of Article 82 if they were based on an "economically justified consideration."[256] It would be possible for the dominant undertaking to justify these fidelity-inducing rebates by referring to efficiency justifications.[257] The consideration by the CFI of the existence of objective economic justifications did not aim to determine whether the rebate scheme has a loyalty-inducing effect, as was the case in *Michelin II*, but followed the characterization step of the rebate scheme as having a fidelity-building character.[258] Thus, it formed part of the second prong of the abuse test—the assessment of anticompetitive foreclosure under a cost benefit analysis test.[259] Moreover, the second prong of the abuse test may include countervailing efficiency gains that benefit consumers.[260]

In *British Airways,* CFI concluded that the loyalty rebates schemes should not only be examined under the first prong of the abuse test, but instead that the competition assessment should include an analysis of their anticompetitive effects under the second part of the test. This is closer to a structured rule of reason approach than to a quasi-per se illegality rule. The ECJ confirmed the approach of the CFI in *British Airways* and adopted a standard resembling a structured rule of reason approach:

> It has to be determined whether the exclusionary effect arising from such a system, which is disadvantageous for competition, may be counterbalanced, or outweighed, by advantages in terms of efficiency which also benefit the consumer. If the exclusionary effect of that system bears no relation to advantages for the market and consumers, or if it

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[256] Case T-219/99, British Airways plc v. Comm'n, 2003 E.C.R. II-5917, ¶ 271 (Ct. First Instance).

[257] *Id.* ¶ 280. This included efficiency gains.

[258] *See* ALISON JONES & BRENDA SUFRIN, EC COMPETITION LAW 504 (3d ed. 2008).

[259] One could refer to this step as an equivalent to an Article 81(3) defense. Article 81 identifies two analytical steps: the prohibition principle of Article 81(1), which is a quick look establishing the existence of anticompetitive effects, and the exception principle of Article 81(3), which integrates a more detailed assessment of the practice under a cost/benefit to consumers test. No such distinction is however mentioned in the context of Article 82.

[260] *British Airways*, 2003 E.C.R. II-5917, ¶¶ 279–80 (not just public policy type of justifications).

> goes beyond what is necessary in order to attain those advantages, that system must be regarded as an abuse.[261]

Second, in contrast to *Michelin II*, the court emphasized the existence of a consumer prejudice, an indication that it placed its analysis under the second prong of the abuse test under Article 82 EC.[262] The consideration of anticompetitive effects and consumer harm constitutes the main difference between the decision of the CFI in *Michelin II* and that of the ECJ in *British Airways.* Nonetheless, examining the existence of exclusionary effects does not necessarily mean that evidence of anticompetitive effects and consumer detriment is required. In other words, the analysis of possible economic justifications of a discount with a fidelity-building effect does not necessarily amount to the adoption of a full effects-based approach that would require empirical evidence of actual consumer prejudice.

In *Microsoft,* the European Commission was constrained by the previous case law of the Court in *Hilti* and in *Tetra Pak II.* Instead of basing its decision on the traditional theory of tying, which advocates a quasi-per se illegality test if the undertaking employing the tying practice holds a dominant position (thus inferring anticompetitive foreclosure from these two elements), the Commission proceeded to the second prong of the abuse test:

> [T]here are indeed circumstances relating to the tying of WMP which warrant a closer examination of the effects that tying has on competition in this case. While in classical tying cases, the Commission and the Courts considered the foreclosure effect for competing vendors to be demonstrated by the bundling of a separate product with the dominant product, in the case at issue, users can and do to a certain extent obtain third party media players through the Internet, sometimes for free. There are therefore indeed good reasons *not* to assume without further analysis that tying WMP constitutes conduct which by its very nature is liable to foreclose competition.[263]

The Commission thus applied a structured rule of reason approach by examining the anticompetitive effects of the practice, including the efficiency justifications argued by Microsoft and Microsoft's incentives to foreclose, before concluding that Microsoft's conduct infringed Article 82.

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[261] Case C-95/04, British Airways plc v. Comm'n, 2007 E.C.R. I-2331, ¶ 86 (Eur. Ct. Justice).

[262] *Id.* ¶ 106.

[263] *Microsoft Comm'n Decision*, *supra* note 3, ¶ 841.

The CFI accepted the position of the Commission, but used language that limits the scope of the structured rule of reason approach in situations of technological tying. The court mentioned that "while it is true that neither [the] provision nor, more generally, Article 82 EC as a whole contains any reference to the anti-competitive effect of bundling, the fact remains that, in principle, conduct will be regarded as abusive only if it is capable of restricting competition."[264] The court referred to *Michelin II*[265] to substantiate this point, a case standing for the proposition that "establishing the anti-competitive object and the anti-competitive effect are one and the same thing."[266] The following paragraph of the *Microsoft* decision also illustrates the ambivalence of the CFI's approach with regard to the applicable antitrust standard for tying:

> [T]he applicant cannot claim that the Commission relied on a new and highly speculative theory to reach the conclusion that a foreclosure effect exists in the present case. As indicated at recital 841 to the contested decision, the Commission considered that, in light of the specific circumstances of the present case, it could not merely assume, *as it normally does in cases of abusive tying*, that the tying of a specific product and a dominant product has by its nature a foreclosure effect. The Commission therefore examined more closely the actual effects which the bundling had already had on the streaming media player market and also the way in which that market was likely to evolve.[267]

It follows that although the CFI did not reject the structured rule of reason approach of the Commission with regard to technical tying, it maintained its previous quasi-per se illegality approach for all other forms of bundling (essentially contractual tying). In the French version of the same paragraph, the CFI even uses the expression "*effet d'exclusion sur le marché per se*" (bundling of two products by a dominant undertaking leads to an exclusionary effect per se) when it refers to the "normal" approach for abusive tying cases.

In sum, in examining the existence of the fourth step of a tying claim,[268] the CFI did not presume that there was foreclosure of competition from the simple fact that a dominant undertaking tied two distinct products; instead, it found that one had to determine if the foreclosure of competitors led to anticompetitive effects and if there were objective justifications (efficiencies). It seems, therefore, that the analysis of objec-

[264] *Microsoft CFI Decision*, *supra* note 5, ¶ 867.

[265] Case T-203/01, Manufacture Française des Pneumatiques Michelin v. Comm'n (*Michelin II*), 2003 E.C.R. II-4071, ¶ 239 (Ct. First Instance).

[266] *Id.* ¶ 241.

[267] *Microsoft CFI Decision*, *supra* note 5, ¶ 868 (emphasis added).

[268] *Id.* ¶ 852 (referring to ¶ 842).

tive (or efficiency) justifications constitutes a necessary complement to the analysis of the existence of an anticompetitive foreclosure. This in turn implicitly injects a structured rule of reason approach into the analysis of technological tying, which raises the issue of who has the burden of proof of the anticompetitive effects and objective justifications (burden of proof) and how much evidence is required (standard of proof).

The court explained the position clearly with regard to the issue of the burden of proof:

> [A]lthough the burden of proof of the existence of the circumstances that constitute an infringement of Article 82 EC is borne by the Commission, it is for the dominant undertaking concerned, and not for the Commission, before the end of the administrative procedure, to raise any plea of objective justification and to support it with arguments and evidence. It then falls to the Commission, where it proposes to make a finding of an abuse of a dominant position, to show that the arguments and evidence relied on by the undertaking cannot prevail and, accordingly, that the justification put forward cannot be accepted.[269]

The CFI seems to distinguish between the legal burden of proof that is borne by the plaintiff and the evidentiary burden of proof of objective justifications that is borne by the defendant. If the defendant raises these objective justifications, the burden shifts to the plaintiff. The position is not very different from that prevailing in U.S. antitrust law.[270]

There are, however, important dissimilarities with regard to the standard of proof for objective justifications—that is, the amount of evidence required by the defendant to substantiate efficiency gains. The Commission's *Guidance* subjects objective justifications to four cumulative requirements, similar to those required for the application of Article 81(3):

> [T]he dominant undertaking will generally be expected to demonstrate, with a sufficient degree of probability, and on the basis of verifiable evidence, that the following cumulative conditions are fulfilled:
> – the efficiencies have been, or are likely to be, realised as a result of the conduct. They may, for example, include technical improvements in the quality of goods, or a reduction in the cost of production or distribution;
> – the conduct is indispensable to the realisation of those efficiencies: there must be no less anti-competitive alternatives to the conduct that are capable of producing the same efficiencies;
> – the likely efficiencies brought about by the conduct outweigh any likely negative effects on competition and consumer welfare in the affected markets;

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[269] *Id.* ¶ 1144.
[270] *See* United States v. Microsoft Corp., 253 F.3d 34, 59 (D.C. Cir. 2001).

– the conduct does not eliminate effective competition, by removing all or most existing sources of actual or potential competition.[271]

The Commission's *Guidance* employs a slightly different formulation of the third requirement, in comparison to the text of Article 81(3), by not explicitly requiring that "a fair share of the resulting benefit" be passed on to consumers. However, this requirement was interpreted restrictively by the Guidelines on Article 81(3), paragraph 85 (the net effect of the agreement must at least be neutral from the point of view of those consumers directly or likely affected by the agreement). The requirement in the Commission's *Guidance* that "the likely efficiencies brought about by the conduct outweigh any likely negative effects on competition and *consumer welfare* in the affected markets" has the same meaning.[272] According to the *Guidance*, "[i]t is incumbent upon the dominant undertaking to provide all the evidence necessary to demonstrate that the conduct concerned is objectively justified," the Commission making "the ultimate assessment of whether the conduct concerned is not objectively necessary and, based on a weighing-up of any apparent anti-competitive effects against any advanced and substantiated efficiencies, is likely to result in consumer harm."[273]

In practice, it would be very difficult for a dominant undertaking to prove the existence of objective justifications, the control and the conditions for such a defense being at least as restrictive as the conditions of Article 81(3).[274] In contrast, the standard of proof for anticompetitive foreclosure (and consumer harm) is particularly low, as there is no need to prove the existence of an actual or direct consumer detriment.[275] There is, thus, an important asymmetry between the standard of proof that is required from the plaintiff and the standard of proof required by the defendant, to the benefit of the former.

This asymmetry of the standard of proof in EC competition law is the principal reason why it is normatively undesirable to adopt a presumption of consumer harm when an undertaking with a dominant position employs tying/bundling practices, subject to the assessment of efficiency justifications.[276] It is true that the single monopoly profit theorem, which constitutes the Chicago School's foundation stone, applies only in cer-

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[271] *Guidance*, *supra* note 70, ¶ 30 (footnote omitted).
[272] *Id.* (emphasis added).
[273] *Id.* ¶ 31.
[274] *See* Case C-95/04, British Airways plc v. Comm'n, 2007 E.C.R. I-2331, ¶ 86 (Eur. Ct. Justice).
[275] *Id.* ¶ 106.
[276] For such a proposal, see Elhauge, *supra* note 8, at 442–51.

tain restrictive conditions and is therefore unfit for policy prescription. However, relying only on market power and absence of objective justifications[277] may increase the risk of false positives because of the asymmetry of the standard of proof between anticompetitive effects and objective justifications in EC competition law. Thus, because of this specific asymmetry of the standard of proof, the requirement of anticompetitive foreclosure, on top of market power/dominant position, may reduce the risk of over-inclusive antitrust standards for tying/bundling practices. This approach will be compatible with the emphasis given by EC competition law on consumer sovereignty and competition as a process of rivalry rather than on consumer surplus and competition as an efficient outcome, which explains the first prong of the abuse test in Article 82. The plaintiff should bring evidence that the competitors will be excluded or marginalized as a consequence of the tying/bundling practice. It is true that this requirement will not take into account two of the "power effects" of tying, which are that "tying can profitably allow price discrimination among buyers of the tying product"[278] and that tying can "profitably permit price discrimination across buyers of both products."[279] In contrast to Section 2 of the Sherman Act, Article 82 does not, however, prohibit the acquisition or exercise of market power but only its abuse. Furthermore, price discrimination constitutes a distinct claim from tying of an abuse of a dominant position under Article 82, with specific requirements for its application. In conclusion, proof of foreclosure of rivals should form a necessary step of the analysis of tying/bundling or loyalty rebates. But is it a sufficient condition for inferring consumer harm?

### B. When Does the Foreclosure of a Competitor Produce Consumer Harm?

Proving anticompetitive foreclosure requires an analysis of the concrete effects of the practice adopted by the alleged monopolist (or dominant firm). It is therefore necessary to analyze how the specific practice may affect consumers. Just excluding or foreclosing competitors is not sufficient to substantiate a claim of anticompetitive foreclosure.[280] Some-

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[277] On the distinction between competition as a process of rivalry and competition as an efficient outcome, see Mark Blaug, *The Fundamental Theorems of Modern Welfare Economics, Historically Contemplated*, 39 HIST. POL. ECON. 185 (2007).

[278] Elhauge, *supra* note 8, at 404.

[279] *Id.* at 405.

[280] This is particularly clear in the recent Commission Notice on the Guidelines on the Assessment of Non-Horizontal Mergers Under the Council Regulation on the Control of Concentrations Between Undertakings, 2008 O.J. (C 265) 6, where the Commission distinguishes between "foreclosure" ("any instance where actual or potential rivals' access to

thing more is required. This is an assertion to which both EC and U.S. antitrust law would agree, at least for technological (technical) tying. There is, however, a significant divergence between the European and the U.S. approach with regard to these additional elements that may substantiate a finding of anticompetitive foreclosure. The role and the standard of proof of objective (or efficiency) justifications were examined in the previous section. We will now focus our analysis on two other factors considered: the anticompetitive harm inquiry and evidence of consumer detriment.

The denial of market access to rivals does not by itself constitute evidence of anticompetitive foreclosure, but only a starting point for the analysis of exclusionary abuses. Both EC and U.S. antitrust law require a showing of anticompetitive harm that links the exclusion of the competitors to the existence of a consumer detriment or to a negative consumer welfare effect. "Leveraging" constitutes an anticompetitive harm in Europe, although it seems to be controversial in the United States. Anticompetitive leveraging was one of the main theories of harm advanced by the Commission in the *Microsoft* case.[281] The CFI also relied on the same theory of anticompetitive harm[282] and confirmed, on this basis, the substantial fine imposed by the Commission.[283]

One could compare the approach of the Commission and the CFI with that of the U.S. case against Microsoft, where the separate claim of monopoly leveraging was dismissed by Judge Jackson of the D.C. District Court.[284] Although the Supreme Court revived a version of the leverage theory in *Eastman Kodak*,[285] it has recently held in *Trinko* that for a leverage claim to succeed there must be a "'dangerous probability of success' in monopolizing a second market."[286] The existence of market power in

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supplies or markets is hampered or eliminated as a result of the merger, thereby reducing these companies' ability and/or incentive to compete," which as such does not bring evidence of a significant impediment to effective competition) and "anticompetitive foreclosure" (when as a result of such foreclosure the merging company will be able to harm consumers), *id.* ¶ 18.

281 *Microsoft Comm'n Decision*, *supra* note 3, ¶ 982.

282 *Microsoft CFI Decision*, *supra* note 5, ¶¶ 1344, 1347.

283 *Id.* ¶ 1363.

284 In *United States v. Microsoft Corp.*, No. CIV.A. 98-1232 (TPJ), 1998 WL 614485 (D.D.C. Sept. 14, 1998), where "[b]ecause the theory of 'monopoly leveraging' is inconsistent with both the Sherman Act's plain text and with Supreme Court pronouncements on the general limitations of its reach," Judge Jackson granted summary judgment in favor of Microsoft (*id.* at *1) and did not accept that "Microsoft [had] unlawfully used its operating system monopoly to obtain a competitive advantage in the browser market," as the States' complaints alleged. *Id. Accord id.* at *26–*27.

285 *See* Eastman Kodak Co. v. Image Tech. Servs., Inc., 504 U.S. 451, 497 (1992).

286 Verizon Commc'ns Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 415 n.4 (2004) (quoting Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 459 (1993)). In this

an adjacent market does not seem to be a requirement for the application of the leverage theory in Europe.[287] Consequently, the standard of proof for leverage claims is higher in the United States than in Europe.[288]

The EC and U.S. approaches also diverge with respect to the analysis of the anticompetitive effects. The Commission claimed in its *Microsoft* decision that the tying of WMP had not only foreclosed competition in the media players market,[289] but had also "spillover effects on competition in related products such as media encoding and management software (often server-side)," as well as "in client PC operating systems for which media players compatible with quality content are an important application."[290] The Commission found the following anticompetitive effects:

- Microsoft uses Windows as a distribution channel to ensure for itself a significant competitive advantage on the media players market;
- because of the bundling, Microsoft's competitors are a priori at a disadvantage even if their products are inherently better than Windows Media Player;
- Microsoft interferes with the normal competitive process which would benefit users by ensuring quicker cycles of innovation as a consequence of unfettered competition on the merits;
- the bundling increases the content and applications barriers to entry, which protect Windows, and facilitates the erection of such barriers for Windows Media Player;
- Microsoft shields itself from effective competition from vendors of potentially more efficient media players who could challenge its position, and thus reduces the talent and capital invested in innovation of media players;

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case, the Supreme Court erred by misunderstanding the fact that Verizon was a monopolist of both the infrastructure network as well as the retail local telecommunications services that were produced using that network and for which use of that network was essential. Verizon leveraged its network infrastructure monopoly by using strategies that raised the costs and degraded the quality of rivals who leased parts of its network to enhance and preserve its monopoly. *See* Nicholas Economides, *Vertical Leverage and the Sacrifice Principle: Why the Supreme Court Got* Trinko *Wrong*, 61 N.Y.U. ANN. SUR. AM. L. 379 (2005); Nicholas Economides, *Hit and Miss: Leverage, Sacrifice, and Refusal to Deal in the Supreme Court Decision in* Trinko, 10 VAND. J. ENT. & TECH. LAW 121 (2007).

[287] *See Microsoft CFI Decision*, *supra* note 5, ¶ 599 (although this paragraph relates to the refusal to supply part of the case, it applies to all types of leverage theory claims, such as the bundling of Windows and WMP).

[288] Leverage claims are rarely successful in the United States. *But see* Conwood Co. v. U.S. Tobacco Co., 290 F.3d 768 (6th Cir. 2002).

[289] *See Microsoft Comm'n Decision*, *supra* note 3, ¶¶ 835–954.

[290] *Id.* ¶ 842.

– by means of the bundling, Microsoft may expand its position in adjacent media-related software markets and weaken effective competition, to the detriment of consumers;
– by means of the bundling, Microsoft sends signals which deter innovation in any technologies in which it might conceivably take an interest and which it might tie with Windows in the future.[291]

The CFI conducted a limited analysis of the alleged anticompetitive effects. This is normal practice as Article 230[292] institutes a limited control of the legality of the Commission's decisions and the intensity of the judicial review of the economic reasoning of the Commission is necessarily restricted.[293] The CFI concluded that "there was a reasonable likelihood that tying Windows and Windows Media Player would lead to a lessening of competition so that the maintenance of an effective competition structure would not be ensured in the foreseeable future."[294] The CFI used the expression "reasonable likelihood" of anticompetitive effects, instead of the expression "capable of having" anticompetitive effects, which it had used in previous decisions.[295] It also used the expression "actual effects" when it referred to the Commission's analysis of the anticompetitive effects of bundling.[296]

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[291] *Microsoft CFI Decision*, *supra* note 5, ¶ 1088 (citations omitted).

[292] Treaty Establishing the European Community (consolidated version), art. 230, Dec. 29, 2006, 2006 O.J. (C 321E) 37.

[293] *Microsoft CFI Decision*, *supra* note 5, ¶¶ 87–89; *see also* Hubert Legal, *Standards of Proof and Standards of Judicial Review in EU Competition Law*, *in* 2005 FORDHAM CORP. L. INST. 107 (Barry Hawk ed., 2006). Compare, however, the recent case law of the CFI and ECJ on the standard of judicial review for merger cases. *See* Matteo F. Bay & Javier Ruiz Calzado, Tetra Laval II*: The Coming of Age of the Judicial Review of Merger Decisions*, 28 WORLD COMPETITION 433 (2005).

[294] *Microsoft CFI Decision*, *supra* note 5, ¶ 1089.

[295] Case T-219/99, British Airways plc v. Comm'n, 2003 E.C.R. II-5917, ¶ 293 (Ct. First Instance). In *British Airways*, the CFI held that "it is sufficient . . . to demonstrate that the abusive conduct of the undertaking in a dominant position tends to restrict competition, or, in other words, that the conduct is capable of having, or likely to have, such an effect." *Id.* The Commission has also referred to the "capability of conduct to foreclose" and to the "likelihood that an anticompetitive foreclosure effect results [from that conduct]." *Discussion Paper*, *supra* note 70, ¶ 59. To compare with the standard of proof when leverage through bundling is examined under the merger regulation, see Case T-210/01, General Electric Co. v. Commission, 2005 E.C.R. II-5575, ¶¶ 399–474 (Ct. First Instance) (the Commission has to establish that the merged entity would have been likely (in other words would have sufficient incentives) to engage in bundling practices). The Commission has also to consider "the potentially unlawful, and thus sanctionable, nature of certain conduct as a factor, which might diminish, or even eliminate, incentives for an undertaking to engage in particular conduct." *Id.* ¶ 304; *accord* Case C-12/03, Comm'n v. Tetra Laval BV, 2005 E.C.R. I-987, ¶¶ 74–78 (Eur. Ct. Justice). However, both of these requirements relate to the prospective analysis undertaken under the merger regulation and do not therefore indicate, as such, a higher standard of proof compared to that applied in Article 82 cases for bundling.

[296] *Microsoft CFI Decision*, *supra* note 5, ¶ 1035.

A closer look at the alleged anticompetitive effects and their analysis by the court reveals though that most of these negative effects on consumers were indirect and emanated from the fact that Microsoft—as compared with its media player rivals—benefited from an "unparalleled advantage with respect to the distribution of its product" that "inevitably had significant consequences for the structure of competition" on the streaming media player market.[297]

First, the bundling of Windows and WMP allowed WMP to benefit "from the ubiquity of that operating system on client PCs, which cannot be counterbalanced by the other methods of distributing media players."[298] There was a risk that the Windows Media Player would become the de facto standard for the media player market as a result of Microsoft's leveraging of its quasi-monopoly from the PC operating system market to the media player market. Although the court accepted that "standardisation may effectively present certain advantages," it did not accept that an undertaking in a dominant position could impose that by means of tying.[299] The emergence of a de facto standard should be the result of competition between the "intrinsic merits" of the products and, in short, depends on the consumers' choice rather than from the arbitrary decision of a dominant firm to impose its own standard.[300]

Second, Microsoft's bundling practice would have restricted consumers' access to similar or better quality products than WMP.[301] Because of the bundling practice, "consumers have an incentive to use Windows Media Player at the expense of competing media players, notwithstanding that the latter players are of better quality."[302] The CFI based this finding on the comparative reviews of media players presented by Microsoft during the administrative procedure before the Commission's decision. These comparative reviews indicated that WMP was of lower quality than some of the other excluded media players, having achieved a lower rank than RealPlayer in more than half of these reviews.[303]

Third, the ubiquity of WMP as a result of its bundling with Windows was capable of having "an appreciable impact on content providers and software designers" because of the significant "indirect network effects"

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[297] *Id.* ¶ 1054.
[298] *Id.* ¶ 1036.
[299] *Id.* ¶ 1152.
[300] *Id.* ¶¶ 1040, 1046–1047.
[301] *Id.* ¶ 1356.
[302] *Id.* ¶ 971.
[303] *Microsoft Comm'n Decision*, *supra* note 3, ¶¶ 949–951.

("positive feedback loop") that existed in the WMP market.[304] The greater the number of users of a given software platform, the more will be invested in developing products compatible with that platform, which in turn will reinforce the popularity of that platform with users.[305] There indeed was evidence that the content providers and software developers chose the technology for which they develop their own products on the basis of the percentage of installation and use of media players. Because of additional development and administrative costs, the developers were inclined to use only one technology for their products. Encoding streamed content in several formats is expensive and time-consuming, and these costs may not be outweighed by the advantages of increasing the potential reach of content providers and software developers' products.[306]

The ubiquity of WMP on Windows PCs "secured Microsoft a competitive advantage unrelated to the merits of its products" and erected a barrier to entry to new "contenders," not only on the media players market but also "on other adjacent markets," such as "media players on wireless information devices, set-top boxes, DRM solutions and on-line music delivery."[307] The evolution of the market consistently pointed to "a trend in favour of usage of [WMP] and Windows Media formats to the detriment of the main competing media players (and media technologies)," such as RealPlayer and QuickTime Player.[308] Furthermore, RealPlayer's installed base was significantly lower than that of WMP, as it was present on only 60 to 70 percent of home PCs in the United States, while the rate of installation of WMP was 100 percent on Windows client PCs and more than 90 percent on all client PCs, including non-Windows ones.[309]

Significantly, nowhere does the CFI discuss the existence of direct consumer harm, but it instead seems to infer consumer detriment from the alteration of the competitive structure of the media player market. This is in conformity with the approach generally followed by the European Courts for exclusionary abuses under Article 82.[310] The preserva-

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304 *Microsoft CFI Decision*, *supra* note 5, ¶¶ 1060–1061.
305 *Id.*
306 *Id.* ¶¶ 1065–1066.
307 *Id.* ¶¶ 1069, 1076.
308 *Id.* ¶¶ 1078–1081.
309 *Id.* ¶ 1087.
310 Case C-95/04, British Airways plc v. Comm'n, 2007 E.C.R. I-2331, ¶ 106 (Eur. Ct. Justice) ("Article 82 EC is aimed not only at practices which may cause prejudice to consumers directly, but also at those which are detrimental to them through their impact on an effective competition structure, such as is mentioned in Article 3(1)(g) EC."). In the context of Article 81 EC, see Case C-8/08, T-Mobile Netherlands v. Raad vanbestuur van de Nederlandse Mededongingsautonteit, at ¶ 38 (Eur. Ct. Justice June 4, 2009) (summary

tion of the competitive process constitutes an important objective of EC competition law. Advocate General Kokott in *British Airways* has explained this position:

> The starting-point here must be the protective purpose of Article 82 EC. The provision forms part of a system designed to protect competition within the internal market from distortions (Article 3(1)(g) EC). Accordingly, Article 82 EC, like the other competition rules of the Treaty, is not designed only or primarily to protect the immediate interests of individual competitors or consumers, but to protect the *structure of the market* and thus *competition as such (as an institution)*, which has already been weakened by the presence of the dominant undertaking on the market. In this way, consumers are also indirectly protected. Because where competition as such is damaged, disadvantages for consumers are also to be feared.[311]

Thus, the ECJ and the CFI take a long-term view of consumer detriment and favor the protection of competitors instead of short-term efficiencies. This approach contrasts with the dominant approach of the U.S. courts to require evidence of at least an increase in prices or a reduction of output in the market.[312]

The perspective of the European Courts is that competition is a process of discovering the most efficient solution that benefits consumers and that restricting competition (in the sense of less rivalry in the market) is presumed to reduce efficiency and be detrimental to consumers in the long term, in particular if the undertaking has an overwhelming dominant position. The obvious shortcoming of this approach is the absence of clear boundaries for competition law enforcement. This approach may also explain why EC competition law considers that anticompetitive effects may result not only from practices that restrict output or increase prices, but also those that restrict more broadly con-

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at 2009 O.J. (C 180) 12) ("Article 81 EC, like the other competition rules of the Treaty, is designed to protect not only the immediate interests of individual competitors or consumers but also to protect the structure of the market and thus competition as such."), *available in full at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:62008J0008:EN:HTML.

[311] *Id.* ¶ 68 (opinion of Advocate General Kokott) (emphasis added) (footnotes omitted).

[312] *See* United States v. Microsoft Corp., 253 F.3d 34, 84 (D.C. Cir. 2001). Section 1 cases: NCAA v. Bd. of Regents of Univ. of Okla., 468 U.S. 85 (1984); FTC v. Ind. Fed'n of Dentists, 476 U.S. 447 (1986) (requiring evidence of anticompetitive effects in the form of reduced output, higher prices or diminished quality). For a comparison, see Barry E. Hawk, *Article 82 and Section 2, in* OECD, POLICY ROUNDTABLES: COMPETITION ON THE MERITS 2005 at 251 (2005), *available at* http://www.oecd.org/dataoecd/7/13/35911017.pdf.

sumer choice.[313] It is not clear, however, if choice is valued as such or if it is preserved only when more choice is likely to lead to identifiable consumer benefits, such as better quality products, lower prices, and additional services.

The CFI's *Microsoft* decision seems to indicate that choice was valued with the purpose of preserving the continuing offer in the market of media players that were at least of similar, if not better, quality than WMP.[314] What would have been the position of the Commission and the CFI if there was no evidence that the excluded media players were better, or at least similar quality, products than WMP? The language used by the CFI[315] seems to indicate that the preservation of consumer choice is linked to the preservation of the competitive structure of the market and the protection of competitors. If this interpretation is correct, then there ultimately is little difference between the previous quasi-per se illegality approach for tying and the CFI's position in *Microsoft* on technological tying.

A possible limiting principle to the expansive approach of the CFI with regard to the scope of Article 82 is the unique character of the *Microsoft* case. The court considered that the ubiquity of Windows granted Microsoft's WMP an overwhelming distribution advantage, compared to other media players. The existence of important network effects provided Microsoft with the opportunity to extend its quasi-monopoly to other markets and to exclude even products of equal or superior quality. Without employing the essential facilities terminology, the court concluded that it would have been very difficult, or even impossible, for other media players to compete on equal terms with WMP without having effective (meaning without additional costs for the final consumer) access to the Windows platform. The protection of the competitive process seems in this case intrinsically linked to the concept of consumer sovereignty, as consumers' effective choice would have been limited by Microsoft's "artificial selection" of media player. The emphasis given to the protection of the competitive process is therefore explained by the presumption that the extension of Microsoft's quasi-monopoly to the media player market would marginalize all existing or potential competition and could therefore lead to consumer harm. The

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[313] *See* Commission Notice on the Guidelines on the Application of Article 81(3) of the Treaty, *supra* note 117, ¶ 24 (interpreting anticompetitive effects as including negative effects on prices, output, innovation, or the variety or quality of goods and services).

[314] *Microsoft CFI Decision*, *supra* note 5, ¶ 1356.

[315] "Microsoft impaired the effective competitive structure on the work-group server operating systems market by acquiring a significant market share on that market." *Id.* ¶ 664.

assumption is that competition guarantees consumer sovereignty, while monopoly does not.

## III. A DIFFERENT EMPHASIS ON CONSUMER CHOICE AND ADEQUATE REMEDIES

Antitrust and competition law are for the benefit of consumers and not necessarily the benefit of competitors.[316] Consumers benefit from lower prices. Consumers also benefit from having choices both in abundance of varieties offered as well as from availability of an array of goods of different quality levels.[317] The effects of tying and bundling are complex and require significant economic analysis to be fully understood, as discussed earlier. The effects of these practices have not yet been fully analyzed by economists, and the legal understanding of economic analysis suffers from significant lags. In the two *Microsoft* cases, the issue of consumers' harm was particularly complicated because, in both the U.S. and EU cases, both the tied products (Internet Explorer and WMP, respectively) and the competing products (Netscape and RealAudio) were offered (at least in their basic versions) at no charge.

The fact that the incremental cost of licensing software is negligible allows it to be distributed for free with the expectation or hope that the software development cost will be recouped if (i) in the future the product will be sold at a positive price; (ii) the firm will be able to sell upgraded versions of the software (with more features) at a positive price; or (iii) the firm will be able to sell products or services complementary to the free product (for example, sell music or video downloads at a positive price). The EU case was additionally complicated by the fact that the WMA format (which is the default format for the WMP) also was publicly available, and a number of firms competing with Microsoft distributed players that played content in this format, among others. In fact, in the peculiar world of freely distributed software, and in particular in media players, we observe a number of companies distributing players that each have a favored format and at the same time can play in a number of other formats, to the extent that the other format owners allow it. So, for example, WMP plays WMA and MP3 formats among others but does not play the RealAudio format because its specifications have not been made public. Similarly, RealAudio plays its proprietary format, as well as WMA, MP3, and others. The distribution advantage that any player enjoys also is limited because each media player can be

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[316] *See* Case T-168/01, GlaxoSmithKline Servs. Unlimited v. Comm'n, 2006 E.C.R. II-2969, ¶¶ 121, 171 (Ct. First Instance).

[317] *See* Neil W. Averitt & Robert H. Lande, *Using the "Consumer Choice" Approach to Antitrust Law*, 74 ANTITRUST L.J. 175 (2007).

downloaded and installed in a few minutes. Additionally, in the aftermath of the *United States v. Microsoft* settlement, any consumer as well as any computer manufacturer can set up any media player as the default one.

The lack of friction in the distribution of all media players, the zero price, the quick download and installation, the ability of the consumer to designate the default media player, and the fact that many media players each play many formats, make it likely that the potential loss to consumers from a skewed distribution of market shares in the media players market will be small. The fact that many players play many formats each, and the fact that they can be downloaded freely and easily, has resulted in many consumers having installed in the same computer and using in the same time period more than one media player. In this setup, it is much more difficult to foreclose rival media players. Similarly, the fact that many media players from different producers each play many formats reduces the chance that some formats will be marginalized or foreclosed.[318] The Commission and the court may have overestimated the distributional advantage conferred to WMP by Windows. Furthermore, in a market where *all* products are priced at zero, it is hard to make an argument of consumer loss because of an anticompetitive price change. It also is hard to make a convincing argument of anticompetitive effects based on pricing below cost by Microsoft because all firms in this market are pricing below cost.

There are only two potentially credible consumer detriment arguments: (i) that there is a restriction of variety or reduction in quality because of the tying of WMP with Windows, and (ii) that there will be a clear detriment to future consumers if WMA becomes the dominant standard in media players. The Commission argued that the eventual dominance of WMP (which it incorrectly predicted) would create a restriction of quality in media players. Not only are these quality differences difficult to establish factually in a high-technology market where product specifications change frequently, but blaming a zero-priced product for its low quality is going a bit far. The Commission also made the argument that future consumers will lose because of less innovation. From an economics point view, it is not always easy to sustain such an argument because there are published economic models where a monopolist innovates more than a perfectly competitive industry.[319]

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[318] If RealAudio was trying to get the largest market share for its format, it is surprising that RealAudio did not license its format to be used (among other formats) in rival players.

[319] Additionally, in the software industry (and in other high technology industries) there are plenty of examples of innovative small new firms being acquired by larger and estab-

The Commission imposed as a remedy on Microsoft the requirement to produce and distribute in the European Union a version of Windows without a media player, which became known as Windows-N. The Commission's remedy allowed Microsoft to continue producing and distributing in the European Union and the United States a version of Windows that was subject to the requirements of the consent decree that resolved *United States v. Microsoft.* The EU did not mandate a specific price difference between Windows and Windows-N.[320] The two versions of Windows were sold at the same price and practically no OEM bought and adopted Windows-N. Thus, the remedy imposed by the Commission had no noticeable effect in the marketplace. At the same time, the dire predictions of expanded dominance of WMA never materialized in the long period between the beginning of the EU case and the Commission's decision. In contrast, a new proprietary format promoted by Apple (tied to hardware also produced by Apple) has become the dominant format in the market for song downloads, a key market for goods that are complementary to media players. Additionally, "flash player," a new player from Adobe, has become the standard video player in Internet browsers.

The most surprising element in the EU decision was the remedy. It was almost mathematically certain that Windows-N (without WMP) sold at the same price as Windows (with WMP), would not sell well, and therefore would have no impact. It is also hard to imagine how depriving consumers of WMP in Windows-N in the post-U.S.-settlement environment, where both the OEM and the final consumer can designate any media player as the default one, would have enhanced consumers' choice. To the extent that the OEMs' purchasing decisions express the desires of consumers, the devastating failure of Windows-N to sell is evi-

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lished firms and using the distribution channels of the established firms. An assessment of innovation incentives without such consideration could lead to the wrong conclusions. *But see* Richard Gilbert, *Looking for Mr. Schumpeter: Where Are We in the Competition-Innovation Debate?*, 6 INNOVATION POL'Y & ECON. 159 (2006); Richard J. Gilbert, *Competition and Innovation* (Competition Policy Ctr., Paper No. CPC07-069, 2007), *available at* http://repositories.cdlib.org/cgi/viewcontent.cgi?article=1070&context=iber/cpc.

[320] The lack of a price difference requirement is in sharp contrast to the proposal to the district court of the nine states (litigating states) that did not agree with the DOJ-Microsoft settlement that was also signed by nine other states. The litigating states proposed to "freeze Windows" to its pre-1998 state and impose on Microsoft the requirement to sell any additional functionality at an additional price. It is interesting, however, that the CFI noted in its decision that "[s]hould Microsoft now decide to sell the unbundled version of Windows at the same price as the bundled version, the Commission would examine that price by reference to the present market situation and in the light of Microsoft's obligations to refrain from any measure having an equivalent effect to tying and, if necessary, adopt a new decision pursuant to Article 82 EC." *Microsoft CFI Decision*, *supra* note 5, ¶ 908.

dence that consumers in fact liked to have WMP in Windows and the imposed remedy was misguided.

Surprisingly, in negotiations before the Commission's decision was announced, the Commission rejected a reported Microsoft proposed remedy to include in the distribution of Windows three rival media players besides WMP and let the consumer designate the default player.[321] This proposal would have guaranteed as wide a distribution of RealAudio and other players as WMP, would have completely erased any distributional advantage of WMP, would have dispelled any tying concerns, and would have given full decision power to consumers. Such a remedy would have addressed the competition law concerns raised by Microsoft's abuse most effectively and precisely.[322] From an economics point of view, this proposal would have eliminated Microsoft's distribution advantage. At the same time, its adoption would have at least guaranteed the ability of even a dominant firm to innovate and distribute in the way it finds most appropriate.

The benefits of this proposal both for consumers and innovation are obvious and substantial in comparison to the imposed remedy.[323] This seems a much more consumer-friendly remedy than the one imposed. It is remarkable that in its most recent investigation of Microsoft's bundling of Windows with Internet Explorer[324] the Commission has noted with interest the commitments offered by Microsoft to address the issues raised by the bundling of Internet Explorer with Windows. Microsoft had withdrawn its unilateral plan of distributing Windows 7-E[325] and pro-

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[321] *See* Byron Acohido & Noelle Knox, *Regulators Want Microsoft to Pull Media Player Out*, USA TODAY, Mar. 25, 2004.

[322] Indeed, the issue in this case was "not that Microsoft integrates [WMP] in Windows, but that it offers on the market only a version of Windows in which [WMP] is integrated, that is to say, that it does not allow OEMs or consumers to obtain Windows without [WMP] or, at least, to remove [WMP] from the system consisting of Windows and [WMP]." *Microsoft CFI Decision*, *supra* note 5, ¶ 1149. The remedy could have identified a number of media players from those existing at the time of the commitment of the abuse that would have been integrated into Windows. It is in this respect different from a common carrier obligation, as it would not necessarily have extended to media players that would have been commercialized after the termination of the abuse.

[323] This is particularly surprising since Professor Mario Monti, Commissioner for Competition at the time, was quoted as to the objectives of the Commission in the decision: "In the end, we decided to do what's best for innovation and European consumers." Acohido & Knox, *supra* note 321.

[324] Following complaints by the Norwegian Internet browser maker Opera, in December 2007, the Commission initiated investigations and sent a Statement of Objection (SO) in January 2009 alleging a violation by Microsoft of Article 82 for tying its Web browser Internet Explorer to its dominant client PC operating system Windows. *See* Press Release, European Comm'n, *supra* note 196.

[325] Microsoft intended to produce and distribute in Europe a special edition of Windows 7, called Windows 7-E, which would not have Internet Explorer or any other browser pre-

posed a final resolution that would commit[326] it to (i) distribute a "ballot screen" through software update[327] to EEA users of Windows XP, Windows Vista and Windows Client PC Operating Systems, by means of Windows Update; and (ii) allow both computer manufacturers and users to turn on or off Internet Explorer.[328] The ballot screen will allow consumers to choose among a number of Internet browsers. This screen will be available only to users whose computers came from the manufacturer with Internet Explorer installed as the default browser. Thus, a browser manufacturer other than Microsoft could provide an incentive to OEMs to install its browser as the default, and then the end user of such a computer will not be offered the choice of the ballot screens.[329] In that sense, the playing field is tilted against Microsoft and in favor of browsers made by for-profit companies that can afford to provide incentives to OEMs. The ballot screen procedure also differs from the "Set Defaults" requirement of the U.S. *Microsoft* settlement that was available to *all* users and covered all middleware, including browsers. On October 7, 2009, the EU gave its preliminary approval to the ballot screen proposal and opened it to testing and feedback.[330]

## IV. CONCLUSION

It is widely accepted that doctrinal categories or concepts emerge to serve a specific (analytical or other) purpose, intrinsically linked to the

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installed, adopting the removal approach of the Windows-N remedy imposed by the Commission in the WMP case as the sole version of Windows in Europe. Computer manufacturers (OEMs) would have the option to install an Internet browser of their choice as the default as well as include other browsers before the PC reaches the final consumers. *See* Posting of Dave Heiner to Microsoft on the Issues, http://microsoftontheissues.com/cs/blogs/mscorp/archive/2009/07/31/windows-7-and-browser-choice-in-europe.aspx (July 31, 2009, 17:20 PST).

[326] Proposed Commitment, Microsoft Corp., Commitment to Address the Competition Concerns Identified by the European Commission in Case No. COMP/C-3/39.530 (July 24, 2009), http://www.microsoft.com/presspass/presskits/eu-msft/docs/07-24-09Commitment.doc.

[327] A preliminary design of the ballot screen is available online at http://www.microsoft.com/presspass/presskits/eu-msft/docs/Annex_B.ppt. The words "ballot screen" are used inappropriately; the appropriate words are "choice screen." There is no ballot here and there is no decision by majority or any other rule that will be imposed on all participants. The screen will allow each consumer to set the default browser and, if he wants to, uninstall Internet Explorer.

[328] A detailed description of how this will be implemented in Windows 7 is available at http://www.microsoft.com/presspass/presskits/eu-msft/docs/ANNEX_A.doc.

[329] Similarly, among old PCs, Windows Update will bring up the ballot screen only on those with Internet Explorer installed as default.

[330] *See* Press Release, European Comm'n, Antitrust, Commission Market Tests Microsoft's Proposal to Ensure Consumer Choice of Web Browsers; Welcomes Further Improvements in Field of Interoperability (Oct. 7, 2009) (Memo/09/439). For an analysis of the remedies aspect of the *Microsoft* cases, see Economides & Lianos, *supra* note 4.

meta-principle that inspires the particular disciplinary field.[331] There are two objectives to be served by classifying: First, there is an instrumental one, which "looks to the reasons that the categories were formulated in the first place" and recognizes that "[b]ehind the different categories lie distinct objectives, principles." Second, there is an analytical one where the aim of classification is to create and maintain "a rational structure for doctrine" that would be rigorous enough to fit in different factual contexts.[332] Both of these objectives should be fulfilled for the operation of classification to be useful.

The comparative analysis of the antitrust standards that are being applied to bundling practices in Europe and in the United States shows that the debate over the "right" analogy for both bundled discounts and the required elements of illegal tying (such as the separate products and the coercion tests) are profoundly interlinked with the prior beliefs or the first principles of competition law in each jurisdiction.[333]

To fulfill their analytical objective, categories in antitrust should "have empirical support" and should "communicat[e] valuable information to courts about the competitive effects of a general practice."[334] "Categorical analysis" also should accomplish an instrumental objective. When the aims of competition law are still evolving and unclear, which is still the case in EC competition law,[335] the relative weight of the analytical or instrumental objectives of classification will depend on the availability of empirical evidence on the pro- or anticompetitive effects of the practice. If there is sufficient empirical support and broad consensus in the economics profession over the competitive virtues or the anticompetitive effects of a category of practices, the analytical objective of classification will be more compelling than the instrumental one, and the specific conduct will be analyzed according to the precepts of economic analysis. However, if empirical evidence or broad consensus is insufficient, the classification process will emphasize the instrumental element, and the objectives of competition law and the input of economic analysis will be less significant. The relative discord of economic analysis on bundled discounts and tying is the main reason EC competition law and U.S. antitrust law have adopted different approaches, as each jurisdiction

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[331] *See* Roscoe Pound, *Classification of Law*, 37 HARV. L. REV. 933, 939 (1924).

[332] Jay M. Feinman, *The Jurisprudence of Classification*, 41 STAN. L. REV. 661, 672–73, 675 (1989).

[333] *See* Ken Heyer, *A World of Uncertainty: Economics and the Globalization of Antitrust*, 72 ANTITRUST L.J. 375, 376 (2005).

[334] Lemley & Leslie, *supra* note 7, at 1212.

[335] *See generally* EUROPEAN COMPETITION LAW ANNUAL 1997: THE OBJECTIVES OF COMPETITION POLICY (Claus Dieter Ehlermann & Laraine L. Laudati eds., 1998).

seems to have different prior beliefs on the existence and/or the degree of the duty of dominant firms to preserve the competitive process.

This analytical schism is particularly evident in the way each jurisdiction deals with the issue of anticompetitive foreclosure. It seems that in Europe the causal link between anticompetitive foreclosure and consumer harm is easily found, that consumer detriment is interpreted very broadly, and that it is not always a requirement for the application of Article 82, or at least that the standard of proof of a consumer detriment is very low in bundling cases compared to the U.S. approach. This, as well as the broad interpretation of the coercion requirement for tying cases, may lead to the risk of over-enforcement of Article 82, and consequently to false positives, as rivals may use Article 82 to extract favorable terms in settlements or to impose an important litigation burden on the dominant firm. This can be avoided if the courts strengthen the standard of proof of anticompetitive effects by requiring a consistent theory of consumer harm, reduce the asymmetry of the standard of proof between anticompetitive effects and efficiency gains, and examine in depth the cost and benefits of the given practice for the consumer (an anticompetitive foreclosure test).

In the meantime, the hostility of the CFI to bundling practices in *Microsoft* will certainly lead to a number of cases being brought to the European Commission and courts by marginalized rivals because of Microsoft's significant distribution advantage. As the CFI recognized in *Microsoft*:

> Since Microsoft is very likely to maintain its dominant position on the client PC operating systems market, at least over the coming years, it cannot be precluded that it will have other opportunities to use leveraging vis-à-vis other adjacent markets. Furthermore, Microsoft had already faced proceedings in the United States for a practice similar to the abusive tying at issue, namely the tying of its Internet Explorer browser and its Windows client PC operating system, and the possibility cannot be precluded that it might commit the same type of infringement in future with other application software.[336]

In fact, even Microsoft's U.S. antitrust problems have yet to end. In April 2009, court oversight of Microsoft's compliance with prior anti-

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[336] *Microsoft CFI Decision*, *supra* note 5, ¶ 1363; *see also* Neelie Kroes, European Comm'r for Competition Policy, Introductory Remarks on Microsoft's Compliance with March 2004 Antitrust Decision, Remarks at Press Conference in Brussels (Oct. 22, 2007) (Speech/07/647) ("[T]he March 2004 Decision, as confirmed by the Court of First Instance last month, also sets a precedent with regard to Microsoft's future market behaviour in this and other areas. Microsoft must bear this in mind.").

trust settlements was extended for the second time, to May 2011.[337] The recent developments in the European Union—including the European Commission's investigation of Microsoft for bundling Internet Explorer with Windows[338] and the current consideration of a "ballot screen" remedy[339]—illustrate that, for now, perhaps the only possible limiting principle for the application of Article 82 to the bundling practices of Microsoft may be international comity for similar practices that have been the object of a U.S. settlement.[340] Without doubt, the CFI's decision does not mark the end of the *Microsoft* case(s).

[337] Jacqui Cheng, *Microsoft in "Much Better Place": Oversight Extended to 2011*, ARS TECHNICA, Apr. 22, 2009, http://arstechnica.com/microsoft/news/2009/04/antitrust-oversight-of-microsoft-extended-to-may-2011.ars.

[338] Press Release, European Comm'n, Antitrust: Commission Initiates Formal Investigations Against Microsoft in Two Cases of Suspected Abuse of Dominant Market Position (Jan. 14, 2008) (Memo/08/19).

[339] *See supra* note 327.

[340] In *Microsoft* the CFI adopted a restrictive position on the sufficiency of the U.S. settlement to put an end to the abuse. *Microsoft CFI Decision*, *supra* note 5, ¶¶ 272, 274, 1227.