Comparative Antitrust Enforcement and Business History

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"For good or ill," observed New York commercial lawyer Barry Hawk in 1992, "we shall have to live throughout most of the world with clones of Article 85 and 86 [81 and 82]. That means dominant firm behavior will be more closely scrutinized than would be the case if [the Sherman Act's] section 2 were the model." Eleven years later, the *OECD Journal of Competition Law and Policy* published the results of a worldwide survey of antitrust regimes. The U.S. antirust regime's core objectives were exceptional in that they combined solely the achievement of "greater economic efficiency" with "promoting and protecting the competitive process." More typical was the European Commission, which balanced these "core competition objectives" with attaining "one or more public interest objectives." The following comments consider the divergent U.S. and EU approaches to cases from an "old" and a "new" industry, tobacco and computers. The purpose is to suggest that antitrust regimes, including their enforcement objectives, reflect the indigenous business-government order within the long-term development of the global political economy. What antitrust enforcement officials determine to be "efficient" or "abusive" conduct in particular industries can benefit, therefore, from considering evidence of these long-term developments. Thus, the EU's approach to "dominance" maybe more typical than America's because it resonates more generally with the history of business-government relations in other nations.

I. Comparative Antitrust Regimes and Business History

Antitrust regimes share a common institutional culture, but also reflect divergent business-government orders. Generally, antitrust regimes possess relative bureaucratic autonomy defined by prescribed due process standards and judicial review. Still, differences in substance and procedure are significant, especially regarding legal damage systems and claims of private parties which are strongest in American antitrust. US antitrust arose from a long history of conflict between business and government rooted in Americans' engrained resistance to unchecked economic and political power. In addition, the nation's deep popular attachment to individualism favored business enterprise and innovation at the same time it embodied the faith that capitalist initiative could be held accountable to a wider public interest. By comparison, despite noteworthy differences between British and German or French legal systems, the European Commission's antitrust enforcement relied more on a bureaucratic approach to business-government relations than American judiciary-centered antitrust. Japan's antitrust regime relied even more than its European counterpart on bureaucratic intervention. Australia borrowed freely from the pragmatic British approach and post-World War II American antitrust principles to create an antitrust regime suited to its unusual system of social-welfare capitalism. More so than the in U.S., bureaucratic intervention in other antitrust regimes attempted to balance competition and public interest objectives.

Like the other major antitrust regimes, the EU's originated and evolved along a distinctive course. Possessing a general understanding of U. S. antitrust, the "father" of European economic integration, Jean Monnet, supported Harvard Law professor Robert Bowie's reconciliation of American antitrust principles with German principles governing abuse of dominance in the Treaty of Paris (1951) establishing the European Coal and Steel Community. According to Monnet, Bowie's accommodation of the American and German principles defined the European Community's competition provisions in the Treaty of Rome (1957), Articles 85 and 86, renumbered presently as 81 and 82. Monnet envisioned antitrust as essential to achieving market integration, thereby enabling Europe to better compete with the United States. Less known is Monnet's conviction regarding integration, that "[e]quality is absolutely necessary between peoples as between individuals. We lost the peace in 1919 because we built discrimination into it, and the will to dominate." In 2003, European economic consultant Matthias Pflanz echoed Monnet, stating that, whereas the US antitrust policy defined efficiency in terms of the "ultimate prices paid by consumers," a "focus of EU competition has been on behavior by companies which prevent others from competing on equal terms." Thus, the "creation of a 'level playing field' between actual and potential competitors (and . . . across different states) has been a primary objective of EU competition law."

Even so, U.S. and European officials assessed the policy goals of enforcement norms, differently. Permeating the Commission's enforcement regime was reliance upon bureaucratic discretion, which sought to balance the member states' economic integration with equal treatment of individuals and business. By the millennium the Commission's bureaucrats and the courts possessed over forty yeas of experience adapting the Rome Treaty's antitrust provisions to the Community's and then the Union's continued expansion. Commission officials and the courts sometimes measured this development by contrasting the differing policy goals of European and U.S. antitrust regimes. During the 1970s and 1980s the policy of Chicago economics defining "efficiency" principally in terms of prices paid by consumers came to prevail in the United States. Although a corrective to unequivocal reliance upon the Chicago microeconomic price theory emerged among U. S. antitrust authorities and the courts by the early 1990s, price competition benefiting consumers remained the principal measure of efficiency. In the EU, by contrast, economic theories must accommodate the fundamental goals of market integration and equal opportunity. As a result, the European Commission and the courts diverge from the Americans regarding such significant issues as vertical agreements "between companies at different levels in the economic chain," conglomerate mergers, and abuse of dominance, as in the *Philip Morris* and *Microsoft* cases.

II. Postwar U.S. Antitrust Approaches to Dominance in the Tobacco Industry

The *American Tobacco* (1946) and the *Philip Morris* (1987) cases suggest the contrasting U.S. and EC policy goals. Each case reflected a formative stage in the evolution of the two regimes' enforcement norms under, respectively, Section 2 of the Sherman Act, and Article 82 of the Rome Treaty. In *American Tobacco* the Supreme Court endorsed the key points from the *Alcoa* decision, handed down the year before by a special appeals court. One of the many cases Thurman Arnold initiated before World War II, the Tobacco case applied what was then Joan Robinson's and E. H. Chamberlin's new economic theories to section 2 monopolization doctrine, rejecting the classical economists' assumptions that monopoly and competition were exclusive, showing, instead, that both factors influenced the pricing practices of most firms. U. S. antitrust enforcement in Section 2 cases elaborated upon these theories until the Supreme Court began adopting Chicago theories in the 1970s. *Philip Morris* arose during the mid-1980s following a series of cases since the late 1960s expanding the Commission's authority under Article 82 to find abuse by dominant firms where complex financial arrangements might "neutralize" competition among firms operating across borders within the Common Market. At issue were the values of equal opportunity on a "level playing field" the Rome Treaty charged the Commission to maintain.

American Tobacco sets out detailed evidence of the industry's structure and performance from the 1920s through the Great Depression. American Tobacco, Liggett and Myers, and R.J. Reynolds were the principal makers of the three most popular cigarette brands, respectively, Lucky Strike, Chesterfield, and Camel. Since the 1920s the three big firms evolved into a standard oligopoly: of all American-made cigarettes these leaders produced 68% in 1939, which nonetheless declined from 90% in 1931. During this period the most produced by any one of the six small manufacturers, such as Philip Morris, was about 10%. The Big Three employed large national advertising budgets, a cost impeding entry from potential competitors. Regarding the domestic crop yield of flue-cured and burley tobacco, the three firms purchased, respectively, from 50% to 80% and 60% to 80%. A perishable crop, farmers sold each season's tobacco leaves at auction in the locales where the crop was grown. The government introduced evidence showing that the buyers for these firms would not purchase at auction unless representatives of all three were present, supporting the allegation that prior to an auction buyers received from each firm guidelines prescribing the express range within which prices should be bid. Inferentially, collusion among the firms ensured that prices were bid to an agreed limit, even where one firm may have had no intention to purchase a given batch of flue-cured or burley.

The government presented additional evidence, particularly regarding selling prices. On the production side the government further alleged that together, the big three began buying large amounts of lower-cost leaf when some makers introduced cheaper “10-cent” brands. The intent of this bulk buying was, the government contented, either to control the low-cost leaf the independent manufactures required to make the cheaper cigarettes or to force a price-increase of those same grades until the cheaper brands were no longer profitable. Concerning selling, before 1923 the three leading firms sold at competitive prices to cigarette-wholesale distributors; from 1923 to 1928 those same prices were “substantially identical” and between 1928 and 1939 they were “absolutely identical.” During the eleven years before 1939 there occurred seven price alterations; in each instance Reynolds initiated the change, followed by the other two big firms at the identical price. In addition, the government introduced strong evidence showing that on June 23, 1931, the year tobacco prices fell to a 25 year low and general production costs were depressed, Reynolds, American, and Liggett, without public notice or explanation, raised the list price, respectively, of Camel, Lucky Strike, and Chesterfield cigarettes from $6.40 to $6.85.

Upon a showing of this and other evidence, the Kentucky federal jury convicted the three firms of conspiracy to monopolize under section 2. Liggett gave testimony that although it considered the June 23 price increase to be mistaken at that point during the Depression, it followed the others’ lead in order to maintain comparable advertising costs, thereby preserving the Chesterfield brand’s “competitive advantage.” At the retail level, these higher prices resulted in smaller volume sales but greater profits—in 1932 the three leaders’ profits were $100 million, one of the three best years in the industry’s history. The total sales of cheaper cigarettes increased from 0.28% to 22.78% between June 1931 and November 1932. In response, the three leaders slashed list prices twice, until they were nearly 20% lower than the June 23 hike. By January 1934, the challenge of the cheap cigarettes having been met, the three firms' sale price per thousand was set at $6.10. Upon appeal, the Supreme Court analyzed this evidence, endorsing the *Alcoa* decision. Thus, Phillip Areeda and Louis Kaplow stated: "(1) Rivalry is a stimulant to industrial progress while unchallenged power deadens initiative. (2) Price fixing by competitors is like price setting by monopolists. (3) . . . .To achieve monopoly or control by combination would offend §2. (4) Progressive embracing of each new opportunity is exclusionary. (5) A violation of §2 requires power and intent but not specific intent because no monopolists monopolizes unconscious of what it is doing."

Some economists questioned whether the evidence in *American Tobacco* justified conviction. Thus, given the structure of oligopoly prevailing among cigarette manufacturers since the 1920s, the few leading firms knew well each other's pricing practices. It was predictable, therefore, that at the leaf tobacco auctions their bidding occurred in harmony; also, their ability to alter prices in line with the leader did not require formal agreement. In addition, the firms' changed conduct between 1923 and 1939 could have meant simply, as A. D. Neale's and D. G. Goyder text quipped, "That it takes time and experience for oligopolists to learn what the economists expect of them." As a result, in section 2 cases involving oligopoly such as *American Tobacco*, the government generally has to prove conspiracy through circumstantial evidence. Since the ascendancy of Chicago economics during the 1970s it became increasingly difficult to employ such evidence against oligopolies. Nevertheless, U. S. Assistant Attorney General

Robert Jackson initiated the *Alcoa* litigation, and his successor, Thurman Arnold, began the *American Tobacco* suit during the 1930s by applying then new law-and-economics thinking of Edward Mason. Moreover, the Justice Department eventually won both cases primarily because the federal judiciary adopted the use of these economic theories to justify massive new discovery techniques. Chicago learning triumphed because of those same techniques, though not until a long-term boom and bust cycle began in the 1970s.

III. The European Commission's Enforcement Norms in *Philip Morris*

The *Philip Morris* case arose amidst the long-term restructuring of the tobacco industry in Europe. Beginning in the 1960s the Commission increasingly confronted what J. J. Servan-Schreiber dubbed the "American Challenge," U. S. multinational corporations' growing investment throughout the Common Market. In a series of leading cases from 1974 to 1986—often involving U.S. multinationals—the Commission and the European Court expanded the abuse of dominance theory. During the1980s corporate restructuring investment and the growth of dominance theory converged in the *Philip Morris* case. The Rembrandt Group, a South-African multinational corporation established by that nation's "brilliant" entrepreneur, Dr. Anton Rupert, controlled as a wholly-owned subsidiary, Rothmans Tobacco Holdings Ltd. (RTH). RTH, in turn, owned the controlling share in Rothmans International p.l.c. (RI). Philip Morris, a U.S. multinational with "substantial interests in the cigarette industry," contracted with Rembrandt to purchase a fifty percent share of RTH. Thus, on the RTH board Rembrandt and Philip Morris possessed equal control. Through a partnership agreement Philip Morris and Rembrandt also co-operated to manage RI's operations. At the same time, within the European Community the cigarette market was oligopolistic, with Philip Morris' subsidiaries having from 12 to 14 percent, and RI subsidiaries' approximately 15 percent, market shares in competition with each other.

Thus, a result of the agreements between Rembrandt and Philip Morris, the latter held a large share in its competitor, RI, the biggest tobacco firm in the Common Market. R. J. Reynolds soon filed a complaint with the Commission alleging violations of Articles 81 and 82. While the Commission's and the Court's decisions regarding both provisions were significant, the following comments focus on the expanded dominance theory under Article 82. Reynolds alleged that in Belgium and the Netherlands Rembrandt's control of RI raised the question whether the Rembrandt -Philip Morris agreements "effectively neutraliz[ed]" competition between RI and Philip Morris "(since it was . . . unlikely that [Philip Morris] would compete with a company it controlled) . . . thereby strengthening Rembrandt's dominant position on a substantial part of the Common Market." In terms of policy, the question was whether Article 82 provided "room for balancing its anti-competitive effects against social and regional needs and allowing the latter to prevail in certain circumstances." Before long, British American Tobacco and Reemtsma, a local company, filed basically the same complaints with the Commission. In addition, Germany's antitrust authority, the Bundeskartellamt, forbade the whole transaction, though the European Court eventually overturned the action because it reached beyond German territory.

The Commission's and the Court's decisions in *Philip Morris* expanded dominance theory under Article 82. In answer to Reynolds' allegations, the Commission held that its approval of the agreement between Rembrandt and Philip Morris required the two firms to restructure the transaction so that Philip Morris and RI remained real competitors within the Benelux markets. Philip Morris would have no representation on RI's board and any data in RI's possession that might benefit Philip Morris could not be given to that firm. Alteration of these stipulations was subject to the Commission review. Thus, the Commission maintained ongoing over-sight of the tobacco industry within the Common Market. Upon review the Court held that the "main issue in these cases is whether and in what circumstances the acquisition of a minority shareholding in a competing company may constitute an infringement of Articles 85 and 86 of the Treaty." The Court upheld the Commission's enlarged construction of both Articles. In the wake of the *Philip Morris* decision one commentator suggested that the Commission and the Court fulfilled the policy potentialities initiated in the 1960s: "in this perspective, Article 85 could be applied to agreements preparatory to a takeover, and Article 86 to the takeover itself where that had the result of eliminating residual competition." Experts agreed that *Philip Morris* encouraged the Merger Regulation of 1990; yet the dominance theory of Article 82 applied also to monopoly, as the *Microsoft* case later demonstrated.

Philip Morris further contributed to the Commission's and the courts' strengthening of the concept of "decisive influence." Under Articles 81 and 82, as well as the Merger Regulation, the Commission and the Court enlarged the scope of what constituted "decisive influence" of single or joint firm control of ever more limited minority share holding and other routine corporate governance rights, beyond those at issue in *Philip Morris*. Especially, the "concept was expanded to apply Article 82 to very small minority shareholdings and limited rights acquired by a dominant firm in a competitor," even if, applying the Court of Justice's holding in *Philip Morris*, the investments were “totally passive . . . or, at a minimum, insufficient to enable the acquiring firm to exercise any influence over commercial policies of the entity in which the minority shareholding was held.” In conjunction with incorporating the “decisive influence” concept into dominance theory, the European Court of Justice’s analysis of the Merger Regulation’s revisions also established, in *Kali und Salz* (1998), a more rigorous microeconomic test of evidence in order to prove that long-term “coordination” of “price and output” fostered “oligopolistic dominance.” Thus, doctrines such as “decisive influence” and the economic analysis governing evidence and standards of proof influenced the Commission’s and the Court’s enforcement of “dominance” in relation to the fundamental principles of equal opportunity and integration within the Union.

IV. The U.S. and EU *Microsoft* Decisions

The U.S. and EU *Microsoft* decisions also reflected divergent core policy goals. Microsoft rebutted clear evidence of predatory and monopolistic conduct by asserting that its investment strategy of internal growth had permitted extraordinary technological innovation. Economic and legal experts disagreed as to whether the anticompetitive behavior should outweigh the efficiency gains. The U.S. federal trial court decided against Microsoft on the merits, resulting in damage awards and continued monitoring of the company’s inner operations. The U. S. Appeals Court, however, overturned the lower court’s decision to break up the company, preserving its control of the web browser. Although Microsoft applauded its victory, the practical outcome was ongoing U.S. state and private suits, as well as foreign litigation, drawing on the proven record of abusive conduct and the transparency of the company’s affairs that public monitoring ensured.

Applying an efficiency theory centered on consumer prices and continuing innovation, the modest remedy nonetheless enabled Microsoft to maintain its impressive technological lead, even as US antitrust officials encountered difficulties implementing their remedy. Enforcing stricter abuse of dominance doctrines, the European Commission imposed a stronger remedy requiring Microsoft to surrender its monopoly over the Media Player. In December 2004 The Court of First Instance upheld the Commission on most, though not all points.

The Commission's and the Court's *Microsoft* decisions enforced the Union's fundamental principles of integration and equal opportunity. The complainant was Sun Microsystems, the U.S. multinational computer company whose net loss in 2002-2003 was $ 2,378 million, which asserted that its loss was due to Microsoft's market conduct that had been proven illegal in U.S. courts. Even though the Commission's investigations found that Microsoft's abusive tactics had not abated, its decision for Sun was based on facts comporting with the "Commission's duty to uphold EU law in the European single market." The remedy focused on facts related to Microsoft's abusive "tying" of Windows and Windows Media Player, which were contrary to the EU's "market integration" and proscription of "dominance." The Commission ordered Microsoft "'to *disclose complete and accurate specifications for the protocols'* [emphasis in original] necessary for its competitors' server products to be able to 'talk' on an equal footing Windows PCs, and hence compete on a level playing-field. It must also offer a version of Windows for clients' PCs which does not include Windows Media Player." The Commission also fined Microsoft 497 euros "for abusing its market power in the EU." The Court's decision essentially upholding the Commission was consisted with the evolution of EU dominance theory under Article 82 applied to integration and equal opportunity, including *Philip Morris*, the "decisive influence" doctrine, and the microeconomic analysis of evidence.

The Commission evaluated the differences between the US and its own *Microsoft* decision. The Commission rebutted experts' presumptions based on U.S. efficiency theories that the decision "protected competitors" rather than promoting the principle of competition identified with consumer prices. By contrast, the Commission asserted, the decision "creates the environment where consumers can benefit and where innovation can flourish." In particular, the decision followed closely the European Court precedents governing interoperability and tying, which, in turn, complied with the principles of market integration and abuse of dominance. In reply to Microsoft's and the critics' arguments that antitrust was ill suited to the "fast moving" innovation demanded in the "hi-tech" global economy, the Commission insisted upon following an economic analysis which, given the "specific characteristics of the market question (e.g. network effects, applications barrier to entry) could mean there is in fact an increased likelihood of positions of entrenched market power compared to certain 'traditional industries.'" Thus, the emphasis on constituting a market "environment" affirmed EU law's multiple-value outcomes including integration and equal opportunity, as well as consumer welfare.

Conclusion

The divergence between U.S. and EU antitrust enforcement regimes in the *Microsoft* case reflected long-term changes in the global political economy. In the U.S., until the 1970s, Chicago economic theories were on the defensive against Edward Mason's and others' law and economics theories Thurman Arnold's activist antitrust regime began implementing in the late-1930s. The Supreme Court's *Alcoa* and *American Tobacco* decisions embraced those theories, including abuse of dominance, to accommodate the American "liberal consensus" prevailing during the quarter-century of global economic growth following World War II. During that same period, the European Commission, like regulatory bureaucracies in Japan, Australia, and elsewhere adopted the American idea of antitrust they had previously rejected, selectively incorporating U.S. antitrust law and theory into their indigenous business-government relations. The *Philips Morris* case suggested how the EU antitrust regime refashioned dominance theory under Article 82 to shape the restructuring of the tobacco industry in accord with the Rome Treaty's fundamental values of market integration and equal opportunity, particularly as more new member states joined the Union from the 1970s on. By the *Microsoft* case the EU antitrust regime had adjusted its antitrust dominance theory to the demands of new member states amidst a chaotic boom and bust economic cycle, as well as the end of the Cold War; during the same period U.S. antitrust enforced narrower efficiency theories.