



Business and Industry Advisory Committee to the **OECD**

Comité Consultatif Economique et Industriel Auprès de l' **OCDE**

Summary of Discussion Points

Presented by the Business and Industry Advisory Committee (BIAC) to the OECD at the OECD Competition Committee Roundtable on Competition on the Merits*

June 1, 2005

1. BIAC appreciates the opportunity to submit the perspective of the business community on the issue of competition on the merits.
2. The objectives of any rational business enterprise are to expand its position in the marketplace to the greatest extent possible and to maximize the return on investment of its stakeholders. These objectives drive companies to out-perform their peers through superior innovation, efficiency and industry. Companies that are the most successful at achieving one or more of these metrics are the most likely to become dominant firms. Often, the firms achieving these objectives employ the most aggressive competitive means possible, combining their skill in innovation and production with savvy and creativity in marketing, distribution and customer relationships that help to maximize the value of their goods to consumers. In protecting competition through the regulation of dominant or monopolistic firms, enforcement agencies must engage in the difficult task of distinguishing between firms that have achieved or maintained a dominant position through the accomplishment of these desirable metrics, and those that have done so through means that retard, rather than advance, the competitive process. The challenge is particularly great when firms employ means that can have both pro-competitive and anti-competitive aspects.
3. A primary consideration in preserving competition on the merits is ensuring that the enforcement process itself does not undermine benefits to consumers. Thus, in order for a practice by a dominant firm, or would-be dominant firm, to qualify for enforcement action, it should cause harm to the competitive process itself. For this reason, no meaningful competition standard can be premised on the concept of harm to or elimination of a competitor, even to the point of eliminating all competitors from a market. It is generally accepted that in a free-market economy competition enforcement agencies should not intentionally act to manipulate a market that is functioning competitively by seeking to promote an industry champion or to hinder a

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disfavored company. If this principal is accepted, then agencies should not seek to disrupt a competitive process which in some cases legitimately may lead to single firm dominance or exclusivity. Enforcement premised on maintaining competitors, therefore, can no more be justified than enforcement designed to manipulate a market. “Results-oriented” enforcement should be rejected.

4. The appropriate model for enforcement should focus on preserving the competitive process by distinguishing between those practices that allow the market to play-out according to the true economic performance of the competitors and those which instead prevent firms in a market from meeting with their true economic fate. It should be recognized that this is a very fact-intensive consideration. There are few, if any, unilateral practices that can be condemned as anticompetitive without consideration of their actual effect on competition. Unlike some horizontal restraints, which long experience and empirical study have shown can lead to competitive harm in virtually all cases – reducing the risk of false positives to a de minimus level – unilateral practices can not so neatly be pigeon-holed. Exclusive distributorships, for instance, most often benefit competition but can, in some circumstances, unduly foreclose competition. Even practices that would be facially suspect – for example the manipulation of government regulatory structures as identified in the note by the United States, may be justified in some circumstances and do not admit the application of *per se* rules. In short, unilateral practices do not lend themselves to bright-line rules or guidelines. Rather, there are certain basic economic principles that should uniformly be applied by regulatory agencies in the consideration of such practices.

Focus on Establishment or Maintenance of Market Power, Not Structural Dominance

5. Consideration of the effects of a practice should focus on the maintenance or enrichment of market power, not mere structural dominance. For example, remedial relief is not warranted where smaller competitors have difficulty competing in a market simply because a dominant entity is more efficient, or has achieved significant economies of scale or other advantages. As stated by the U.S. Supreme Court, “It is axiomatic that the antitrust laws were passed for “the protection of competition, not competitors.”¹
6. Competition laws frequently look in the first level of analysis to a party’s market share as an indication of market power or dominance. There is, however, no specific market share threshold that reliably establishes that a firm has market power. In the U.S. and Canada, a *prima facie* determination of market power may be made on the basis of market share in a relevant market.² For example, in determining whether a supplier has

¹ *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 224 (1993).

² The Canadian Competition Tribunal has provided the following framework for analyzing whether the alleged dominant entity has the requisite control:

- examine whether an entity has the ability to maintain prices above competitive levels for a considerable period;
- determine the entity’s market share;
 - under 25% - unlikely to find dominance, but consider any evidence of an increasing trend;

market power, the Competition Tribunal has indicated in addition to a firm's market share, it will also consider factors such as the number of competitors and their respective market shares, excess capacity in the market, ease of entry, profits, dissatisfied customers and pricing policies will also be taken into account. In assessing barriers to entry, relevant factors include observed entry and exit, sunk costs, incumbent advantages, length of time to enter, process patents/technological barriers, and regulatory approvals required.

7. In the United States, market share alone is not enough to prove dominance. While a prima facie showing may be made in cases involving high market shares, there is no "bright line" test that applies.³ Judicial guidance suggests certain screening levels, specifically: (i) a market share above 70 percent will likely establish prima facie monopoly power; (ii) a share between 50 and 70 percent will create a possibility of establishing monopoly power; and, (iii) a share below 50 percent are unlikely to result in a finding of monopoly power.⁴ Importantly, however, factors such as barriers to entry, excess capacity, market dynamics, and effectiveness of competitors in the market can rebut this presumption, regardless of a firm's market share.⁵ Ease of entry,

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- under 50% - no prima facie finding of dominance;
 - 100% - prima facie finding of dominance absent evidence that there are no barriers to entry;
 - assess market structure - the smaller the number of competitors and the tighter the capacity, the more likely a given entity will be found to have market power;
 - evaluate entry barriers – the higher the entry barriers, the more likely an entity will be found to have market power; and
 - consider the profits of the dominant entity - if profits are above levels expected in a competitive market, a company likely has market power.

³ *United States v. Aluminium Co. of America*, 148 F.2d 416, 430 (2d Cir. 1945) [hereinafter *Alcoa*] (90 percent market share is sufficient to establish a prima facie determination of market power, doubtful whether sixty or sixty-four percent would be enough and thirty-three per cent would certainly not be enough).

⁴ See ABA Section of Antitrust Law, *Antitrust Law Developments* 234-37 (5th ed. 2002) citing *Grinnell Corp.*, (87% of the relevant market left no doubt of the existence of market power); *du Pont*, (75% of a market, had it been defined as the relevant one, would have sufficed); *Standard Oil Co. of N.J. v. United States*, 221 U.S. 1, 75 (1911) (90% of the business of producing shipping, refining, and selling petroleum and its products constituted monopoly power); *Town of Concord v. Boston Edison Co.*, 915 F.2d 17, 43 (1st Cir. 1990) (70-90% indicative of monopoly power); *Reazin v. Blue Cross and Blue Shield*, 899 F.2d 951, 967 (9th Cir. 1990) (noted in dicta that courts generally require a minimum market share between 70% and 80%); *Fineman v. Armstrong World Industries Inc.*, 980 F.2d 171, 201 (3d Cir. 1992) (55% share, absent other relevant factors, is insufficient); *Domed Stadium Hotel, Inc. v. Holiday Inns, Inc.*, 732 F.2d 480, 489 (5th Cir. 1984) ("Supreme Court cases, as well as cases from this Court, suggest that, absent special circumstances, a defendant must have a market share of at least fifty percent before he can be guilty of monopolization."); *The Movie 1 & 2 v. United Artists Communications*, 909 F.2d 1245, 1254 (9th Cir. 1990) (noting that market share as low as 45-70% might constitute monopoly power); *Langerdorfer v. S.E. Johnson*, 917 F.2d 1413, 1431 (6th Cir. 1990) (existence of market share ranging from 40-30% is insufficient on the facts of the case to constitute monopoly power); *Barry v. Blue Cross of Cal.*, 805 F.2d 866, 874 (9th Cir. 1986) (16% "is far below what we would require for a monopoly").

⁵ In *Microsoft*, the District Court made a finding of fact that Windows accounted for a greater than 95% share of the relevant market. Microsoft did not challenge this finding before the Court of Appeal, but claimed that even a predominant market share did not by itself indicate monopoly power. The Court of Appeal agreed that, while the existence of monopoly power may ordinarily be inferred from a predominant share of the relevant market, looking to current market share alone could be misleading. *Massachusetts v. Microsoft Corp.*, 362 U.S. App. D.C. 152 (D.C. Cir. 2004).

in particular, provides an example of a fact that would undermine the ability of a firm to establish or enhance – or even to exercise – market power. This determination, however, can only be made through full consideration of the conditions of entry and the current constraints placed on market participants by the threat of entry. Thus, while market structure can provide an indication of the risk that monopolisation or enhancement of a dominant position is theoretically possible, it cannot be used as the sole basis for drawing such a conclusion.

8. Moreover, the entry issue provides just one example of the difficulty in establishing bright-line policies for the application of competition laws to the area of dominance or monopolization. While it may be possible to develop screening mechanisms to determine “safe harbors” (e.g., firms with a low market share may presumptively be able to engage in certain unilateral conduct without undue risk of creating market power), it is a dubious proposition to conclude that certain acts that occur within a given market structure necessarily harm competition.

Avoid Attacking Practices With Ambiguous or Procompetitive Economic Effects in Order to Preserve Efficiency-Enhancing Conduct

9. The challenge for businesses and competition law authorities is distinguishing anticompetitive conduct from superior competitive performance and avoiding the deterrence of legitimate competitive conduct. From this perspective, enforcers should consider that attacking practices that may have anticompetitive consequences only in certain narrow applications, may discourage those same practices in situations where they may provide significant economic benefits.
10. Competition laws and jurisprudence often highlight practices that may harm competition. Usually, in the area of dominance or monopolisation these practices are provided as non-exclusive examples.⁶ Recognizing that even dominant firms must be allowed to compete aggressively, most laws require an affirmative demonstration that the practices result in demonstrable economic harm.
11. In practice, it is often difficult in abuse of dominance cases to distinguish between when an act is anticompetitive as opposed to when it is a “sign of healthy or at least normal commercial competition.”⁷ A particularly high risk is present in cases involving discounting, rebates, loyalty programs, predatory pricing or other practices that facilitate lower prices to consumers. Even if – and there is significant dispute in the economic literature on the point – such discounting practices might lead to a serious risk of anticompetitive effects in some cases, the anticompetitive effect of challenging such practices in a market must carefully be weighed. As enforcement agencies desire, prudent firms base their marketplace activities on perceived

⁶ Neither Canada nor the United States has a definitive list of activities that constitute anticompetitive conduct. However, Section 78 of the Canadian Competition Act does provide a non-exhaustive list of anticompetitive acts. Similarly, the EC Treaty also includes a non-exhaustive list of offences.

⁷ *Director of Investigation and Research v. Laidlaw Waste Systems Ltd.*, Case No. CT-1991-002, The Competition Tribunal (1992) at 78.

enforcement standards. Thus, there is a significant probability that an enforcement action against a particular practice will lead to a decline in that practice across a spectrum of industry.

12. Recognizing, as we discuss above, that a single practice may have quite different competitive effects in various markets, there is a risk the practice will be discontinued even in markets in which the practice would benefit competition. For example, one result of the Third Circuit decision in *LePage's Inc. v. 3M* is that many firms having one arguably dominant product discontinued their multi-product discounts, despite the fact that these often reflected real economic savings for the manufacturer.⁸ This risk is compounded by the indisputable fact that there is significant dispute in the regulatory, economic and academic community about the competitive effects of discounting practices. Thus, enforcement agencies must weigh the possible economic consequences of challenging a discounting practice that provides at least short term consumer benefit against the impact that the discontinuation of that practice may have not only in the affected market but in other markets as well and should seek to avoid enforcement against practices with ambiguous or equivocal effects.

Facilitate Competition Not Competitors

13. The primary purpose of competition law and enforcement is to enhance consumer welfare by facilitating the operation of competitive markets, not to aid particular competitors. As noted above, enforcement agencies acting with the purpose of aiding particular competitors interferes with the effective functioning of competitive market forces.
14. Under Canadian law, for example, in determining whether a practice has had or is having the requisite effect on competition the Competition Act requires the Tribunal to consider whether the practice is a result of superior competitive performance. The Canadian Competition Tribunal has remarked that:

It would not be in the public interest to prevent or hamper even dominant firms in an effort to compete on the merits. Competition, even "tough" competition, is not to be enjoined by the Tribunal but rather only anti-competitive conduct.⁹

A core principal of U.S. competition law rests on the premise that “the successful competitor, having been urged to compete, must not be turned upon when he wins.”¹⁰ Recently, the U.S. Supreme Court also suggested that the consequence of monopoly pricing is to induce investment, risk-taking, innovation and economic growth.¹¹

⁸ *LePage's Inc. v. 3M*, 324 F.3d 141 (3d Cir. 2003), *cert. denied*, 124 S. Ct. 2932; 159 L. Ed. 2d 835 (2004).

⁹ *Director of Investigation and Research v. Tele-Direct (Publications) Inc.*, Case No. CT-1994-003, The Competition Tribunal (1997) at 258 [hereinafter *Tele-Direct*].

¹⁰ *Alcoa* at 430.

¹¹ *Verizon Communications Inc., v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004).

15. The Canadian Competition Tribunal has acknowledged, moreover, that decisions restricting competitive actions on the grounds that a competitor feels a dominant firm's response has been "overwhelmingly intense" instead may chill competition:

Decisions by the [Competition] Tribunal restricting competitive action on the grounds that the action is of overwhelming intensity would send a chilling message about competition that is, in our view, not consistent with the purpose of the [Competition] Act, as set forth in section 1.1. We are concerned that, in the absence of some objective test, firms can have no idea what constitutes a "competitive" versus an "anticompetitive" response when responses like those used by Tele-Direct in this case are involved (*e.g.*, price freezing or cutting, incentives, product improvements, increased advertising).¹²

16. In this connection, a rule fashioned upon a "proportionality" test, as identified in the note of the EC is particularly hazardous to the efficient operation and advancement of a market. Restricting a dominant firms' ability to compete freely on the merits deprives the relevant market of the full benefits of the efficiency that should be made available. The only explanation for such an approach is that consumers should be denied the benefits of competition now because, if the dominant firm were actually allowed to operate based on its economic efficiency, it *necessarily* would be able to eliminate competition to the point that it could and would charge supracompetitive prices at some point in the future which more than offset the benefits now being denied to the market. This approach, however, presupposes incredible foresight by a competition authority, subjugating – at a minimum – the concepts of innovation, actual or potential entry, and repositioning. Obviously, the confluence of circumstances that circumstances necessary to allow a confident decision to this effect is doubtful. Rather, competitors should not be protected for the sake of maintaining competitors. Consumers should be permitted to derive the full measure of economic efficiency from the market, competitors should be forced to produce their full measure of ingenuity and industry and market forces should be allowed to determine the market participants in the long run.

Competition Law Should Not Trample Intellectual Property Rights That Promote Innovation

17. Real efficiencies should give rise to consumer benefits¹³, for example: (i) lower product prices through economies of scale and synergies; and (ii) innovation and technological advances that lead to the development of new products or more efficient

¹² *Tele-Direct* at 291.

¹³ See, *e.g.*, "Antitrust and Competitiveness: Efficiencies, Failing Firms, and the World Arena," Statement by Eleanor M. Fox before the Global And Innovation-Based Competition Hearings Before The Federal Trade Commission (December 13, 1994). See remarks of Deborah Platt Majoras when she was the Deputy Assistant Attorney General, Antitrust Division, U.S. Department of Justice, "GE-Honeywell: The U.S. Decision", before the Antitrust Law Section State Bar of Georgia, November 29, 2001. See also *Draft Commentaries to Possible Elements for Articles of a Model Law or Laws*, United Nations Conference on Trade and Development, prepared as a background document by the UNCTAD Secretariat, 21 August 1995.

production methods. The protections offered by intellectual property laws provide incentives to innovation, leading to such dynamic efficiency gains.¹⁴ The requirement that IPRs be protected in order to provide incentives for the development of valuable works, has been accorded global recognition in treaties such as the World Intellectual Property Organisation (WIPO) treaties and the WTO treaty concerning Trade-Related Aspects of Intellectual Property (TRIPs). As a result, it is important that competition laws be designed and implemented in a manner that avoids overriding these valuable protections, and the objectives of competition law must be advanced in a manner consistent with the exclusive rights afforded to owners of intellectual property, and the incentives for innovation that such rights confer.

18. Traditional competition law, particularly in its enforcement, cannot foreshadow the pace of invention. A focus on short-term allocative efficiency goals (versus dynamic efficiencies) may result in enforcement activities which could adversely affect the incentives to innovate and the long-term benefits to society that flow from the research and development activities which are fostered by the protection of IPRs. This principle is best reflected by balancing the exclusive rights afforded to the owner of IPRs and the objectives of competition law:

Antitrust law promotes market structures that encourage initial innovation with a competitive market ‘stick’ - that is, firms that fail to innovate will get left behind. Intellectual property law encourages initial innovation with the ‘carrot’ of limited exclusivity, and the profits that flow therefrom. Antitrust law enables follow-on innovation by protecting competitive opportunities beyond the scope of the exclusive intellectual property right. Intellectual property law enables follow-on innovation by requiring public disclosure of the initial innovation (at least in the patent context) and affording follow-on innovators rights of ‘fair use’ and freedom from intellectual property ‘misuse’. The basic principle that mediates the tensions ... is that intellectual property rights provide legal monopoly power, but only within the defined, limited scope of the right.¹⁵

19. Canadian law implicitly recognises that traditional competition laws and IPRs are designed for the same purpose – to reward success on the merits of skill and hard work. For example, section 79(5) includes an intellectual property exception to the abuse of dominance provisions, which provides that an act engaged in pursuant only to the exercise of any right or enjoyment of any interest derived under the *Copyright Act*, *Industrial Design Act*, *Integrated Circuit Topography Act*, *Patent Act*, *Trade-marks*

¹⁴ See Brian Jackson (2003), “Innovation and Intellectual Property: the Case of Genome Patenting” 22 *Journal of Policy Analysis and Management*, and John Barton (1999), “Intellectual Property Rights and Innovation” in Nicholas Imparato, ed. *Capital for out Time: The Economic, Legal, and Management Challenges of Capital* (Stanford: Hoover Institution Press) at 123.

¹⁵ Debra A. Valentine, former General Counsel, U.S. FTC: "Abuse Of Dominance In Relation To Intellectual Property: U.S. Perspectives And The Intel Cases", Remarks before The Israel International Antitrust Conference, Tel Aviv, Israel, November 15, 1999.

Act or any other Act of Parliament pertaining to intellectual or industrial property is not an anti-competitive act.

20. An application of competition law that forsakes the risk-reward structure embodied in the balance that currently exists threatens to reduce the level of innovation that will result. As in the case of enforcement against discount practices, the mandatory licensing of intellectual property as a remedy for perceived abuse of dominance in one case carries substantial negative “spillover effect.” It thereby places in jeopardy the expected rewards of every innovation worthy of IPR protection. Predictably, this upsets the status quo in two ways, both of which have significant negative consequences. First, it will reduce the incentive to invest in innovation. Second, it will reduce the incentive to disclose (e.g., through patent applications) those innovations that do occur. Derivative of the second point, it will reduce the occurrence of follow-on innovation (which is already reduced by the first point).