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The Millenium Approaches: Rethinking Article 85 and the Problems and Challenges in the Design and Enforcement of the EC Competition Rules

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Mario Siragusa

Abstract

This Essay contributes to the discussion of competition law reforms, both at the level of the European institutions and within the Member States of the European Union, by considering the scope for altering the economic evaluation performed in the context of Article 85 of the EC Treaty. The Essay first describes, and accounts for, the European Commission's current interpretation of Article 85. The Essay then presents a number of criticisms of that interpretation and assesses possible changes to the present system of European competition enforcement. Finally, examples are given from the case law of the Court of Justice and the Court of First Instance where a rule of reason approach has been applied. This Essay concludes that the introduction of a rule of reason is not only desirable but practicable within the framework of European competition rules as they already exist.

THE MILLENNIUM APPROACHES: RETHINKING ARTICLE 85 AND THE PROBLEMS AND CHALLENGES IN THE DESIGN AND ENFORCEMENT OF THE EC COMPETITION RULES

Mario Siragusa*

INTRODUCTION

There has been much recent discussion of competition law reforms, both at the level of the European institutions and within the Member States of the European Union.¹ The discussion has centered upon the necessity and potential for refocusing, rather than renewing, a set of rules which has been in place for approximately forty years, and which it is felt should adapt to the changed political and economic situation in Europe.²

This Essay contributes to that discussion by considering the

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1. See, e.g., COMMISSION OF THE EUROPEAN COMMUNITIES XXVIth REPORT ON COMPETITION POLICY 1996, at 20, ¶ 11 (1997); J. Faull, *The Future of Competition Law in the EUM*, COMPETITION WORKSHOP, EUROPEAN UNIVERSITY INSTITUTE, FLORENCE (1997); Patrick Massey, *Reform of EC Competition Law - Substance, Procedure and Institutions*, in 1996 FORDHAM CORP. L. INST. (Barry Hawk ed., 1997); Roger Van den Bergh, *Modern Industrial Organisation Versus European Competition Law*, EUR. COMP. L. REV. 75, 81 (1996); M. Waelbroeck, *Do Not Give Up All Hope! Ye Who Enter*, COMPETITION WORKSHOP, EUROPEAN UNIVERSITY INSTITUTE, FLORENCE (1997); Donald L. Holley, *EEC Competition Practice: A Thirty-Year Retrospective*, in 1992 FORDHAM CORP. L. INST. 669, 690-91 (Barry Hawk ed., 1993); Barry E. Hawk, *System Failure: Vertical Restraints and EC Competition Law*, 32 COMMON MKT. L. REV. 973, 987-88 (1995); J. Venit, *Economic Analysis, "Quick Looks" and Article 85: A Way Forward?*, COMPETITION WORKSHOP, EUROPEAN UNIVERSITY INSTITUTE, FLORENCE (1997); Pietro Manzini, *La Rule of Reason nel Diritto Comunitario della Concorrenza: Una Analisi Giuridico-Economica* [The Rule of Reason in EC Competition Law: A Law and Economics Analysis], 31 RIV. DIR. EUROP. 859, 877-92 (1991); Helmuth R.B. Schröter, *Antitrust Analysis Under Article 85(1) and (3)*, in 1987 FORDHAM CORP. L. INST. 645, 691-92 (Barry Hawk ed., 1988); Alexander Schaub, *Objectives and Goals of European Competition Policy*, COMPETITION WORKSHOP, EUROPEAN UNIVERSITY INSTITUTE, FLORENCE (1997).

2. The Commission itself has identified the three main areas in which modernization of competition policy is required. These areas are (i) a more economic analytical approach in the appraisal of cases; (ii) improved cooperation with domestic competition authorities with a view to respecting the principle of subsidiarity; and (iii) a modernization of instruments so as to render procedures swifter and more transparent. See

scope for altering the economic evaluation performed in the context of Article 85 of the EC Treaty. The Essay first describes, and briefly accounts for, the European Commission's current interpretation of Article 85. The Essay then presents a number of criticisms of that interpretation and assesses possible changes to the present system of European competition enforcement.

The principal proposal for change concerns the introduction of a "rule of reason" approach. Under this approach, potentially restrictive agreements would undergo a full economic analysis under Article 85(1), with both pro- and anti-competitive aspects being considered. At present, only anti-competitive aspects are identified under Article 85(1). The impact of pro-competitive aspects of agreements is assessed only in the context of Article 85(3). More importantly, because the Commission has exclusive jurisdiction to exempt under Article 85(3), the Commission alone, at present, is perceived to be empowered to pass judgment on the overall competitive impact of agreements.

The new approach would lead to a substantial reduction in the number of notifications to the Commission. This is because agreements that are not seriously restrictive of competition, but that do contain anti-competitive elements, would no longer necessarily be subject to notification. In this connection, several improvements to competition procedure are also suggested.

Finally, by way of contrast to the Commission's approach described at the beginning of this Essay, examples are given from the case law of the Court of Justice and the Court of First Instance where a rule of reason approach has been applied. This Essay concludes that the introduction of a rule of reason is not only desirable but practicable within the framework of European competition rules as they already exist.

I. CURRENT INTERPRETATION OF ARTICLE 85

A. *The Commission's Approach*

Procedurally, only the Commission can apply Article 85(3) of the EC Treaty, whereas both the Commission and national courts and/or authorities can apply Article 85(1).³ Substan-

COMMISSION OF THE EUROPEAN COMMUNITIES XXVITH REPORT ON COMPETITION POLICY 1996, at 20, ¶ 11 (1997).

3. Article 9(1) of Regulation 17/62, implementing Article 85, provides that only the Commission can grant exemptions: "Subject to review of its decision by the Court

tively, a fundamental choice was made as to the application of Article 85 early in the development of European competition law, and, in particular, as to the respective roles of paragraphs (1) and (3) of that provision. The Commission decided that, under Article 85(1), any restriction of the commercial freedom of one or more of the parties to an agreement would amount to a restriction of competition. It therefore decided that under Article 85(1) there would be no examination of the overall economic impact of an agreement, nor of whether any competitive benefits provided by the agreement would be possible without the restriction. The practical consequence of this substantive interpretation is that the Commission's initial finding has almost invariably been that agreements containing any restrictive element are anti-competitive. Thus Article 85(1) has been interpreted in a "literal, almost mathematical, manner,"⁴ despite recognition by the Commission that much conduct caught by the broad sweep of the provision, as so interpreted, is in fact acceptable.⁵

Only in the context of Article 85(3) has the Commission usually tried to balance pro- and anti-competitive effects, and to make an assessment of the overall competitive impact of the agreement on the freedom of undertakings to determine their commercial behavior and/or the possible merits of the agreement in furthering other Treaty objectives. The Commission does not deny that agreements may be commendable in their effect and intentions. However, it insists that the analysis should first determine that restrictions of competition exist and then approve them.

Early and important evidence of the Commission's tendencies is provided in *Société Technique Minière*,⁶ where it set out its

of Justice, the Commission shall have sole power to declare Article 85(1) inapplicable pursuant to Article 85(3) of the Treaty." Commission Regulation No. 17/62, art. 9(1), O.J. L 204/62, at 87 (1962). By contrast, Article 85(1) "create[s] direct rights in respect of the individuals concerned which the national court must safeguard." *Belgische Radio en Televisie v. SV Sabam*, Case 127/73, [1974] E.C.R. 51, [1974] 2 C.M.L.R. 238.

4. Ian Forrester & Christopher Norall, *The Laicization of Community Law: Self-Help and the Rule of Reason: How Competition Law Is and Could Be Applied*, COMMON MKT. L. REV. 11, 12 (1984).

5. See Alberto Pera & Mario Todino, *Enforcement of EC Competition Rules: Need for a Reform?*, in (1996) FORDHAM CORP. L. INST., 125 (Barry Hawk ed., 1997).

6. *Societe Technique Miniere v. Maschinenbau*, Case 56/65, [1966] E.C.R. 235, [1966] C.M.L.R. 357.

basic view of what amounts to a restriction. Before the Court of Justice, the Commission argued that a restriction on competition arises when the freedom of action of the contracting parties is limited, and when the position of a third party is adversely affected.⁷ This concept has been adhered to by the Commission ever since.⁸ It has been stated that “clearly the Commission does not go far in the interpretation of the phrase ‘restriction’.”⁹ Indeed, one can go so far as to affirm that the Commission’s current approach to Article 85 is “formalistic and restrictive,”¹⁰ its main consequence being that all potentially anti-competitive agreements require notification.¹¹

An example of the Commission’s approach may be found in the *Re Davidson Rubber* decision.¹² In that case, Davidson had granted three separate licenses to manufacturers in three Member States. Davidson agreed with each licensee to grant no other license in the licensee’s territory without its consent, and each licensee agreed not to sell outside its territory. The Commission initially found that the agreement was caught by Article 85(1), only to exempt it subsequently under Article 85(3), on the

7. *Id.* at 240, [1966] C.M.L.R. at 357.

8. An interesting formulation appears in the Commission’s argument to the Court of Justice in *Consten and Grundig v. Commission*, Joined Cases 56 & 58/64, [1966] E.C.R. 299,377, [1966] C.M.L.R. 418.

The decisive criterion for the coming into force of the prohibition mentioned in Article 85(1) . . . consists of the finding that the agreement interferes with the freedom of action of one of the parties or with the position of third parties on the market not only in a theoretical but also in a perceptible manner.

Consten & Grundig, [1966] E.C.R. at 377, [1966] C.M.L.R. at 418. Ian Forrester observes that

this cannot mean exactly what it says, since any agreement by its very nature limits the freedom of action of the parties. . . . It is clear that the Commission intended to cast the net of Article 85(1) very broadly, adding the rider about perceptibility or “appreciability” to exclude *de minimis* situations.

Forrester & Norall, *supra* note 4, at 11. The Commission also stated, in relation to an exclusive copyright license, that “these are typical restrictions on freedom of economic action which generally fall within the scope of Article 85 (1).” *Coditel SA, Compagnie Générale pour la Diffusion de la Télévision v. Ciné-Vog Films SA*, Case 262/81, [1982] E.C.R. 3381, 3389, [1983] 1 C.M.L.R. 49.

9. Christopher Bright, *Deregulation of EC Competition Policy: Rethinking Article 85(1)*, in 1994 FORDHAM CORP. L. INST. 505, 514 (Barry Hawk ed., 1995).

10. Pera & Todino, *supra* note 5, at 125.

11. In 1996, the Commission received 209 notifications pursuant to Article 85, but only 21 formal decisions were adopted. COMMISSION OF THE EUROPEAN COMMUNITIES XXVITH REPORT ON COMPETITION POLICY 1996, at 50, ¶ 110 (1997).

12. Commission Decision No. 72/328/EEC, O.J. L 143/39 (1972).

grounds that without the protection of exclusive manufacturer licenses, the Davidson technology would not have become available in Europe.

This approach was applied by the Commission until the Court's decision in the *Nungesser* case.¹³ In *Nungesser*, the Court of Justice ruled that "open" exclusive licensing agreements, where the licensor undertakes not to exploit the licensed invention in the licensed territory himself, and not to grant further licences there, are not by themselves incompatible with Article 85(1), provided that they concern the introduction and protection of new technology in the licensed territory. Through this approach, the Court acknowledged the importance of the research undertaken, and risk involved, in manufacturing and marketing a new product, and made it clear that it did not consider open exclusive licensing agreements which fulfilled these conditions to fall within the scope of Article 85(1).

Two years after *Nungesser*, the Commission adopted the Patent Licence Regulation.¹⁴ Article 1 of the Regulation provides that all open exclusive licensing agreements are exempted. This has blurred the distinction between open exclusive licenses related to the introduction and protection of a new technology, that were deemed to fall outside the scope of Article 85(1), and other open exclusive licenses which were not. This distinction is recognized by the Commission in the Preamble to the Regulation.¹⁵

13. *L.C. Nungesser KG & Kurt Eisele v. Commission of the European Communities*, Case 258/78, [1982] E.C.R. 2015, [1983] 1 C.M.L.R. 278.

14. Commission Regulation No. 2349/84, O.J. L 219/15 (1984), amended by Commission Regulation No.151/93, O.J. L 21/8 (1993).

15. Paragraph 11 of the Preamble states that

Exclusive licensing agreements, i.e. agreements in which the licensor undertakes not to exploit the 'licensed invention', i.e. the licensed patented invention and any know-how communicated to the licensee, in the licensed territory himself and not to grant further licences there, are not in themselves incompatible with Article 85(1) where they are concerned with the introduction and protection of a new technology in the licensed territory, by reason of the scale of the research which has been undertaken and of the risk that is involved in manufacturing and marketing a product which is unfamiliar to users in the licensed territory at the time the agreement is made. This may also be the case where the agreements are concerned with the introduction and protection of a new process for manufacturing a product which is already known. In so far as in other cases agreements of this kind may fall within the scope of Article 85(1) it is useful for the purposes of legal certainty to include them in Article 1, in order that they may also benefit from the exemption. However,

B. *Reasons for the Current Approach*

The current approach was adopted for three main reasons. First, in the early stages of European integration, Member States, apart from France and Germany, were unfamiliar with competition rules. Interpreting Article 85 in a formalistic manner meant that the Commission could exercise control over the interpretation and development of those rules. Second, it was considered easier to achieve the completion of the Single Market by deeming all agreements between undertakings to be *prima facie* anti-competitive, than by removing the necessity of Commission notification in those cases where pro-competitive benefits outweighed anti-competitive effects. This was most important in the context of vertical agreements that have traditionally been considered capable of segmenting markets into national and regional zones. Third, the approach was justified by the initial difficulty, due again to unfamiliarity with competition rules, of making a full market analysis in each case. None of these reasons now apply.

1. Initial Unfamiliarity with Competition Rules

When the EC Treaty came into force, there was relatively little experience of competition law enforcement in Europe. France and Germany were the only Member States with laws relating to competition and their laws were very different. Germany was concerned mainly about horizontal agreements, whereas France treated vertical restrictions more severely than horizontal ones. The usefulness of a wide competence in these circumstances was clear. Formalism represented a tool to ensure centralized control of the enforcement of EC competition rules by the Commission.¹⁶ The Commission hoped to ensure the uniform application of the competition rules through its exclusive power to exempt. The Commission could use this power as the basis to review, assess, and identify the real issues of concern. The low jurisdictional threshold of Article 85(1) arguably served

the exemption of exclusive licensing agreements and certain export bans imposed on the licensor and the licensees is without prejudice to subsequent developments in the case law of the Court of Justice regarding the status of such agreements under Article 85(1). Commission Regulation No. 2343/84, O.J. L 219/16 (1984), *amended by* Commission Regulation No. 151/93, O.J. L 21/8 (1993).

16. See Pera & Todino, *supra* note 5, at 125.

a purpose in laying the foundations of the Community's law in relation to anti-competitive agreements. Moreover, this solution assured maximum disclosure to the Commission of business practices as they actually existed, and a maximum role for the Commission in deciding whether such practices were acceptable and legal.

While unfamiliarity with competition law may have been an explanation for starting with this approach, it does not constitute a reason to continue with it. After almost forty years of experience with Article 85, the Commission's competition order is near to maturity. Moreover, practically all EC Member States have passed antitrust legislation at the national level, and have set up national competition enforcement authorities. National antitrust legislation is strongly inspired by EC competition rules. Thus, even if an overly-wide jurisdiction competence could have been justified in the early years, it no longer can be.

2. Completion of the Single Market

Another supposed justification for the Commission's present approach to Article 85(1) was the formerly dominant objective of European competition law, namely the establishment of the internal market. European competition law is one of the few systems of competition law — or maybe the only system — having a market integration goal, besides the goal of promoting competition. This emphasis on promoting and protecting European integration was especially important in the earlier stages of integration when the danger that private agreements might segment the market into national and regional markets was virulent.¹⁷

Due to the perception that these agreements harmed the economic integration of Member States, the Commission placed a special emphasis on vertical relationships when enforcing anti-trust rules, thus condemning a variety of agreements between manufacturers and distributors designed to protect national

17. "European competition law is an instrument for achieving a free flow of goods, services, persons and capital, i.e. the necessary precondition for establishing the internal market (integration function) and is a goal in itself, protecting and promoting free competition in the emerging internal European market (competition function)." Christian Kirchner, *European Competition Law: Proposal for Change*, in COMPETITION WORKSHOP, EUROPEAN UNIVERSITY INSTITUTE, FLORENCE (1997).

markets.¹⁸ While a number of objections have been raised to this approach, until recently those objections have had little impact on the attitude of the Commission. Integration considerations have continued to be one of the dominant concerns in the enforcement of Article 85.

Logically, however, the realization of the internal market in 1992 affected the appropriateness of the integration aim as the dominant goal of competition policy. Accordingly, it is submitted that the integration argument must be replaced by an exclusively economic assessment of the effects on competition, thereby shifting the weight into the direction of the competition function. Antitrust law is today essentially applied in order to ensure that competition in the internal market remains in a healthy state.¹⁹

Moreover, there is no longer a need for the Commission to maintain such a formalistic and restrictive attitude towards vertical relations. Indeed, many have considered it questionable whether vertical restraints really hinder or prevent market integration at all.²⁰ Furthermore, the Commission itself, in its Green Paper on vertical restraints,²¹ seems ready to narrow the scope of Article 85(1) and to shift the economic appraisal of arrangements from Article 85(3) to Article 85(1).²² Commissioner Van Miert himself has recently declared that:

18. See, e.g., *Consten and Grundig v. Commission*, Joined Cases 56 & 58/64, [1966] E.C.R. 299, [1966] C.M.L.R. 418; *Brasserie de Haecht v. Wilkin*, Case 23/67, [1973] E.C.R. 77, [1973] C.M.L.R. 287; *Metro v. Commission*, Case 26/76, [1977] E.C.R. 1875, [1978] 2 C.M.L.R. 1; *Demo-Studio Schmidt v. Commission*, Case 210/81, [1983] E.C.R. 3045, [1984] 1 C.M.L.R. 69; *Procureur de la Republique v. Giry and Guerlain*, Case 253/78, [1980] E.C.R. 2327, [1981] 2 C.M.L.R. 99.

19. Rein Wesseling, *The Commission Notices on Decentralization of E.C. Antitrust Law: In For a Penny, Not For a Pound*, 18 EUR. COMP. L. REV., 94 (1997).

20. See VALENTINE KORAH, *EC COMPETITION LAW AND PRACTICE*, (5th ed. 1994); See also F. Carlin, *Vertical Restraints: Time for Change?*, 17 EUR. COMP. L. REV., 283 (1996).

21. Green Paper on Vertical Restraints, COM (96) 721 (1996) [hereinafter Green Paper].

22. Option IV is as follows

As a response to criticisms that the current block exemption have has a strait-jacket effect and that Article 85(1) has been applied too widely to vertical restraints without reference to their economic and market context, this option proposes the introduction of a rebuttable presumption of compatibility with Article 85(1) (the "negative clearance presumption") for parties with a market share of less than 20%. This negative clearance presumption could be implemented by a Commission notice and subsequently, in the light of experience acquired, within the framework of a negative clearance regulation.

Id. at 78, ¶ 293.

as the single market becomes a reality, a shift in emphasis is taking place in the application of Article 85. In the past, more attention was given to the legal vetting of contractual clauses which might have restricted the freedom of trade and consequently impeded the development of a single market. This was the reason for the great importance attached to vertical restrictions. But as time goes on, a more and more structural approach is emerging In handling individual cases we must be careful that the competitive structure of markets does not suffer.²³

3. The Difficulty of Making a Market Analysis in Individual Cases

Finally, the Commission may initially have been influenced by the difficulty of making a market analysis in each case, both for lawyers advising businessmen, and for its officials dealing with particular cases. As one commentator has noted "it is easier mechanically to point to clauses that restrict someone's conduct; then, the Commission is free to make a complex economic assessment under Article 85(3) in those cases it investigates in depth."²⁴ Given the now considerable experience of making market analyses in the enforcement of competition rules, such an argument is clearly no longer valid.

II. CRITICISMS OF THE COMMISSION'S APPROACH

Further criticisms of the Commission's current approach can be made. These are that the formalistic interpretation of Article 85(1) exerts an excessive compliance burden on undertakings, discourages commercial innovation by undertakings, and creates a huge and unmanageable workload for the Commission.

A. Excessive Compliance Burden

As noted above, the result of the Commission's current approach is that even agreements with little or no risk of being economically anti-competitive are deemed unenforceable if they

23. K. Van Miert, *Opening Speech to the EG-Kartellrechtsforum des Studienvereinigung Kartellrecht* (Brussels, May 11, 1995).

24. Valentine Korah, *The Rise and Fall of Provisional Validity — The Need for a Rule of Reason in EEC Antitrust*, Nw. J. INT'L L. & Bus. 320, 348-49 (1981) [hereinafter *Rise and Fall*].

have not been notified. Companies may have a formal choice of whether to notify an agreement and thereby obtain an exemption, but they have nonetheless to be concerned about the consequences of Article 85(2) on the validity of the agreement. By reducing the threshold for the application of Article 85(1) to a very low level, the effect of Article 85(2) has been to induce companies to notify a large number of agreements not having serious restrictive effects. This process requires advice, and has a real cost for the parties. Because the Commission has no enforcement interest in many cases falling within Article 85(1), the heavy compliance burden on companies cannot be justified. It has been noted that

a substantial proportion of the compliance costs has little to do with safeguarding effective competition. Costs are incurred by business in ensuring the conformity of innocuous agreements with formalistic wide-ranging rules, and in dealing with cumbersome administrative procedures. Competition law applicable to business is therefore a priority area for administrative simplification, *i.e.* the removal of unnecessary burdens and the limiting of regulation to matters of genuine economic importance.²⁵

In sum, many companies and lawyers continue to notify agreements whenever there is a possibility that they might infringe Article 85(1), simply because (i) a truthful notification confers immunity from fines,²⁶ and (ii) if a contractual provision is ever challenged in litigation, by way of claims of unenforceability or for damages, it is thought that a party to such an agreement is in a stronger position if the agreement has been notified. Thus, on those occasions when the competition rules are invoked before national courts, the argument that an agreement is acceptable because it has been notified is not infrequently made.²⁷

25. UNICE, *Modernising EU Competition Policy: Re-Focusing the Scope and Administration of Article 85 and Reform of State Aid Control*, 11-12 (June 28, 1996) [hereinafter *Modernising EU Competition Policy*].

26. Article 15(5) of Regulation 17/62, states that "the fines provided for in paragraph 2(a) shall not be imposed in respect of acts taking place: (a) after notification to the Commission and before its decision in application of Article 85(3) of the Treaty, provided they fall within the limits of the activity described in the notification" Commission Regulation No. 17/62, art. 15(5), O.J. L 204/62, at 91, (1962).

27. Forrester & Norall, *supra* note 4, at 11, 41-45.

B. *Discouragement of Commercial Innovation*

The Commission's practice of only making a market analysis under Article 85(3), and not under Article 85(1), may discourage firms from implementing projects involving substantial sunk costs.²⁸

C. *Huge Commission Workload*

As noted, an enormous number of agreements have been considered at least *prima facie* unenforceable despite the fact that they contain more pro- than anti-competitive elements, and are highly likely to be exempted under Article 85(3). The availability of exemptions is thus indispensable for the system to function as it was designed. Yet, the current formalistic approach, by encouraging recourse to individual exemptions, has resulted in a huge workload for the Commission's staff. Cases take years to move forward and "remain indefinitely in a kind of limbo."²⁹ Only a few specific exemptions are issued each year.³⁰

Thus, a structural discordance exists between the asserted jurisdictional reach of the Commission and its administrative capacity to deliver the legal certainty for which its theory creates a need.³¹ The large number of notifications is consistent with the logic of the system, but also contributes to its unworkability.³² Moreover, the Commission's excessive workload has meant that

28. Margot Horspool & Valentine Korah, *Competition*, 37 ANTITRUST BULL. 337 (1992). Horspool and Korah stated that "the Commission has tended to perceive the agreement *ex post*, after investments were made, and not *ex ante* when parties were negotiating their agreements, and each needed to insure that he would reap any harvest resulting from his investment." *Id.* at 347. "The parties need to know when they are negotiating the contract and committing themselves to incurring sunk costs that the contractual provisions will be enforceable." *Id.* at 355.

29. *Id.* at 358.

30. In 1996, DG-IV registered 471 new cases, including 209 notifications, 168 complaints, and 94 cases opened on the Commission's own initiative. COMMISSION OF THE EUROPEAN COMMUNITIES XXVITH REPORT ON COMPETITION POLICY 1996, at 50, ¶ 110 (1997). The European Commission noted that "although the number of new cases is lower than in 1995, it exceeds the average number of incoming cases over the last nine years by more than 10%. In 1996 notifications were sharply down, whereas complaints and own-initiative proceedings showed a substantial increase." *Id.* at 38-39. During 1996, the Commission closed 386 cases, of which 365 ended informally, such as by comfort/discomfort letter, rejection of complaint without a decision, or administrative closure of the file, and only 21 by formal decision. *Id.*

31. Ian Forrester, *Competition Structures for the 21st Century*, in 1994 FORDHAM CORP. L. INST. 445 (Barry Hawk ed., 1995).

32. Forrester & Norall, *supra* note 4, at 14; Christopher Bright, *Deregulation of EC*

it has not been able to concentrate on important and politically sensitive cases.³³ Many serious restrictions of competition therefore escape the Commission's attention because of its excessive focus on cases having only minor restrictive consequences.

Finally, with increased deregulation of nationalized industries and the completion of the internal market, the Commission workload is likely to increase further as whole sectors, such as telecommunications, energy, or postal services are fully subject to the application of the competition rules. Introducing competition necessarily means enlarging the scope of state aids rules to these sectors. Otherwise, the new competitive environment would be hampered from the outset by severe distortions of competition. The number of cases dealt with by the Commission has tripled within a period of eight years. Parallel to the increased number of cases, the Commission has also observed an increase in the complexity of the cases dealt with. On the other hand, the overall number of DG-IV staff dealing with State aid cases has remained relatively stable in the same period.

Block exemption regulations under Article 94 of the EC Treaty could contribute to a reinforced State aid policy. Such regulations would exempt certain categories of aid, by way of block exemptions, from the notification obligation, and would cover aid to small and medium-sized enterprises, as well as certain types of aid for research and development, employment, training, and environmental protection. Moreover, such regulations would provide a safe legal basis for the *de minimis* rule in the field of State aids.³⁴

D. *Commission's Failed Attempts to Reduce its Workload*

The Commission is well aware of the necessity of resolving the shortfalls of the current system. Indeed, since the mid-1970s, wave after wave of initiatives have aimed at doing just that. However, none of the attempts by the Commission to improve the system have been successful. In particular, group exemption regulations have led to a loss of flexibility; comfort letters lack

Competition Policy: Rethinking Article 85 (1), in 1994 FORDHAM CORP. L. INST. 505, 514 (Barry Hawk ed., 1995).

33. See Mario Siragusa, *Future Competition Policy*, COMPETITION WORKSHOP, EUROPEAN UNIVERSITY INSTITUTE, FLORENCE (1997).

34. WOLFGANG MEDERER, *The Future of State Aid Control*, COMPETITION POLICY NEWSLETTER 12 (1996).

legal certainty; and decentralization attempts have been ineffective, due to the limited enforcement powers granted to national courts and authorities.

1. Loss of Flexibility Through Group Exemption Regulations

The Commission has tried to overcome its inability to grant many individual exemptions by granting group exemptions for specified classes of agreements.³⁵ Block exemption regulations solve some problems, but often their terms are too rigid and their scope of application is limited. For instance, the exemption for exclusive distribution applies only where goods are supplied for resale and not to the distribution of services. Thus, compliance with the terms of a group exemption frequently entails a substantial loss of flexibility which may be regarded as undesirable. Unfortunately, each of the block exemptions applies to only a narrow class of contracts. The tailoring of agreements to fit into a block exemption may lead to the ossification of contractual structures.³⁶

2. Lack of Legal Certainty Through Comfort Letters

The Commission has also attempted to find a solution by issuing comfort letters. In practice, most files are closed by a letter, stating that the Commission thinks that the agreement does not restrict competition, often owing to the small market shares of the parties. The Court of Justice has ruled that a com-

35. The following block exemption regulations have been adopted: Commission Regulation No. 1983/83, O.J. L 173/1 (1983) (concerning distribution agreements), Commission Regulation No. 1984/83, O.J. L 173/5 (1983) (concerning exclusive purchasing agreements), Commission Regulation No. 417/85, O.J. L 53/1 (1985) (concerning specialization agreements), Commission Regulation No. 418/85, O.J. L 53/12 (1985) (concerning R&D agreements), Commission Regulation No. 4087/88, O.J. L 353/46 (1988) (concerning franchise agreements), Commission Regulation No. 1475/95, O.J. L 145/25 (1985) (concerning motor vehicle distribution and servicing agreements), Commission Regulation No. 240/96, O.J. L 31/2 (1996) (concerning technology transfer agreements).

36. Horspool and Korah note that

the drawback of proceeding by regulating agreements through providing group exemptions is that some agreements are distorted by the parties to come within them and be enforceable without improving the fairness or efficiency of the economy. Those who pay substantial sums to obtain good advice may select the group exemption that requires the least distortion to the agreement. Smaller firms, obtaining less sophisticated advice, may find they cannot enforce important parts of their agreements.

Horspool & Korah, *supra* note 27, at 357.

fort letter may be taken into account by a national court asked to enforce the agreement, but does not bind it.³⁷ Indeed, the principal disadvantage of comfort letters is that they have no legal effect. If an undertaking accepts a comfort letter, there is always the risk that, at some point in the future, the benefit of the comfort letter will be removed.³⁸ Finally, a comfort letter stating that the agreement merits exemption, but that the Commission is closing its file, implies that the agreement infringes Article 85(1), otherwise, it would not need exemption.³⁹ This type of comfort letter creates legal uncertainty.

3. Limited Enforcement Powers of National Courts

In view of its limited resources and the increasing number of cases, the Commission has also tried to decentralize the enforcement of EC antitrust law. To this end, the Commission has, for many years, encouraged civil actions before national courts, thus in theory enabling it to devote its resources to cases involving cross-border transactions. Two Court judgments⁴⁰ lend support to the Commission's campaign for greater private enforcement at the national level.

Decentralization is a logical consequence of the growing importance of the concept of subsidiarity.⁴¹ In the context of EC competition law, subsidiarity means that cases in which the Community has an important economic, political, or legal interest should be handled by the Commission, while national authorities should deal with agreements or practices affecting only na-

37. *Procureur de la République v. Giry and Guerlain*, Case 253/78, [1980] E.C.R. 2328; Valentine Korah, *Comfort Letters - Reflections on the Perfume Cases*, EUR. L. REV., 14, 38-39 (1981). According to the Commission, a national court may consider a comfort letter stating that the agreement being litigated before it merits exemption "as a factual element." Commission Notice, O.J. C 39/6 (1993) (concerning cooperation with courts).

38. *Rise and Fall*, *supra* note 23, at 334; *Modernising EU Competition Policy*, *supra* note 24, at 12.

39. *Modernising EU Competition Policy*, *supra* note 25, at 12.

40. *Delimitis v. Henninger Bräu*, Case C-234/89, [1991] E.C.R. I-935, [1992] 5 C.M.L.R. 210.

41. "Subsidiarity" is defined in Article 3b of the Treaty on European Union. Treaty on European Union, Feb. 7, 1992, art. 3, O.J. C 224/1 (1992), [1992] 1 C.M.L.R. 719, 31 I.L.M. 247 (amending Treaty Establishing the European Economic Community, Mar. 25, 1957, 298 U.N.T.S. 11, as amended by Single European Act, O.J. L 169/1 (1987), [1987] 2 C.M.L.R. 741 [hereinafter SEA], in TREATIES ESTABLISHING THE EUROPEAN COMMUNITIES (EC Off'l Pub. Off. 1987)).

tional markets.⁴²

However, attempts at decentralization fall far short of the required degree of reform. As noted above, the broad and legalistic interpretation of Article 85(1) transfers the economic analysis of antitrust cases to Article 85(3). The application of Article 85(3) implies the exercise of considerable discretionary power. As noted also, pursuant to Article 9(3) of Regulation 17, only the Commission enjoys such discretion. Consequently, at present, the Commission itself is exclusively qualified to enforce EC competition law comprehensively. Thus, in the present circumstances increased cooperation with national courts and authorities does not seriously resolve the Commission's overload problem.

III. *THE RULE OF REASON AND PROCEDURAL IMPROVEMENTS*

The adoption of a rule of reason approach in the assessment of agreements in the European competition law context, together with various accompanying procedural improvements, may constitute a solution to many of the problems discussed above.

A. *Rule of Reason Approach*

A relaxation of the interpretation of Article 85(1) is needed to increase the number of cases where economic behavior can be said to comply with Article 85, without it being necessary to resort to Article 85(3). Under the rule of reason, a full competitive balance would be made in the context of Article 85(1).⁴³ Agreements containing restrictions would be evaluated through an appreciability test. The appreciability test would make it possible to balance pro- and anti-competitive elements of commercial agreements. When the anti-competitive elements were outweighed, agreements would not be caught by Article 85(1), and would not require notification to the Commission.⁴⁴

How would such a rule of reason be applied in practice? It is clear that a redrafting of the Treaty competition rules is not only a politically controversial proposition, but would be entirely

42. Ivo Van Bael, *The Role of National Courts*, 1 *EUR. COMP. L. REV.* 3 (1994).

43. Pera & Todino, *supra* note 5, at 125.

44. *Modernising EU Competition Policy*, *supra* note 25, at 12.

unnecessary. Article 85 is drafted broadly enough to allow the Commission and the Court of Justice to bring about important changes in the current application of EC competition law, without departing from the existing framework. Moreover, because Article 85(1) of the EC Treaty mirrors section 1 of the Sherman Act, which is interpreted by means of a rule of reason approach, there is in principle no reason why it should not be similarly interpreted.

Thus, these changes may be achieved through a gradual shift in the Commission's economic appraisal of agreements from Article 85(3) to Article 85(1). Such a shift could begin with a different approach to the application of the phrase "prevention, restriction or distortion of competition" in Article 85(1). Before deciding that a given restriction of competition was illegal, the Commission would (i) assess whether such competition could exist at all; and (ii) carry out an economic balance of the agreement's positive and negative market effects, for example, by considering whether a firm benefiting from exclusivity would have found it worthwhile to make an investment, in the absence of such exclusivity.

B. *The Residual Role of the Exemption Process Under Article 85(3)*

In the context of the proposed system, the role of Article 85(3) would change. Article 85(3) exemptions would be applied only in cases involving political issues, so that agreements or practices that are deemed restrictive on pure antitrust grounds would be authorized where "redeeming virtues" of industrial,⁴⁵ regional, social,⁴⁶ or environmental policy were found to outweigh the detrimental impact of the cooperation or collusion

45. Industrial policy considerations, such as the development and dissemination of new technologies throughout the Community or the competitiveness of European industries, have been taken into account, to some extent, by the Commission in its decisions concerning specialization agreements. *See e.g.* Commission Decision No. 72/231/EEC, O.J. L 182/24 (1972) (Fine Paper); Commission Decision No. 84/387/EEC, O.J. L 212/1 (1984) (BPLC/ICI); Commission Decision No. 87/3/EEC, O.J. L 5/13 (1987) (ENI/Montedison); Commission Decision No. 76/249/EEC, O.J. L 51/15 (1976) (KEWA); Commission Decision No. 77/781/EEC, O.J. L 327/26 (1977) (GEC-Weir Sodium Circulators).

46. Employment problems have played a limited role in crisis cartel cases. *See e.g.*, Commission Decision No. 84/380/EEC, O.J. L 207/17 (1984) (Synthetic Fibers). *See also* Commission Regulation No. 1475/95, arts. 5(2)(2)-(3) and 8(2), O.J. L 145/25 (1995) (including, in context of block exemption for motor vehicle distribution and servicing agreements, provisions covering matters of social, fiscal, and industrial policy,

between the parties.⁴⁷

However, individual exemptions would still be subject to the two-fold condition that the agreement neither (i) imposes on the parties restrictions which are not indispensable to the attainment of the non-competition objectives mentioned above, nor (ii) affords them the possibility of eliminating competition in the relevant market.⁴⁸ Moreover, because an exemption under Article 85(3) is limited in time, restrictions of competition considered indispensable to achieve industrial, regional, social, or environmental policy objectives would be eliminated at the end of the period for which the exemption has been granted.

C. *Advantages of the Proposed System*

The introduction of a rule of reason approach would have numerous advantages. First, conducting a market analysis before finding that Article 85(1) is infringed would mean that agreements which do not in fact restrict any competition, or any competition that would be possible without the agreement, could be made, knowing that they would be enforceable. This would enable businessmen to place incentives where they should be. Reducing the need for prior notification of pro-competitive agreements would alleviate the excessive compliance burden on undertakings discussed above and allow the Commission, as noted, to concentrate on important and politically sensitive cases.

Second, the proposed change would be helpful from the point of view of the decentralized enforcement of Community competition law. It would facilitate the application of substantive competition provisions by national courts. In cases where a national court was confronted with a notified agreement, that court would no longer be obliged to await the Commission's decision or informal comfort letter, but could decide on its own that Article 85(1), correctly construed, was inapplicable.

Third, applying a rule of reason approach would have the advantage of a concomitant reduction in the Commission's abil-

such as required notice period to be given when dealer is dismissed, and harmonization of car prices throughout European Union).

47. Siragusa, *supra* note 32, at 13-14.

48. Examples of exemptions include where the parties to an agreement have negligible market power or, though holding significant positions within the EU market, face substantial competitive pressure from non-EC competitors.

ity to exercise universal surveillance over all questionable cases. In many cases, national courts and authorities are perfectly competent to make a competition assessment, and there is no reason for the Commission to intervene.

Fourth, the proposed system would have the effect of improving judicial review of competition decisions. In fact, decisions adopted by the Commission under Article 85(1) are easier to judicially review than decisions rendered under Article 85(3), which imply the exercise of a broad discretionary power by the Commission.

Finally, this new approach would be beneficial to the development of market arrangements, no longer constrained to the standardization imposed by block exemption regulations. This would be because less agreements would be caught by Article 85(1), and therefore require tailoring to fit the terms of block exemption regulations.

D. The Adoption of a "Rule of Reason" Approach by the Italian Antitrust Authority

A "rule of reason" approach not dissimilar from the one proposed in this Essay has been applied by the Italian Antitrust Authority ("IAA") in its practice in application of Articles 2 and 4 of Law No. 287/1990 of October 10, 1990. The Italian provisions correspond to Article 85(1) and 85(3) of the Treaty, respectively. The IAA has described its approach in the following terms:

Consistently with the Community approach, the Authority has stated that, after an agreement is found to have a restrictive object, an assessment of the restrictive nature of its effect is not necessary for purposes of establishing a violation of Article 2(2) of Law No. 287/90, since the two prerequisites laid down in this provision are alternative As a qualification to the above, however, . . . it cannot be ruled out that, even if an agreement is found to have a restrictive object, the analysis of its effects, as a possible indicator of the agreement's restrictive nature with respect to the structure of the relevant market, may become appropriate. The agreement's effects may become relevant for the purpose of establishing possible external factors, which must be taken into account in the whole assessment, with particular respect to the agreement's appreciability. Under the settled case law of Court of Justice,

the effects of an agreement must be assessed in its legal and economic context. Therefore, the way in which market relationships would have developed in the absence of the agreement in question must be taken into account; furthermore, the agreement must be assessed jointly with any other similar agreements existing in the same market. Where scrutiny of an agreement's effects appears necessary, an economic analysis of the markets, which must take into account such elements as the existence of intellectual property rights, the existing degree of competition and the competitors' reaction to the agreement's effects, will thus be indispensable.⁴⁹

E. Procedural Improvements

In the context of the new system, a number of measures could be adopted in order to increase the role of national courts in the enforcement of EC competition rules, free the Commission to concentrate its energies effectively, and aid the practical application of the rule of reason approach. These procedural improvements fall into four main categories: (i) guidelines and Notices; (ii) block negative clearances; (iii) improved cooperation between the Commission and national courts and authorities; and (iv) further development of the informal settlement of cases.

1. Guidelines and Notices

The implementation of the rule of reason approach described above could be supported by explanatory and illustrative guidelines drawn up by the Commission and published in a new Notice. Such guidelines would assist both businessman and lawyers in determining whether agreements required individual exemption, or fell outside the scope of Article 85(1). The guidelines could, in practice, be based on certain existing Commission communications, particularly the Notices on cooperation between enterprises, subcontracting agreements, and exclusive dealing contracts with commercial agents, as well as the Green Paper on vertical restraints. Further guidelines concerning the methods for applying the appreciability test to cooperation agreements could be added to the existing Notices.

49. AUTORITÀ GARANTE DELLA CONCORRENZA E DEL MERCATO, *RELAZIONE ANNUALE SULL'ATTIVITÀ SVOLTA 1994* [1994 Annual Report] 129 (1995).

Even this approach would not resolve all uncertainty, and so increased flexibility in the interpretation of Article 85(1) should be accompanied by an expansion of the scope of the Notice on agreements of minor importance, and by removing certain further classes of agreement from the necessity of notification.⁵⁰

2. Block Negative Clearances

One of the principal objectives of introducing a rule of reason approach is to achieve a decrease in the number of notifications of agreements or practices to DG-IV. The likelihood of such a result being achieved would be significantly enhanced if private parties were able to rely, before European and national courts and competition authorities, upon block negative clearances. Block negative clearances would take the form of official acts that the Commission, on the basis of its individual casework, would produce and publish for the purpose of aiding in the proposed new approach to the interpretation of Article 85(1). Such clearances would have the effect of clarifying and reducing the perceived scope of Article 85 in those areas where no policy issues arise.

As to the form that such block negative clearances would take, the Notices issued by the Commission thus far are merely an expression of its thinking in abstract terms, and do not prejudice its power to depart from them in individual cases. Notices bind neither European nor national courts. They are, therefore, unable to provide a desired level of certainty for businessmen or their lawyers. Any future explanations of the Commission's policy in the application of the rule of reason will amount to simple communications, having no binding legal effect, unless the Commission is empowered by the Council of Ministers to adopt group negative clearances in the form of regulations.⁵¹

In practical terms, the Commission's recent publication of a Green Paper on vertical restraints — which is intended to form the basis for consultation with Member States, other EU institutions, and business, and to be followed by a white paper selecting the best policy option — could serve as a model in other areas of

50. See *Modernising EU Competition Policy*, *supra* note 25, at 12.

51. This is pursuant to Article 87 of the Treaty, as it was the case for the adoption of Article 85(3) regulations. See Council Regulation No. 19/65, 36 J.O. 533/65 (1965), O.J. Eng. Spec. Ed. 1965-1966, at 35.

application of Article 85(1). Moreover, because a number of group exemptions under Article 85(3) are due to expire shortly,⁵² in the first phase of the new enforcement system based on the rule of reason, the development of new Commission Notices could be planned to coincide with the adoption of renewed block exemptions. The "white lists" of provisions deemed rarely to infringe Article 85(1) would be longer in the new group exemptions than under the original regulations.⁵³ The Commission, however, should not place clauses on the white list in an indiscriminate way, or grant exemptions merely for the sake of legal certainty.⁵⁴

3. Improved Cooperation between the Commission and National and International Courts and Authorities in the Enforcement of Competition Rules

As noted above, under the new approach to Article 85 fewer agreements would be notified to the Commission. Fewer notifications would likely lead to an increase in third party complaints, both to the European Commission and to national competition authorities ("NAAs"). At the procedural level, this increase would require the establishment of a strong and well-defined system of cooperation amongst all the authorities involved in handling such complaints, including authorities outside Europe.⁵⁵

52. Regulation No. 1984/83 on exclusive purchasing agreement; Regulation No. 417/85 on specialization agreements; and Regulation No. 418/85 on R&D agreements will expire on December 31, 1997; whereas Regulation No. 4087/88 on franchise agreements as well as Regulation No. 1983/83 on exclusive distribution agreements will expire on December 31, 1999.

53. As was the case, for example, for Commission Regulation No. 240/96, O.J. L 31/2 (1996) (Technology Transfer Block Exemption), whose white list under Article 2 is considerably longer than the white lists in Article 2 of the earlier Regulations No. 2349/84 on patent licensing agreements and No. 556/89 on know-how licensing agreements. See Commission Regulation No. 240/96, O.J. L 31/2 (1996); Commission Regulation No. 2349/84, O.J. L 219/15 (1984); Commission Regulation No. 556/89, O.J. L 61/1 (1989).

54. See Recital 18 and Article 2(2) of the Technology Transfer Block Exemption. Commission Regulation No. 240/96, *supra* note 52, art. 2(2), O.J. L 31/2 (1996).

55. In the field of international cooperation there were, for example, from July 1, 1996 to December 31, 1996, no fewer than 18 notifications of merger cases by the European Commission to the U.S. authorities and 9 notifications of non-merger cases. In the same period, there were 9 notifications of merger cases by the U.S. authorities to the European Commission, and 3 notifications of non-merger cases. See Commission Report on the Application of the Agreement between the European Communities and the Government of the United States of America Regarding the Application of their Competition Laws COM (97) 346 Final (July 1997).

Within Europe, it may, in particular, become necessary for the Commission to assist in coordinating NAA actions. For example, assistance may be required where an NAA, in the course of an investigation under Article 85 or its national competition provisions, establishes that allegedly anti-competitive conduct may have an impact in another Member State. The Commission could assist principally by providing information, obtained in other proceedings, about the undertakings under investigation by the NAA.

In such a circumstance, an important procedural requirement would be that an NAA, which obtains relevant information from the Commission, should be empowered to use such information in order to prove the alleged infringement of Article 85 that are the subject of its proceedings. Such a power would naturally be subject to the obligation, provided for by Article 20 (2) of Regulation 17, not to disclose information "of the kind covered by the obligation of professional secrecy."

This position was endorsed by the Commission in the *Spanish Banks* case.⁵⁶ Moreover, in a recent judgment, *Postbank NV v. Commission*,⁵⁷ the Court of First Instance, ruled that

the principle of sincere cooperation inherent in Article 5 of the Treaty requires the Community institutions, and above all the Commission, which is entrusted with the task of ensuring application of the provisions of the Treaty, to give active assistance to any national judicial authority dealing with an infringement of Community rules. That assistance, which takes various forms, may, where appropriate, consist in disclosing to national courts documents acquired by the institutions in the discharge of their duties.⁵⁸

It is unclear to what extent this judgment of the Court of

56. See *Dirección de Defensa de la Competencia v. Asociación Española de Banca Privada*, Case C-67/91, [1980] E.C.R. I-4785, I-4812 [hereinafter *Spanish Banks*]. This case, which arose from an Article 177 reference from the Spanish Tribunal for the Defence of Competition, provided the Court with the first occasion to discuss for what purposes a competent NAA can use information provided by one or more undertakings to the Commission in response to a request for information pursuant to Article 11, or in notifications made pursuant to Articles 2, 4 or 5 of Regulation 17/62, in national proceedings. *Id.*

57. *Postbank NV v. Commission*, Case T-353/94, [1996] E.C.R. II-921, [1997] 4 C.M.L.R. 33.

58. *Id.* at 945, ¶ 64, [1997] 4 C.M.L.R. at 37.

First Instance alters the previous ruling of the Court of Justice, in the *Spanish Banks* case, which rules that

such information cannot be relied on by the authorities of the Member States either in a preliminary investigation procedure or to justify a decision based on provisions of competition law, be it national law or Community law. Such information must remain internal to those authorities and may be used only to decide whether or not it is appropriate to initiate a national procedure.⁵⁹

The Court of Justice reasoned that, notwithstanding the fact that Article 10(1) of Regulation 17 envisages the transmission of information collected by the Commission to NAAs, the purpose of this provision is to inform the Member States of any Commission proceedings concerning companies located in other territories, and to promote the collection of information by the Commission, by enabling NAAs to make observations. According to the Court, "the mere disclosure of such information to the Member States does not, of itself, mean that they may use it under conditions which would undermine the application of Regulation No 17 and the fundamental rights of undertakings."⁶⁰ However,

the very view that the use of information obtained by the Commission in antitrust proceedings conducted by NAAs would amount to a 'use for other ends' within the meaning of Article 20 of Regulation 17 seems unreasonably formalistic to the extent that, no matter who the enforcer in a specific case is, that information is used for the purpose of applying the same set of rules, except for rules governing the imposition of sanctions.⁶¹

4. Further Development of Informal Settlement of Cases

In adopting a rule of reason approach, the Commission should develop its current policy of adopting a relatively small number of formal decisions, under Regulation 17, in selected cases of great importance for the development of European competition policy. A correspondingly increased number of

59. *Id.* at 939, ¶ 42, [1997] 4 C.M.L.R. at 42.

60. *Spanish Banks*, [1980] E.C.R. at I-4832, ¶ 34.

61. *Siragusa*, *supra* note 33, at 13-14.

cases should be settled in informal ways, particularly through comfort letters.

As noted above, comfort letters are not at present legally binding. The smooth functioning of the proposed system would be greatly aided if DG-IV were able to issue "formal" comfort/discomfort letters. It is clear that a letter signed by a Director of DG-IV may amount to a decision within the purview of Article 189 of the EC Treaty.⁶² In developing the comfort letter procedure, DG-IV should first direct its efforts towards supporting its letters with a fully reasoned opinion. Second, the Commission should draw on its two Notices on procedures for applications for negative clearance⁶³ and notifications,⁶⁴ which provide that the essential contents of notified agreements should be routinely published in the Official Journal in order to invite comments from third parties.⁶⁵

If the European courts were willing to endorse these, and possibly further adjustments in the Commission's enforcement methods, a system based on the rule of reason would develop in time. This system would provide businessmen, lawyers, and national courts and competition authorities with both security and a practical framework for analysis.⁶⁶

CONCLUSION: PRACTICAL APPLICATIONS OF THE RULE OF REASON APPROACH

As noted above, a redrafting of the European competition rules would be entirely unnecessary to bring about important changes in the current application of EC competition law. The changes proposed here may be achieved through a gradual shift

62. *British American Tobacco and RJ Reynolds v. Commission*, Joined Cases 142 & 156/84, [1987] E.C.R. 4487, [1988] 4 C.M.L.R. 24. Formal comfort letters would become subject to judicial review under Article 173 of the Treaty. See *Bureau European Des Unions Des Consommateurs v. Commission*, Case T-37/92, [1994] E.C.R. II-285, [1995] 4 C.M.L.R. 167.

63. Commission Notice, O.J. C 343/4 (1982) (concerning application procedures for negative clearance pursuant to Article 2 of Council Regulation No. 17/62).

64. Commission Notice, O.J. C 295/6 (1983) (concerning notification procedures pursuant to Article 4 of Council Regulation No. 17/62(1)).

65. In the Commission's view, "[t]he legal certainty provided by a comfort letter is even stronger if a notice has been published pursuant to Regulation 17, Article 19(3), which has not elicited adverse comments from third parties." Green Paper, *supra* note 21, COM (96) 721 at 56, ¶ 190.

66. *Id.* at 56, ¶ 190.

in the Commission's economic appraisal of agreements from Article 85(3) to Article 85(1). The feasibility of this approach is confirmed by the position sometimes adopted by the European courts in interpreting Article 85(1). In this respect, the European courts have, on several occasions, adopted a less narrow and systematic, more economically-based approach, than the Commission.⁶⁷ As two commentators stated, the case law of the European courts

reveals two ways in which the rule of reason can be applied. The first, established in a line of cases from *Technique Minière* to *Delimitis*, applies a rule of reason by stressing that thorough analysis of the economic context surrounding the agreement and the effect of the agreement in the relevant market is necessary to determine whether the obligations are anti-competitive to any significant extent. The second approach, adopted in cases from *Metro I* to *Pronuptia*, focuses more on the terms of the agreement itself, so that if on balance the economic advantages of the agreement mean that the agreement can be seen to be pro-competitive overall, any restrictions which are essential to the performance of the agreement fall outside Article 85(1).⁶⁸

By way of conclusion, these two practical applications of the rule of reason are now discussed, and illustrations are given. These cases demonstrate the feasibility of the Commission following the European courts' approach, and similarly adopting a rule of reason.

67. See e.g., *Société Technique Minière*, [1966] E.C.R. at 235, [1966] C.M.L.R. at 357; *Brasserie de Haecht*, [1973] E.C.R. at 77, [1973] C.M.L.R. at 287; *Völk v. Vervaecke*, Case 5/69, [1969] E.C.R. 295, [1969] C.M.L.R. 273; *Metro*, [1977] E.C.R. at 1905, [1978] 2 C.M.L.R. at 1; *Remia*, [1985] E.C.R. at 2545, [1987] 1 C.M.L.R. at 1; *Coöperatieve Stremsel-en Kleursel-fabriek*, Case 61/80, [1981] ECR 851, 867, [1982] 1 C.M.L.R. 240; *Nungesser*, [1982] E.C.R. at 2068-69, [1983] 1 C.M.L.R. at 278; *Coditel*, [1982] E.C.R. at 3401-02, [1983] 1 C.M.L.R. at 49; *AEG v. Commission*, Case 107/82, [1983] E.C.R. 3151, 3194, [1984] C.M.L.R. 325; *BAT Cigaretten-Fabriken v. Commission*, Case 35/83, [1985] E.C.R. 363, [1985] 2 C.M.L.R. 470; *Pronuptia de Paris v. Schillgalis*, Case 161/84, [1986] E.C.R. 353, 381, 388-89, [1986] 1 C.M.L.R. 414; *Erauw-Jacquery v. La Hesbignonne*, Case 27/87, [1988] E.C.R. 1919, 1938-39, [1988] 4 C.M.L.R. 576; *Delimitis*, [1991] E.C.R. at I-935, [1992] 5 C.M.L.R. at 210; *Gøttrup-Klim Grovwareforeninger v. Dansk Landbrugs Grovareselskab*, Case C-250/92, [1994] ECR I-5641, [1996] 4 C.M.L.R. 191; *Langnese-Iglo v. Commission*, Case T-7/93, [1995] ECR II-1533, [1995] C.M.L.R. 602.

68. BELLAMY & CHILD, COMMON MARKET LAW OF COMPETITION 68-69 (4th ed., 1993).

A. *Rule of Reason Applied to Interpret Context of Agreement*

As noted above, the European courts have often stressed that a thorough analysis of both the economic context and overall effect of agreements is necessary to determine whether restrictive obligations are anti-competitive to any significant extent.

For example, in *Brasserie de Haecht*, in considering the validity of a brewery tie agreement, the Court concluded that agreements, in which an undertaking agreed to obtain its supplies from one undertaking to the exclusion of all others did not "of their nature" fall within Article 85(1), but might do so if a market analysis taking account of other similar agreements disclosed an appreciable restriction on competition. In this case, the Court confirmed that in considering whether an agreement has the effect of restricting competition within the meaning of Article 85(1), it is relevant to consider the whole economic context including, in particular, the existence of other agreements to the same effect.

Similarly, in *Delimitis*, the Court of Justice ruled that a purchasing contract brought advantages to both parties, even though the contract required the tenant of a bar owned by a brewery to buy most of the beer sold at the bar from the brewery. In deciding that such an agreement did not have the object of restricting competition, the Court ruled that an exclusive purchasing agreement must be considered in its economic and legal context to determine whether it contributes significantly to the foreclosure of the relevant market and hence falls within Article 85(1). In this respect, once the relevant market has been defined, one has to assess the nature and the importance of the totality of exclusive purchasing contracts and then examine the other conditions of the market, including the number and size of other producers and market saturation. Market share and the duration of the contracts are also important factors in determining whether foreclosure is likely to occur. When the totality of the agreements does not have the effect of foreclosing the market, these agreements do not fall within Article 85(1).⁶⁹

Thus, the Court of Justice held that before finding that the agreement, together with other agreements tying other bars to

69. *Delimitis*, [1991] E.C.R. at I-984, ¶ 14 - 33, [1992] 5 C.M.L.R. at 210.

one brewer or another, had the effect of restricting competition, a national court should inquire whether the agreements would in fact foreclose other brewers. The Court of Justice said that this would be the case only if it were difficult to open new bars, and if so many were tied to one brewer or another for so long that there were no real and concrete opportunities for a new brewer to enter or for an existing one to expand. Moreover, even if the aggregate effect of many ties to different brewers does foreclose, it is only those agreements that make a substantial contribution to foreclosure that are void. This may be judged by both the market share of the supplier or the duration of the ties. The Court of First Instance recently followed the approach suggested by the Court of Justice.⁷⁰

B. *Rule of Reason Applied to Interpret Terms of Contract*

The second example of the Court's application of the rule of reason approach is its use of the ancillary restraints doctrine in interpreting the terms of particular potentially anti-competitive agreements.

On the basis of a broad interpretation of the ancillary restraints doctrine, the Court has considered that a large number of restrictive clauses escape Article 85(1). The Court often clears restraints necessary to make viable a transaction that is not, in itself, anti-competitive, but which contains restrictive elements. The Court has held, for example, that exclusive distribution agreements and exclusive license agreements are not caught by Article 85(1) where they are necessary to enable the penetration of an undertaking into a new market.

In *Nungesser*, for example, in determining whether there was a restriction of competition within the meaning of Article 85(1), the Court of Justice looked at the economic nature and consequences of the conduct involved. The Court concluded that certain territorial exclusivity provisions in patent licenses favor the introduction and exploitation of new technologies.⁷¹

70. See *Langnese-Iglo*, [1995] E.C.R. at II-1533, [1995] C.M.L.R. at 602.

71. The Court of Justice stated that

In case of a license of breeders's rights over hybrid maize seeds newly developed in one Member State, an undertaking established in another Member State which was not certain that it would not encounter competition from other licensees for the territory granted to it, or from the owner of the right himself, might be deterred from the risk of cultivating and marketing that

Licenses would not be willing to take the necessary risks if they were not assured of this degree of exclusivity.

The Court used this analysis, which the Commission has traditionally accepted but relegated to Article 85(3), to reach the conclusion that these provisions were not caught by Article 85(1). The Court distinguished between (i) an open exclusive license, whereby the licensor merely agrees not to license anyone else for the same territory and not to compete with the licensee; and (ii) a protected exclusive license, whereby the parties go further and take contractual and other measures to prevent all competition from parallel importers or licensees in other territories. In sum, in *Nungesser*, the Court seems to be saying that an exclusive right does not "of its nature" fall within Article 85(1) where the grant of such a right is essential to the penetration of a new market by the distributor or licensee.

Finally, the *Pronuptia* case also bears indications of a rule of reason approach. In that case a franchisee shopowner was required, *inter alia*, to use the Pronuptia name and sell Pronuptia goods only in the shops specified in each agreement and to obtain its requirements of wedding and other dresses from the franchisor or suppliers nominated by him.

The Court considered that restraints that were prerequisites to the functioning of the franchise system did not constitute "restrictions of competition" within the meaning of Article 85(1). The Court held that the first such prerequisite was for the franchisor to be able to transfer his know-how and methods to the franchisee without running the risk that he was aiding a competitor. As the transfer of intellectual property rights is vital to the franchising exercise, it is legitimate for a franchisor to impose terms on a franchisee to protect these rights. The second prerequisite identified by the Court was for the franchisor to be able to preserve the identity and the reputation of the network by imposing common standards on all franchisees. The prohibitions on the franchisee that were justified on these grounds fell outside Article 85(1).

Having first stated that a franchise system of the kind in

product; such a result would be damaging to the dissemination of a new technology and would prejudice competition in the Community between the new product and similar existing products.

Nungesser, [1982] E.C.R. at 2069, ¶ 58, [1983] 1 C.M.L.R. at 278.

question was in itself not restrictive of competition, having advantages for both parties and enabling new markets to be established, the Court thus concluded that restrictions seeking to maintain common standards and to protect intellectual property were not within Article 85(1) at all.