Consumer Welfare in EU Competition Policy

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Abstract

The paper does not address the wider debate about the aims of competition law. It focuses instead primarily on a narrower issue of the choice and implementation of a so-called 'welfare standard'. In particular, I discuss what seems to be the dominant self-declared paradigm for many competition authorities, that is, that their job is to protect consumer welfare. I give an introduction to the discussion among economists about the merits of consumer welfare as opposed to total welfare, the leading other candidate as a welfare standard. I furthermore argue that transporting the consumer welfare paradigm into action may lead the practitioner to face difficult choices – and that a literal implementation of the consumer welfare standard at times may seem to make little sense.

1. Introduction

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1. The views expressed in this article are solely those of the author and do not necessarily reflect those of the European Commission. The author thanks Pinar Akmar, Kai-Uwe Kühn, Henning Leupold, Luc Peeperkorn, Vincent Verouden, Wouter Wils and Hans Zenger for helpful comments.

welfare as opposed to total welfare, the leading other candidate as a welfare standard. I furthermore argue that transporting the consumer welfare paradigm into action may lead the practitioner to face difficult choices – and that a literal implementation of the consumer welfare standard at times may seem to make little sense.

The paper does *not* attempt to analyse the position of the European Courts with respect to concepts such as consumer, producer, and total welfare. Rather, I will mostly use examples from Commission Regulations, guidelines and other policy documents as a starting point for my discussion.

As a final point of introduction, let me clarify that in the following 'competition policy' only encompasses antitrust and merger control; the paper is not intended to say anything about state aid control.

2. Consumer Welfare in EU Competition Policy

There are many statements indicating that, seen from the European Commission, modern EU competition policy to a large extent is about protecting consumer welfare. Vice-President Almunia said in a speech shortly after he was nominated commissioner in charge of competition policy that '[a]ll of us here today know very well what our ultimate objective is: Competition policy is a tool at the service of consumers. Consumer welfare is at the heart of our policy and its achievement drives our priorities and guides our decisions.'[2]

The word 'consumers' also appears in official documents. Starting from the top of the hierarchy, consumers are mentioned in the Treaty itself. In Article 101(3) it is stated that the prohibition under Article 101(1) is not applicable to agreements etc. which contribute to 'improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit'. One step down the ladder, consumers also show up in the Merger Regulation.[3] Yet another step down, we arrive at various Commission guidelines and guidance papers

2. Joaquín Almunia, Competition and consumers: the future of EU competition policy, speech at European Competition Day, Madrid, 12 May 2010.
3. 'It is possible that the efficiencies brought about by the concentration counteract the effects on competition, and in particular the potential harm to consumers, that it might otherwise have and that, as a consequence, the concentration would not significantly impede effective competition ...' Recital 29 of Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings (the EU Merger Regulation), OJ L 24/1, 29.1.2004.

where consumers regularly appear. In what Commission officials now call the 'General Guidelines', it is stated that '[t]he objective of Article 81 is to protect competition on the market as a means of enhancing consumer welfare and of ensuring an efficient allocation of resources.'[4] Similar statements, although with some variations, can be found in other Commission guidelines such as the Vertical Guidelines,[5] the Technology Transfer Guidelines,[6] and the Merger Guidelines.[7] Finally, the Commission's Article 102 'Guidance

4. Paragraph 13 in Commission Notice: Guidelines on the application of Article 81(3) of the Treaty, OJ C 101/97, 27.4.2004. The quote continues with '[c]ompetition and market integration serve these ends since the creation and preservation of an open single market promotes an efficient allocation of resources throughout the Community for the benefit of consumers.' The observant reader notices that the paragraph not only mentions consumer welfare but also an 'efficient allocation of resources'. It also says that 'competition and market integration serve these ends'. However, paragraph 105 in the same guidelines says that '[i]n other words, the ultimate aim of Article [101] is to protect the competitive process'.
5. 'The objective of Article 101 is to ensure that undertakings do not use agreements – in this context, vertical agreements – to restrict competition on the market to the detriment of consumers. Assessing vertical restraints is also important in the context of the wider objective of achieving an integrated internal market. Market integration enhances competition in the European Union. Companies should not be allowed to re-establish private barriers between Member States where State barriers have been successfully abolished.' Paragraph 7 of Commission Notice: Guidelines on Vertical Restraints, OJ C 130/1, 19.5.2010.
6. Paragraph 5 of the Technology Transfer Guidelines (Guidelines on the application of Article 81 of the EC Treaty to technology transfer agreements, OJ C 101/2, 27.4.2004) repeats almost ad verbatim the first sentence of paragraph 13 of the General Guidelines. However, there is no such general statement in the Horizontal Guidelines (Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union to horizontal cooperation agreements, OJ C 11/1, 14.1.2011).
7. 'Effective competition brings benefits to consumers, such as low prices, high quality products, a wide selection of goods and services, and innovation. Through its control of mergers, the Commission prevents mergers that would be likely to deprive customers of these benefits by significantly increasing the market power of firms.' Paragraph 8 of the Horizontal Merger Guidelines (Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, OJ C 31/5, 5.2.2004). These 'customers' show up again in various parts of the guidelines (e.g. paragraphs 28-31) while the consumers almost disappear until the section on efficiencies where, for instance, paragraph 79 explains that '[t]he relevant benchmark in assessing efficiency claims is that consumers will not be worse off as a result of the merger.' Essentially similar statements can be found in the Non-horizontal Merger Guidelines (Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings, OJ C 265/7, 18.10.2008).

Paper' places consumers at the centre of the Commission's enforcement policy in the area of exclusionary abuses of dominant positions by saying that '[i]n applying Article [102] to exclusionary conduct by dominant undertakings, the Commission will focus on those types of conduct that are most harmful to consumers.'[8]

It should therefore be clear that 'consumers' play an important part in EU competition policy – at least if judged from various 'hard' and 'soft' law documents. Before I go on, let me immediately deal with – or perhaps rather not deal with – the obvious 'elephant in the room', which is the internal market objective. I know that historically this has been an important part of EU competition policy. And I know that the Courts are attached to this objective and still make references to it in their judgments.[9] However, I will not have that much to say about it here, except that perhaps the fact that it is out there and that the Commission attempts to deal/live with it in a pragmatic way could be seen as another sign that EU competition policy – just as probably the competition policy of most other jurisdictions – at the end of the day has many thoroughly pragmatic aspects to it.

3. Consumers, Consumer Welfare, and Total Welfare

Most of the policy documents (with the exception of the General Guidelines) talk about 'consumers' or 'customers' rather than the expression 'consumer welfare' which Vice-President Almunia used in his speech. Consumer welfare is, however, the concept that economists (and Almunia is an economist (as well as a lawyer) by training) naturally would turn to in order to implement the directions given in these documents.

In economics, consumer welfare is the difference between what consumers would have been willing to pay for a good and what they actually had to pay. It is the 'surplus' that consumers get from buying a good, and the term 'consumer surplus' is therefore often used as a synonym for consumer wel-

8. Paragraph 5 of Communication from the Commission – Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings, OJ C 45/2, 24.2.2009.
9. See, for instance, Joined Cases C-468/06 to 478/06 Sot.Lékos kai Sia and others [2008] ECR I-7139, and Joined Cases C 501/06 P, C-513/06 P, C-515/06 P and C-519/06 P GlaxoSmithKline and Others [2009] I-9291. It can also be argued that the internal market objective had been reconfirmed and strengthened by Protocol 27 of the Lisbon Treaty.

fare. An economist could therefore reasonably understand the quotes given above as indicating that the (main) aim of EU competition policy is to protect consumer welfare or consumer surplus.

For economists, an alternative candidate as a welfare measure would be total welfare or total surplus. The difference between total and consumer welfare is 'producer surplus' – basically the producers' profits. Total welfare may therefore increase in a situation where consumer welfare is decreasing, if the profits of the producers increase more than the decrease in consumer welfare.

The first instinctive reaction of many economists would be to say that total welfare, rather than consumer welfare, ought to be the guiding principle of competition policy. This is what many economists were taught at university: The job of economists is to make the pie as big as possible and then let politicians decide how to divide the pie. If redistribution is needed, this is best done through tax and welfare systems and not through pursuing distributional goals via individual policies. Transported to competition policy, this line of reasoning would say that it is wrong to 'favour' consumers through competition policy, rather than making the pie (total welfare) as big as possible. Another, although related, argument in favour of total welfare is that in western societies, companies are more and more owned by investment and pension funds. This means that the division between consumers and producers is false – or at least blurred – since consumers are also producers (through their investments) and producers are also consumers (possibly in other markets). In such a confused scenario, the argument goes, even if there are valid reasons for redistribution, it seems difficult to achieve anything meaningful through the crude categories of 'consumers' and 'producers' used in competition policy cases.

In debates about whether competition policy ought to use consumer surplus or total surplus as welfare criterion, one can distinguish at least three different positions among economists interested in competition policy. First, those who argue that total welfare ought to be the welfare criterion used, also in individual cases.[10] Second, those who argue that consumer welfare is the

10. See, for instance, Ken Heyer, Welfare Standards and Merger Analysis: Why Not the Best, Competition Policy International, vol. 2, no. 2 (2006), pp. 29-54, and Ken Heyer, Welfare Standards and Merger Analysis Revisited, Competition Policy International, vol. 8, no. 1 (2012), pp. 143-145.

'correct' welfare criterion, for instance because of its distributional effects,[11] and that it therefore should be applied in cases. Third, those who acknowledge that total welfare in theory is the correct criterion, but that there are arguments that can be made why in practice it may be better to use consumer welfare. Since these arguments may not be generally known, I will spend a bit of time on them.

The first argument is a general, well-known one from the public finance literature: Since it is costly to collect taxes – both because of direct administrative costs and of the distortions that taxes introduce – it may be too costly to conduct redistribution through the tax system. Doing it through individual policies – such as competition policy – may therefore be preferable. This argument has, however, been contested; the counter-argument is basically that the distortions coming from pursuing the redistribution through individual policies will be just as large or larger. Since the overall pie to distribute furthermore will be smaller, the best policy is indeed to focus individual policies on maximizing total welfare.[12]

The other line of argument is more specific to competition policy and similar types of regulatory Bodies. The starting point is that a legislator or a government (for simplicity I will use 'government' for both) can assign an 'objective function' or 'operational target' to a competition agency. Assume that the government cares about total welfare. Is it then obvious that it should instruct the competition agency to decide cases on the basis of a total welfare standard? Several papers show that this indeed is not obvious. Taking into account the complexities of the environment in which the competition agency operates, the government may realise that it will actually get closer to maximizing total welfare by telling the competition agency to maximize consumer welfare.

These papers all deal with merger control. One group of papers evolve around the idea that the competition agency does not see all possible mergers, and that the mergers presented to the agency are selected by companies according to the private interests of these companies. The selection of mergers that are presented to the agency will be influenced by the objective function of the competition agency. One classical paper analysing such a situation is

11. See, for instance, Russell Pittman, Consumer Surplus as the Appropriate Standard for Antitrust Enforcement, Competition Policy International, vol. 3, no. 2 (2007), pp. 205-224.
12. See, for instance, Louis Kaplow, On the choice of welfare standards in competition law, in Daniel Zimmer (ed.), The Goals of Competition Law, Edgar Elgar Publishing (2012), pp. 3-26.

Besanko and Spulber (1993).[13] In their model the merging parties have private information about the post-merger (marginal) costs that the competition agency cannot learn. Lower marginal costs increase both producer and consumer surplus (and therefore total surplus). But producer surplus may also increase because of increased market power. Besanko and Spulber assume that there are fixed costs involved in a merger process. Companies therefore only propose mergers to the competition agency that are sufficiently profitable ex post that these fixed costs can be covered. Besanko and Spulber model the decision process at the agency as a simple probability that a proposed merger is prohibited. The agency will determine this probability taking into account the objective function that the government has given it and its expectations about the ex post marginal costs of mergers. What really 'drives' the model is the interaction between the prohibition probability set by the agency and the 'quality' of the proposed mergers. An increase in the prohibition probability will lead companies to propose mergers that on average have lower ex post marginal costs, that is, higher quality. But a higher quality of proposed mergers should lead the agency to lower the probability of prohibiting a proposed merger. Solving the model for this complicated interaction in a situation where the agency is given a total welfare standard shows that companies will propose some mergers that increase producer surplus but not total welfare. Besanko and Spulber show that the government typically will be better off (that is, may maximize total welfare) by giving the agency a 'tougher' objective function which gives more weight to consumer welfare than does the total welfare function.

Lyons (2002)[14] focuses on the fact that a given merger typically will exclude other potential mergers. The mergers that are proposed to the competition authority are chosen by the companies according to their profitability and not according to the resulting increase in total surplus. However, competition authorities are not allowed to prohibit mergers on the grounds that the merger, although on its own increasing social welfare, would prevent another merger from taking place, which would increase social welfare even more. Lyons shows that instructing the competition agency to use a consumer welfare standard may eliminate some mergers which increase total surplus relatively little and force companies to choose among mergers with relatively

13. David Besanko and Daniel F. Spulber, Contested Mergers and Equilibrium Antitrust Policy, Journal of Law, Economics & Organization, vol. 9, no. 1 (1993), pp. 1-29.
14. Bruce Lyons, Could Politicians Be More Right Than Economists? A Theory of Merger Standards, Mimeo, University of East Anglia (2002).

high increases of total surplus. The consumer welfare standard may therefore result in higher total welfare than the total welfare standard.

Another type of argument is presented by Neven and Röller (2005).[15] They consider a situation where a competition agency that has to decide on proposed mergers may be influenced by third parties, and in which the agency is imperfectly monitored. They show that even if a government cares about total welfare it may be better off assigning a consumer welfare standard to a competition agency if the merging parties are willing to use some of their gains from a merger on lobbying the competition agency.[16] In such a situation a competition agency operating with a total welfare standard would be convinced to give too much weight to producer surplus. 'Twisting' its 'objective function' towards consumer welfare may end up with a result better aligned with the government's total welfare objective.

All these models are very stylized, and it is easy to criticize them for lack of realism. Nevertheless, I think that each of them brings something to the debate. And together they make the point that one should not necessarily think that the government should simply give the competition agency the same objective function as the government has. However, it is also true that the papers only show that it *may* be better to instruct the competition agency with a consumer welfare standard even if the government itself uses a total welfare standard. What the papers do not show is that it is better. So there *is* still room for debate.[17]

15. Damien J. Neven and Lars-Hendrik Röller, Consumer surplus vs. welfare standard in a political economy model of merger control, International Journal of Industrial Organization, vol. 23, no. 9-10 (2005), pp. 829-848.
16. Neven and Röller assume that consumers do not lobby in merger proceedings. However, the general intuition would seem to be valid also if consumers are less active or less efficient in lobbying than the merging parties, which can be expected given that their individual interests would likely be smaller and more dispersed than that of the merging parties. Together with Tomaso Duso the two authors in a later paper test empirically whether firms have influence over the merger control process. They find no evidence that either the merging firms or their competitors have any such influence. Tomaso Duso, Damien J. Neven, and Lars-Hendrik Röller, The Political Economy of European Merger Control: Evidence using Stock Market Data, Journal of Law and Economics, vol. 50, no. 3 (2007), pp. 455-489.
17. Interested readers are referred to Heyer, Welfare Standards and Merger Analysis: Why Not the Best; Joseph Farrell and Michael L. Katz, The Economics of Welfare Standards in Antitrust, Competition Policy International, vol. 2, no. 2 (2006), pp. 3-28; and Pittman, Consumer Surplus as the Appropriate Standard for Antitrust Enforcement. Farrell and Katz present in more detail the papers discussed here.

4. Some Practical Issues with Consumer Welfare

I now turn to some practical considerations that can come up when applying the consumer welfare concept.

4.1. Will the Real Consumer Please Stand Up?

The main theme for the first part of this section is the question of who are the 'consumers' that the competition agency is supposed to take into account. In my view, this question seems to have been answered mainly from pragmatic considerations. I hasten to say that I am not at all an enemy of pragmatism. It is just useful to know that there may not be lofty principles behind certain practices, but rather the humble acknowledgement of what is doable in practice and what is not.

So let us search for the 'consumers'. As we saw earlier, some of the policy documents (for instance, the Horizontal Merger Guidelines) seem to swerve between the terms 'consumers' and 'customers'. And in practice it turns out that we should understand 'consumers' as customers rather than 'real' or 'final' consumers. Paragraph 84 of the General Guidelines takes a first step towards clarifying this: '[C]onsumers within the meaning of Article 81(3) are the customers of the parties to the agreement and subsequent purchasers.' Similar expressions can be found in other documents.[18] But the statement is, of course, somewhat misleading. In practice, there is rarely an analysis of what happens to all 'subsequent purchasers'. In a 'horizontal' Article 101 case and in a horizontal merger the competition agency will basically look at what happens to the customers of the 'parties to an agreement' as well as the customers of their competitors.

In a case with vertical aspects such as a vertical merger, a vertical agreement, or an exclusionary abuse of dominance case, the agency will look at what happens to the immediate customers of the 'upstream' company but often also to the customers' customers. This approach is stated clearly in paragraph 16 of the Non-horizontal Merger Guidelines: 'When intermediate customers are actual or potential competitors of the parties to the merger, the Commission focuses on the effects of the merger on the customers to which the merged entity and those competitors are selling. Consequently, the fact that a merger affects competitors is not in itself a problem. It is the impact on effective competition that matters, not the mere impact on competitors at

18. See, for instance, Article 2(b) of the EU Merger Regulation, footnote 105 of the Horizontal Merger Guidelines, and paragraph 16 of the Non-horizontal Merger Guidelines.

some level of the supply chain. In particular, the fact that rivals may be harmed because a merger creates efficiencies cannot in itself give rise to competition concerns.'[19] Downstream firm D2 may not be very happy if one of its suppliers, upstream firm U1, merges with one of D2's downstream rivals, D1. It may quite reasonably fear that U1 will raise the price it charges to D2. It may also think that merger will eliminate a so-called double marginalisation problem between U1 and D1 so that merged entity U1-D1 will operate with a lower marginal downstream cost than D1 did pre-merger. What the quotation from the Non-horizontal Merger Guidelines says is that the Commission will look at the effect of the merger on the customers of D1 and D2, and not at the effect on D2. The reason is that the combined effect of a lower marginal cost of D1 and a higher price to D2 may well be a lower price to the customers of D1 and D2. To be sure, it may also be a higher price, and the task of the agency is to figure out in which situation we are.

Similarly, many of the possible efficiencies of vertical agreements mentioned in the Vertical Guidelines describe how a vertical agreement between, for instance, a manufacturer and a distributor can lead to lower prices or better services for the customers of the distributor. The emphasis of the analysis is clearly on the effects on the customers of the distributor, not on the distributor itself or its rivals.

Most of the cases that the Commission deals with involve companies whose outputs are intermediate products or services and whose customers therefore mainly are other companies (and often even the customers of the customers are companies). Of course, there are also cases with companies whose customers are final consumers, but compared to national competition agencies the proportion of such cases with the Commission is surely considerably lower. So in most of the Commission's cases there are actually no consumers in sight, only customers.

How is it that the 'consumers' mentioned in the Treaty and the Merger Regulation in practice have mutated into 'customers'? Well, this is, of course, to a large extent for practical reasons. It could prove rather difficult to follow the effects of certain upstream agreements, mergers or behaviours as these effects trickle down through possibly several levels before they reach the final consumer. And there does not seem to be a really good reason to try to do so. Except for the situation described above for vertical mergers (and agreements) it is difficult (although not impossible) to imagine that something that

19. A similar statement is found in footnote 2 of the Article 102 Guidance Paper: 'Where intermediate users are actual or potential competitors of the dominant undertaking, the assessment focuses on the effects of the conduct on users further downstream.'

will have anticompetitive effects (e.g. higher prices) at one level will suddenly turn out to have pro-competitive effects (e.g. lower prices) at lower levels, including the final consumer.[20] The effects may peter out before they reach the final consumer, but they will normally not be reversed. So from a practical point of view, it does make a lot of sense to focus at the level immediately below those of the parties.[21]

Note, however, that this is not the same as saying that the agency always can rely on the opinions of the direct customers. This is explicitly recognised in the new US Horizontal Merger Guidelines, which state that '[w]hen direct customers of the merging firms compete against one another in a downstream market, their interests may not be aligned with the interests of final consumers, especially if the direct customers expect to pass on any anticompetitive price increase. A customer that is protected from adverse competitive effects by a long-term contract, or otherwise relatively immune from the merger's harmful effects, may even welcome an anticompetitive merger that provides that customer with a competitive advantage over its downstream rivals.'[22] In fact, it is, in theory, possible that if the customers to the parties of a merger are intermediate producers, *all* of them may be happy to see their input costs increase, since this will increase their profits.[23]

20. There may be situations with complicated effects of a merger, an agreement or a practice on non-linear pricing schemes where this statement may not be true. But this does not seem to me to be a sufficient reason to abandon the general presumption described above. For a different opinion, see Pinar Akmar, 'Consumer' versus 'Customer": The Devil in the Detail, Journal of Law and Society, vol. 37, no. 2 (2010), pp. 315-344.
21. One of the interesting experiences of working in the European institutions is to realise that what seems to be a deep issue in one language may seem much less so in another. Thus the 'consumer' of the English version of Article 101(3) is in the French version an 'utilisateur', rather than a 'consommateur'.
22. US Horizontal Merger Guidelines, p. 5.
23. Sheldon Kimmel, Effects of Cost Changes on Oligopolists' Profits, Journal of Industrial Economics, vol. 60, no. 4 (1992), pp. 441-449. Explaining the full logic behind Kimmel's results is somewhat complicated. However, one example given by Kimmel is when identical firms (which therefore have equal market shares) are engaged in Cournot competition. If there is a constant elasticity of demand, and demand is inelastic, an increase in the marginal costs would increase the profits of the firms. In equilibrium increase prices more than their cost. With inelastic demand the quantity loss resulting from the price increase is not sufficient to offset this margin increase, and profits will go up. For more on this and other examples of when a competition agency should be careful when listening to customers, see Joseph Farrell, Listening to Interested Parties in Antitrust Investigations: Competitors, Customers, Complementors, and Relativity, Antitrust, vol. 18, no. 2 (2004), pp. 64-68, and Ken Heyer, Predicting

Having shown that, in practice, with the usual caveat for vertical mergers and agreements, the Commission will focus on the customers of the companies involved and not on final consumers, the next question that comes to mind is whether this means *all* the customers of the companies and *only* the customers of the companies involved. The last part of the question is easily answered. The Commission clearly focuses not only on the customers of the companies directly involved, but also on the customers of the competitors of these companies. But again, does it take into account what happens to *all* the customers of *all* the competitors? The answer is given in the various policy documents already referred to above. The General Guidelines state that the Commission will look at customers in each relevant market[24] as a group.[25] If this group of customers is not made worse off by an agreement, then the agreement does not violate Article 101. What happens outside a relevant market under investigation is, in principle, irrelevant for the analysis of this particular market.[26] The only exception is if something that happens outside the relevant market benefits *the same customers* as those within the relevant

the Competitive Effects of Mergers by Listening to Customers, Antitrust Law Journal, vol. 74, no. 1 (2007), pp. 87-127.

24. 'The assessment under Article 81(3) of benefits flowing from restrictive agreements is in principle made within the confines of each relevant market to which the agreement relates. The Community competition rules have as their objective the protection of competition on the market and cannot be detached from this objective. Moreover, the condition that consumers must receive a fair share of the benefits implies in general that efficiencies generated by the restrictive agreement within a relevant market must be sufficient to outweigh the anti-competitive effects produced by the agreement within that same relevant market.' General Guidelines, paragraph 43 (footnotes in the text omitted).
25. 'The decisive factor is the overall impact on consumers of the products within the relevant market and not the impact on individual members of this group of consumers.' General Guidelines, paragraph 87.
26. 'Negative effects on consumers in one geographic market or product market cannot normally be balanced against and compensated by positive effects for consumers in another unrelated geographic market or product market.' General Guidelines, paragraph 43.

market.[27] A similar statement can be found in the Horizontal Merger Guidelines.[28]

It seems somewhat difficult to defend the position of the Commission from a 'philosophical' point of view. Why are some customers/consumers (those inside the relevant market) seemingly more important than others (those outside)? Why can't we weigh the harm of customers inside a relevant market with the benefits of those outside the relevant market when we can do it for those inside the relevant market?[29] The issue becomes even more puzzling when one recalls that the concept of 'relevant market' is an abstraction invented for the purposes of competition analysis. There are no relevant markets in the real world. How can such a concept become deciding for which customers count and which don't?

Honest answers to these questions are, in my view, likely to be pragmatic rather than philosophical. I can think of two major arguments. The first argument is the practical difficulty of having an overly 'broad' concept of consumers/customers. This would include an analysis not only of those relevant markets where there would be (significant) competition problems, but also those where there would be small, but not significant competition problems, and those where there would be no imaginable competition problems but where there could be possible benefits to the customers. All the negative and positive effects from the different markets would then need to be added together in order to reach a conclusion. This would in many merger cases involve a detailed analysis of a large number of markets, which likely would involve much larger resources than presently dedicated to such cases. Presented in this way, this does indeed not sound like an attractive option for the Commission – or any other competition agency for that matter – and the restriction of the analysis to relevant markets where there are (possible) competition problems is from a pragmatic point of view understandable. As mentioned earlier, there is an exception to this restriction, which is that the Commission is willing to count efficiencies outside a relevant market if the cus-

27. 'However, where two markets are related, efficiencies achieved on separate markets can be taken into account provided that the group of consumers affected by the restriction and benefiting from the efficiency gains are substantially the same.' General Guidelines, paragraph 43 (footnotes in the text omitted).
28. '[E]fficiencies should (...), in principle, benefit consumers in those relevant markets where it is otherwise likely that competition concerns would occur.' Horizontal Merger Guidelines, paragraph 79.
29. It is accepted that some customers inside the relevant market may be worse off as long as the 'overall impact' on the customers in the relevant market is not negative (see footnote 25).

tomers are the same as those inside the relevant market, the idea being that the customer groups that are harmed should benefit from the efficiencies. This may seem to go against the pragmatic explanation that I give for the rule of generally restricting the analysis to relevant markets with potential competition problems. However, the exception is so particular that it is not likely to be relevant very often, and, if it does become relevant, the two markets are likely to be so closely linked that the analysis may, in the end, not be that much more difficult than the analysis of the 'original' relevant market on its own.

The second argument touches on geographic market definition and what kind of 'contract' the member states have with the European Commission when it comes to competition policy.[30] Have the Member States 'delegated' their choices to the European Commission with the implicit understanding that the Commission will take the same decision as the Member States would have taken if they had decided themselves (leaving aside different capabilities, schools of thought, etc.)? Or have the Member States given the Commission the mandate to make proper 'European' decisions based on the overall European welfare? If the relevant geographic market is national and the first 'model' is correct, then the Commission should indeed look at the customers of each relevant (national) market in isolation, and ensure that they are not harmed. If the second model is correct, the Commission should be willing to allow a merger, agreement or unilateral behaviour to proceed if customers in, say, Germany, are made so much better off that it compensates for losses of customers in other countries.

It is interesting that the United States antitrust agencies seemingly are willing to be more flexible than the Commission. In their horizontal merger guidelines they say that they are willing in their 'prosecutorial discretion' to consider efficiencies from outside the relevant market under consideration if they are 'inextricably linked' with the merger.[31] Basically, US agencies may

30. I first heard the argument made by Damien Neven.
31. 'The Agencies normally assess competition in each relevant market affected by a merger independently and normally will challenge the merger if it is likely to be anticompetitive in any relevant market. In some cases, however, the Agencies in their prosecutorial discretion will consider efficiencies not strictly in the relevant market, but so inextricably linked with it that a partial divestiture or other remedy could not feasibly eliminate the anticompetitive effect in the relevant market without sacrificing the efficiencies in the other market(s). Inextricably linked efficiencies are most likely to make a difference when they are great and the likely anticompetitive effect in the relevant market(s) is small so the merger is likely to benefit customers overall.' (US Horizontal Merger Guidelines, footnote 14.)

therefore accept some consumer harm in a relevant market if it is the only way to get some efficiencies outside the relevant market.[32]

4.2. Abuse of Dominant Position

Early in the Commission's Article 102 'Guidance Paper' it is stated that '[i]n applying Article [102] to exclusionary conduct by dominant undertakings, the Commission will focus on those types of conduct that are most harmful to consumers. Consumers benefit from competition through lower prices, better quality and a wider choice of new or improved goods and services. The Commission, therefore, will direct its enforcement to ensuring that markets function properly and that consumers benefit from the efficiency and productivity which result from effective competition between undertakings.'[33]

Later on it is stated that '[t]he aim of the Commission's enforcement activity in relation to exclusionary conduct is to ensure that dominant undertakings do not impair effective competition by foreclosing their competitors in an anti-competitive way, thus having an adverse impact on consumer welfare, whether in the form of higher price levels than would have otherwise prevailed or in some other form such as limiting quality or reducing consumer choice. In this document the term 'anti-competitive foreclosure' is used to describe a situation where effective access of actual or potential competitors to supplies or markets is hampered or eliminated as a result of the conduct of the dominant undertaking whereby the dominant undertaking is likely to be in a position to profitably increase prices to the detriment of consumers. The identification of likely consumer harm can rely on qualitative and, where possible and appropriate, quantitative evidence. The Commission will address such anti-competitive foreclosure either at the intermediate level or at the level of final consumers, or at both levels'.[34]

This emphasis on consumer harm is evident all through the document, both in the discussion of the analysis of the various types of exclusionary

32. One reason for this difference may be that the fact that the US agencies can rely on their 'prosecutorial discretion' probably makes it easier for them to take such considerations into account than it would be for the European Commission which in many situations has to provide its reasoning in decisions that can be challenged in court.
33. Paragraph 5 of Communication from the Commission – Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings, OJ C 45/2, 24.2.2009 ('Article 102 Guidance Paper').
34. Article 102 Guidance Paper, paragraph 19 (footnotes omitted).

conduct and in the section on efficiencies.[35] However, one can make the argument that the analytical framework endorsed in the Article 102 Guidance Paper actually does not always focus directly on consumer welfare. At least not in the same way that the concept is used in the Horizontal Merger Guidelines – and possibly also in the Horizontal Agreements Guidelines.

In the Horizontal Merger Guidelines the main question is, in principle, fairly simple: Will the prices in the relevant market go up[36] as a result of the merger? The guidelines do not specify a time period within which the prices would have to go up, but I guess that most observers would think it normally should be within a relatively near future.[37] If an agency in a refusal to deal case would ask the question whether prices in the downstream market, at least in the short run, would go down if the agency forced the dominant company to deal with a competitor active or potentially active in the downstream market, the answer in many cases is very likely to be that yes, the prices would go down. Aggressively forcing dominant companies to deal with their downstream rivals would likely be a policy that often would lead to lower downstream prices in the short run and very rarely, if ever, would lead to higher prices.

Yet this is not what the Commission proposes to do in the Article 102 Guidance Paper. On the contrary, the Article 102 Guidance Paper makes it clear that the Commission will only rarely impose an obligation to supply: 'When setting its enforcement priorities, the Commission starts from the position that, generally speaking, any undertaking, whether dominant or not, should have the right to choose its trading partners and to dispose freely of its property. The Commission therefore considers that intervention on competition law grounds requires careful consideration where the application of Article [102] would lead to the imposition of an obligation to supply on the dominant undertaking'.[38]

35. See paragraphs 28-31 of the Article 102 Guidance Paper which discuss 'Objective necessity and efficiencies'.
36. As usual, I use 'increased prices' as shorthand for the various ways a merger can lead to competitive harm. Horizontal Merger Guidelines, paragraph 8.
37. It should, however, be noted that merger control at times sees beyond short-term consumer harm (in the form of higher prices) and takes into account also medium- to long-term consumer harm (for a recent example see Case No COMP/M.6497 Hutchison 3G Austria/Orange Austria, Commission decision of 12.12.2012). One could also, in principle, imagine an efficiency argument that long term dynamic considerations would outweigh short term price increases, but this is very rarely, if ever, accepted.
38. Article 102 Guidance Paper, paragraph 75 (footnote omitted).

The Article 102 Guidance Paper immediately thereafter explains this reluctance to intervene: 'The existence of such an obligation – even for a fair remuneration – may undermine undertakings' incentives to invest and innovate and, thereby, possibly harm consumers. The knowledge that they may have a duty to supply against their will may lead dominant undertakings – or undertakings who anticipate that they may become dominant – not to invest, or to invest less, in the activity in question. Also, competitors may be tempted to free ride on investments made by the dominant undertaking instead of investing themselves. Neither of these consequences would, in the long run, be in the interest of consumers.'[39]

These considerations are in my view eminently reasonable. But they do not seem to have in mind the same type of short term consumer welfare concern that merger control mostly focuses on. Rather the consumer welfare concept used is a long term one taking into account incentives to invest on the part of both the dominant company and the companies asking for the dominant company to supply them.[40]

I should add that there may well be other concerns behind the development of the analytical framework described in the Article 102 Guidance Paper. One could, for instance, imagine that legal concerns of the Courts about respecting private property could be part of the background for the case law that the Article 102 Guidance Paper tries to fit into the framework described above.

Another example is the approach that the Article 102 Guidance Paper takes to what is called 'price-based exclusionary conduct'.[41] The general principle is here that 'the Commission will normally only intervene where the conduct concerned has already been or is capable of hampering competition from competitors which are considered to be as efficient as the dominant undertaking'.[42] This so-called as-efficient-competitor test advocated by the Article 102 Guidance Paper does, in my opinion, not safeguard short-term consumer welfare in the same way as usually done in merger control.

To be concrete, let us consider the canonical price-based exclusionary abuse, predatory pricing. Let's assume that we are dealing with a dominant

39. Article 102 Guidance Paper, paragraph 75.
40. This is spelled out in more detail in paragraphs 86-88 of the Article 102 Guidance Paper.
41. See paragraphs 23-27 for the Article 102 Guidance Paper's general discussion of such abuses.
42. Article 102 Guidance Paper, paragraph 23 (footnote omitted). Paragraph 24 indicates that the Commission may in certain circumstances deviate from this general principle.

company that has only one competitor which it is trying to exclude through aggressive pricing. Let's further assume that the costs of the competitor are higher than those of the dominant company, so that the dominant company can exclude the competitor through pricing above its own but below the competitor's costs. Finally, there is no risk of entry (or re-entry), so after having excluded the single competitor the dominant company increases its price to the monopoly price. It seems quite likely that consumer welfare would be harmed by such a scenario, yet the Article 102 Guidance Paper states that this would not be considered an abuse (or at least that the Commission normally would not intervene).

Although the as-efficient-competitor test in its focus on price-cost comparisons may seem a thoroughly economic test, the explanations for this seeming 'deviation' from a 'pure' consumer welfare standard are, in fact, probably closely related to the fact that competition policy is an administrative legal system. The basics of the test used for predatory pricing in most major jurisdictions come from US antitrust tradition. Indeed, it is commonly known as the Areeda-Turner test.[43] The judgment often considered as the first to outline clearly the thinking behind that test was written by Judge, now Justice, Breyer for the Court of Appeals, 1st Circuit, in *Barry Wright*.[44] The plaintiff in that case argued that 'price cutting by a monopolist may still prove unlawful, even if prices remain above total cost'. Breyer first states that low prices normally are good for consumers and then goes on to explain the logic of tests based on finding that the monopolist prices below costs. Turning then to above-cost pricing, Breyer discusses a test proposed by another Court of Appeals. Here he writes that the 'virtue of [that test] is that it recognizes an economic circumstance in which even 'above total cost' pricing might not be procompetitive and might, in theory, hurt the consumer'. He also notes that economists have identified this type of behaviour as potentially harmful.

Breyer then goes on to the central – and famous – part of the judgment: 'Nevertheless, while technical economic analysis helps to inform the antitrust laws, those laws cannot precisely replicate the economists' (sometimes conflicting) views. For, unlike economics, law is an administrative system the effects of which depend on the content of rules and precedents only as they are applied by judges and juries in courts and by lawyers advising their clients. Rules that seek to embody every economic complexity and qualification may

43. Phillip Areeda and Donald F. Turner, Predatory Pricing and Related Practices under Section 2 of the Sherman Act, Harvard Law Review, vol. 88, no. 4 (1975), pp. 697-737.
44. Barry Wright Corp. v. ITT Grinnell Corp., 724 F.2nd 227 (1983).

well, through the vagaries of administration, prove counter-productive, undercutting the very economic ends they seek to serve. (...) [W]e must be concerned lest a rule or precedent that authorizes a search for a particular type of undesirable pricing behaviour end up discouraging legitimate price competition.'

Breyer then enters into a detailed criticism of the test proposed by the other Court of Appeals, and uses as one argument that 'a price cut that ends up with a price above total costs (...) is almost certainly moving in the 'right' direction (towards the level that would be set in the competitive marketplace). The antitrust laws very rarely reject such beneficial 'birds in the hand' for the sake of more speculative (future low-price) 'birds in the bush'.' In modern academic language, the argument would probably be couched in terms of risks of Type I and Type II errors and the costs of such errors, but the message is the same. If there is a high risk of getting the assessment wrong, and the costs of such an error could be high, it's better to be humble and stick to a safer rule, even if this rule does not exactly map to short term consumer welfare.

One of difficulties of detecting above-cost predation that Breyer mentions is that if the competition agency has to decide whether the dominant company is predating, it will basically have to determine whether the company's prices are profit maximizing. Doing this without a clear, bright line such as pricing below cost (in practice, even this line is often not so clear and bright) is very likely going to be exceedingly difficult. Another option that some might contemplate could then be to use not the costs of the dominant firm, but rather the costs of the competitors as a benchmark. This could, for instance, be done using a test along the lines of 'do not price below the costs of your competitors'. But also such a test would seem to run into problems. As stated recently by the Court of Justice, 'it is necessary to adopt a test based on the costs and the strategy of the dominant company itself'.[45] The Court added that such an approach is 'consistent with the general principle of legal certainty in so far as the account taken of the costs of the dominant undertaking allows that undertaking (...) to assess the lawfulness of its own conduct. While a dominant undertaking knows what its own costs and charges are, it does not, as a general rule, know what its competitors' costs and charges are'.[46]

So we have seen that – just as for refusals to deal – the 'test' for predatory pricing advocated in the Commission's Article 102 Guidance Paper does not

45. Case C-280/08 P Deutsche Telekom ECR [2010] I-9555, paragraph 198.
46. *Deutsche Telekom*, paragraph 202.

strictly correspond to a consumer welfare test – or at least does not cover the same ground as the welfare test used in merger control. But we have also seen that there are good reasons for such an approach.[47]

4.3. Buyer Cartels

The last example I will give concerns buyer cartels.[48] Imagine a situation where there are local upstream procurement markets for a product but a worldwide (very) competitive downstream market for either the product itself or some other product for which the upstream product is an input.[49] Suppose all buyers in a small local procurement market form a cartel to push down the price of the upstream product. Suppose further that the buyers can offer no efficiency explanations (no common logistics, no common marketing, etc.) so that the only effect on the upstream market is that input prices (and possibly also the output volume) are depressed. Since the downstream market is competitive, there will be no discernible effect on prices or output since the local procurement market is small compared to the worldwide market. So there is no measurable consumer harm and hence no reason to intervene if a pure consumer welfare standard is applied. Yet, my guess is that many competition authorities – possibly including the European Commission[50] – would find the behaviour per se illegal.[51] Here the consumer welfare standard taken

47. Farrell and Katz, The Economics of Welfare Standards in Economics, argue that in reality U.S. antitrust policy does not implement a specific welfare standard, but rather 'may prohibit firms from harming consumers and/or efficiency ... only to the extent that firms do so through actions that are deemed anticompetitive'. The definition of what is 'anticompetitive' is therefore, according to Farrell and Katz, not derived from a welfare standard. They further argue that 'the law has evolved toward prohibiting only acts that both (a) hurt competition in an ordinary (if sometimes vague) sense and (b) hurt efficiency and/or consumer surplus. The debate over the so-called 'standard' is the debate over the standard applied in prong (b).'
48. For other discussions of this example see, for instance, Dennis W. Carlton, Does Antitrust Need to be Modernized, Journal of Economic Perspectives, vol. 21, no. 3 (2007), pp. 155-176; Heyer, Welfare Standards and Merger Analysis: Why Not the Best, fn. 28; Pittman, Consumer Surplus as the Appropriate Standard for Antitrust Enforcement; and Gregory J. Werden, Monopsony and the Sherman Act: Consumer Welfare in a New Light, Antitrust Law Journal, vol. 74, no. 3 (2007), pp. 707-737.
49. The typical examples given of such markets are grain, raw materials, etc.
50. After all, Article 101 itself mentions 'fixing' purchase prices as one of behaviours covered.
51. For legal analyses of the case law in Europe, see Ariel Ezrachi, Buying Alliances and Input Price Fixing: In Search of a European Enforcement Standard, Journal of Competition Law & Economics, vol. 8, no. 1 (2012), pp. 47-71, and Ioannis Kokkoris,

at face value would, in my view, give an absurd answer. Such price fixing would seem to be so clearly violating the 'competitive process' that it should be prohibited.

5. Conclusion

With this paper I do not intend to take a firm stand on whether the aim of competition policy ought to be the consumer welfare standard or the total welfare standard – or indeed any other standard, goal, or aim. Rather, my main argument is that it is unlikely that any such goal will be able to be implemented in practice without making compromises based on practical and pragmatic considerations. I have shown that this is the case, for the consumer welfare standard as implemented in EU competition policy. I'm fairly convinced that the same would be true for any other abstract standard/aim/goal.

In all likelihood we will therefore – as said by a former chief economist of one of the US antitrust agencies when discussing welfare standards in antitrust – continue to be in a situation where 'a somewhat murky status quo should muddle along until we understand more'.[52]

Personally, I do not have a problem with this at all. Competition enforcement is an administrative system; practical considerations have to have their say. We cannot expect to have a perfect logically consistent system that fits seamlessly to all situations. The world is too complicated for that. This does not mean that we should give up improving our understanding and perhaps implement changes based on new learning. But I expect most such changes to be (very) incremental, rather than sudden declarations of new directions for EU competition policy.

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