Contribution of
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on
Commission Notice on the definition of the relevant market for the purposes of Union competition law

1. INTRODUCTION

1.1 Section 1.1 should state that: (1) the relevant market is the arena in which the competition at issue occurs, and (2) the relevant market is specified as a range of products and locations (as stated in paragraph 19).

The last sentence of paragraph 1 is the first appearance of a recurring theme that the Commission defines the relevant market to aid in assigning shares (paragraph 9) and assessing market power (paragraphs 1, 7–8). Defining the relevant market, however, serves a larger, analytic purpose, which section 1.1 should state. US competition law operated for almost six decades without the relevant market, but eventually required it to assess competitive effects from mergers.

As paragraph 14 implies, defining the relevant market separates the active forces of competition with relatively direct and immediate effects on performance from passive forces and from active forces lacking direct and immediate effects. Competition law followed the practice of economics (pioneered by Alfred Marshall) by using this separation to bring analytic order to real-world chaos. Formal economic modeling in competition cases also makes this separation. See Gregory J. Werden, The Relevant Market Concept in Antitrust Law, in Global Antitrust Economics: Current Issues in Antitrust Law & Economics 117 (Douglas H. Ginsburg & Joshua D. Wright, eds. 2016); Gregory J. Werden, Why (Ever) Define Markets? An Answer to Professor Kaplow, 78 Antitrust Law Journal 719 (2013).

The last two sentences of paragraph 2 indicate that the Commission is updating its guidance on the relevant market because of changes in the economy, but the Commission is not merely inserting new material prompted by digitalization and globalization, nor should the Commission limit itself that way. Paragraph 2 also should mention new economic learning and the Commission's accumulated experience with old economy industries.

Paragraph 4 concerns 'increased predictability,' which should be the Commission's aim. The much of the Notice, however, merely says that the Commission does what makes sense under the circumstances of individual cases. Stating a rationale for particular choices can achieve 'increased predictability,' but rules or principles should be cited when possible. The comments below identify specific paragraphs in which the Commission should try to provide more guidance.

1.2 Paragraph 5 makes the first text reference to 'competitive constraints,' but the term is not explained until paragraph 25. Paragraph 5 should contain either a cross reference to paragraph 25 or much of its current content.

Paragraph 5 contains a misleading sentence from the 1997 Market Definition Notice: 'The main purpose of market definition is to identify in a systematic way the immediate competitive constraints that the undertaking(s) involved face when offering certain products in a certain area.' Paragraph 5 should say that market definition identifies which constraints operate inside the relevant market and which constraints operate from outside it, much as paragraph 14 indicates.

Section 1.2 should mention the analytic role of the relevant market in providing the framework for competitive analysis, including formal economic modeling. Paragraph 8, particularly the second subpoint, could be expanded to mention this.

1.3 Paragraph 12 focuses on what 'consumers consider relevant,' but what competitors do is more important and easier to ascertain. The Commission's focus on consumers could be taken as an indication that it defines relevant markets on the basis of how it thinks competition should work, rather than on the basis of how competition actually does work.

Despite using the word 'may,' the first subpoint of paragraph 15 greatly exaggerates the extent to which competition 'in product improvement' is separate from price competition. The two competitions necessarily involve the same products and the same suppliers. Footnote 25 makes a distinct point relating to future products, which necessarily differ from current products and could have different suppliers.

2. CONCEPT OF THE RELEVANT MARKET AND GENERAL METHODOLOGY

2.1 The contents of paragraph 19 would be helpful to readers of the Introduction. Paragraph 19 could instead define the terms 'relevant product market' and 'relevant geographic market.'

Paragraph 20 states: 'The relevant product market comprises all those products that customers regard as interchangeable or substitutable to the product(s) of the undertaking(s) involved . . . .' This statement appears to define 'relevant product market,' and footnote 38 calls it a 'definition.' Critically, this 'definition' refers only to substitutability on part of customers, consistent with the US practice of defining the relevant market on the basis of demand substitutability alone (accounting for supply substitutability in identifying competitors).

Paragraph 20, however, is not meant as a definition, which should be indicated by its wording and that of footnote 38: Paragraph 25 states that: 'Supply substitution can also be relevant for the definition of the relevant market . . . .' And paragraph 26 states that: 'The assessment of demand and supply substitution helps identify the products in the relevant market . . . .'

Paragraph 21 states: 'The relevant geographic market comprises the area in which the undertaking(s) involved supply or demand relevant products, in which the conditions of competition are sufficiently homogeneous and which can be distinguished from neighbouring geographic areas, in particular because conditions of competition are appreciably different in those areas.' This statement is flexible enough that the relevant geographic market could refer to the locations of the market's customers, to the locations of the market's suppliers, or to both.

US practice is to define relevant geographic market around supplier locations unless the market is defined on the basis of price discrimination. Paragraph 88 hints at this practice, but the Notice otherwise is to the contrary. The Notice should clearly state the Commission's practice. The practice should not invariably be to define the relevant geographic market around customer locations, without regard to whether price discrimination is feasible.

2.2 Paragraph 26 states: 'To provide a useful framework for the competitive assessment, market definition must also identify the customers that are likely to face similar effects of the conduct or concentration in question. Accordingly, the Commission focuses on the degree to which customers face similar or differing conditions of competition when it decides on which customers are included in the relevant market.' To provide the necessary framework, however, market definition must identify suppliers imposing immediate competitive constraints. When price discrimination is infeasible, focusing on customers has no evident utility.

2.2.1.1 Paragraph 27 states: 'Where there is sufficient demand substitution between the products of different suppliers, the Commission includes those products in the same relevant product market.' But Paragraph 29 observes that the issue is not whether products A and B are in the same relevant market, but rather whether product B is in the relevant market defined for product A. Asymmetric substitution can cause B to be in the market defined for A, even if A is not in the market defined for B. As indicated by paragraph 30, the focal product in defining the relevant product market is a product of a firm of interest.

Paragraph 29 states that the Commission examines evidence on the extent to which customers 'would switch in response to a deterioration in the supply situation of the products of the undertaking(s) involved relative to other products.' The paragraph explains that the Commission 'usually focuses on reactions to price increases' but might consider changes in 'quality or level of innovation.' The latter practice, however, is neither grounded in economic theory nor consistent with the Notice's statement (paragraphs 5–6, 14, 24–25) that definition of the relevant market focuses on 'immediate' competition. Innovation competition is never immediate, and quality competition can work just like innovation competition.

Paragraph 30 states that products are added to a candidate market 'in decreasing order of the degree to which the customers would substitute the products of the undertaking(s) involved with these alternative products.' But several distinct metrics that can gauge this 'degree.' The choice among metrics can matter, and the best choice is the 'relative diversion ratio'—the diversion ratio divided by the ratio if diversion were proportionate to market share. See Gregory J. Werden, Demand Elasticities in Antitrust Analysis, 66 Antitrust Law Journal 363, 405 (1998).

Paragraph 31 states that the Commission asks 'whether a hypothetical monopolist in the candidate market would find it profitable to implement a small but significant non-transitory increase in price.' The question to ask in applying the hypothetical monopolist test (HMT), however, is whether the profit-maximizing price increase for a hypothetical monopolist's would be significant. See Gregory J. Werden, Market Delineation under the Merger Guidelines: A Tenth Anniversary Retrospective, 38 Antitrust Bulletin 517, 537–39 (1993). Paragraph 31 notes the connection between the HMT and the market power concern of competition law, and that connection is broken when an arbitrary price increase is posited.

2.2.1.2 Paragraph 35 gives 'necessary conditions for the market to be broadened based on supply substitution.' The structure of the Notice suggests that the Commission's practice is to account for supply substitution in market definition if the necessary conditions are met, unless reasons mentioned paragraphs 38–39 apply. The Notice should clearly state whether this is the Commission's practice.

If the Commission's practice cannot be reduced to a simple rule, the Notice should say that. Several considerations not mentioned in the Notice might matter. One recurring complication is heterogeneity across competitors in the range of products over which supply substitution occurs. This heterogeneity is seen, for example, with hospitals, and US practice generally has been to aggregate a range of services common to merging hospitals.

Another complication is interaction between demand and supply substitution. Suppose that two merging firms produce X and that firms now producing Y can easily switch to X. Also suppose Y has good substitutes in demand, causing the X+Y candidate market to fail the HMT, even though X has no demand substitutes. US practice has been to define the relevant product market as X and assign shares to producers of both X and Y based on their capacity to produce X (and perhaps also their profitability of doing so).

2.2.2 Article 9(7) of the 2004 Merger Regulation states:

> The geographical reference market shall consist of the area in which the undertakings concerned are involved in the supply and demand of products or services, in which the conditions of competition are sufficiently homogeneous and which can be distinguished from neighbouring areas because, in particular, conditions of competition are appreciably different in those areas. This assessment should take account in particular of the nature and characteristics of the products or services concerned, of the existence of entry barriers or of consumer preferences, of appreciable differences of the undertakings' market shares between the area concerned and neighbouring areas or of substantial price differences.

The 1989 Merger Regulation contained a nearly identical provision, but the 1997 Market Definition Notice did not discuss it at length.

Paragraph 40 of the Notice states that the Commission takes a location of affected customers as a starting point 'then analyses whether the conditions of competition' in that location 'are sufficiently homogeneous' and 'can be distinguished from neighbouring areas because the conditions of competition are appreciably different in those areas.'

The 'sufficiently homogenous' notion originated in the *United Brand* judgment, in which the Court of Justice cited heterogeneity across member states in customs duties for banana imports. Complete homogeneity in the conditions of competition evidently exists when there are no trade barriers and no transport costs (and it also might require a homogeneous product). '[S]ufficiently homogeneous' 'conditions of competition' are difficult to specify because no legal or economic literature articulates a homogeneity metric or a sufficiency standard.

'[S]ufficiently homogeneous' 'conditions of competition' also are difficult to specify because the Merger Regulation does not state the purpose such conditions serve. The *United Brands* judgment used the more complete expression: 'sufficiently homogeneous for the effect of the economic power of the undertaking concerned to be able to be evaluated.' Much as the Court of Justice did, the Commission should specify the consequence for the competitive assessment of insufficient homogeneity.

The Commission's contribution to a 2016 OECD roundtable, asserted that, in the merger context, the 'key question' under the 'sufficiently homogeneous' criterion is whether 'competitors from other geographic areas will be able to exercise sufficient competitive pressure on the merging companies.' In this way, the Commission reconciled the notion of 'sufficiently homogenous' with the economic insight that substitution at the margin in response to price changes is what matters. The Notice could undertake a similar reconciliation.

The HMT can be applied to geographic market definition, and the US agencies apply it. Footnote 57 of the Notice hints that Commission does as well. If so, the Notice should emphasize that fact, yet the rest of the Notice gives no suggestion that the Commission applies the HMT in geographic market definition.

Paragraphs 43–44 address the scenario in which the EEA imports the relevant product because internal production does not satisfy demand. With significant transport costs, '[c]ustomers located in the area where the imports originate [always could be said to] face different conditions of competition compared to customers located in the area where imports are delivered.' On that basis, the Notice indicates that defining the relevant geographic market to 'include in the relevant market customers who would likely be affected differently . . . would hamper rather than facilitate the competitive assessment.'

Case law does not mandate the Commission's practice. Applying the 'sufficiently homogeneous' notion, the Court of Justice endorsed the Commission's definition of relevant geographic markets in which 'one-way trade flows' were prominent.

Judgment of 31 March 1998, French Republic and Société Commerciale des Potasses et de l'Azote (SCPA) and Entreprise Minière et Chimique (EMC) v Commission, joined cases C-68/94 and C-30/95, EU:C:1998:148, paragraph 136.

What would 'facilitate the competitive assessment' in some cases is defining the relevant geographic market around supplier locations. Paragraph 44 asserts that the Commission 'fully takes into account the competitive constraint from imports in the relevant market,' but that constraint sometimes can be reflected fully in market shares assigned at the point of production and only with a relevant geographic market defined to include the origin of constraining imports.

The Notice should address asymmetric geographic markets. The Notice poses the question of whether location A and location B are in the same geographic market, but what the Commission typically asks is whether the relevant market containing A (typically the EEA or a member state) also extends to some outside location B. The relevant market for A can include B even of the relevant market for B does not include A. This is apt to be true when B exports to A.

3. PROCESS OF DEFINING MARKETS

3.2 Paragraph 52 exaggerates the utility of substitution evidence generated by natural experiments. A cost shock affecting just a focal product (around which the market is delineated) could be very useful, but such events are exceedingly rare, and the Notice provides no illustrative case. The paragraph also cites a new product launch, but one cannot infer relevant demand elasticities from such an event. Even if new product X took all of its customers from Y, X and Y could be poor substitutes at the margin in the post-entry world.

Footnote 72 should provide a solution to the puzzle it presents. How can there be 'high diversion ratios or (cross-price) elasticities to products outside the candidate market' yet the relevant market does not include such products? The 'circle principle' holds that the relevant market must include any substitute for the focal product that at least as close as any included product. The circle principle is followed in the US, and the Notice should say whether the Commission follows it.

Paragraph 55 should explain how the Commission accounts for 'the expected changes in substitution possibilities resulting from the change in competitive dynamics' within 'rapidly evolving industries.' With no explanation, the paragraph can be read to suggest that the Commission speculates.

Paragraph 59 endorses a critical loss analysis that does not implement the HMT. It is an analysis that merging firms have long advocated in support of a broad definition of the relevant market. Paragraph 59 posits an arbitrary price increase that could be less than the price increase from a proposed merger. And paragraph 59 asks only whether the arbitrary price increase is more profitable than none at all, when a larger or smaller price increase would be profit maximizing.

The General Court is apt to get confused if the Commission relies on critical loss analysis. Despite considerable experience and scholarship, critical loss analysis remains a matter of substantial confusion in US litigation. See Gregory J. Werden, The Hypothetical Monopolist Test in *Sysco*: A Litigation Muddle Needing Analytic Clarity, 12 Journal of Competition Law & Economics 341 (2016).

Rather than compare critical loss to a projected actual loss, the HMT generally can be implemented by comparing the critical elasticity of demand for a candidate market with a projected actual demand elasticity. See Gregory J. Werden, Demand Elasticities in Antitrust Analysis, 66 Antitrust Law Journal 363, 391–96 (1998).

No variation on the theme of critical loss can implement the HMT under supply and demand conditions observed in some cases. It can be necessary instead to model the hypothetical monopolist's profit maximization using realistic cost and demand curves. See Gregory J. Werden, Beyond Critical Loss: Tailored Application of the Hypothetical Monopolist Test, 4 Competition Law Journal 69 (2005).

3.3 Paragraphs 62–75 concern evidence used to define geographic markets, and they make use of the 'sufficiently homogeneous' notion. The discussion makes the Commission's practice appear arbitrary because it does not articulate principles grounded in the market power concerns that animate competition law.

Paragraph 64 states that 'when the market shares of [the same] suppliers vary substantially across different areas, this typically indicates that conditions of competition in these areas are not sufficiently homogeneous' to place 'these areas in the same relevant geographic market.' Such differences, however, cannot negate the possibility that areas are strongly connected. Paragraph 74 observes that suppliers have an advantage in serving nearby customers when transport costs are substantial. Absent price discrimination, all competition occurs on the margins, and geographic market definition should focus on that competition.

Paragraph 69 asserts that: 'when the set of products which customers regard as substitutes to the products of the undertaking(s) involved differs between geographic areas, this is generally a strong indication that conditions of competition are not sufficiently homogeneous for those areas to belong to the same geographic market.' This presumes geographic markets defined around customer locations and appears to presume price discrimination. If price discrimination is infeasible, the geographic market should be defined around supplier locations, in which case customers in a relevant market could have widely varied preferences.

Paragraphs 73–74 discuss the definition of relevant geographic markets in the presence of spatially differentiated customers and suppliers, as well as significant transport costs. Paragraph 74 indicates that the Commission's practice is to define relevant geographic markets encompassing 70–90% of the consumption from a point of supply. The Commission's practice, however, can prove problematic.

The process of defining the relevant geographic market is meant to identify suppliers that are close competitors, and the process often works best if the relevant geographic market is defined around supplier locations. A supplier's relevant market can be far larger than the area encompassing 70–90% of its customers, and a supplier's relevant market need not contain any of the customers served. See Gregory J. Werden, Market Delineation and the Justice Department's Merger Guidelines, 1983 Duke Law Journal 514, 555–64; Gregory J. Werden, On the Use and Misuse of Shipments Data in Defining Geographic Markets, 26 Antitrust Bulletin 719 (1981). These insights and the overarching market power concern of competition law inspired development of the HMT. See US Department of Justice, Antitrust Division, Competition in the Coal Industry 26–27 (May 1978).

4. MARKET DEFINITION IN SPECIFIC CIRCUMSTANCES

4.1 Paragraph 84 defines 'differentiation' to include all instances of product or location differences that matter, which includes nearly every case. Paragraph 86 then states: 'When products are differentiated, market shares may provide a less reliable indicator of market power.' The Commission should narrow the definition of 'differentiation' or limit Paragraph 86, perhaps to just consumer products.

4.2 This section should indicate whether the Commission sometimes treats each customer, or even each transaction of each customer (in a procurement setting), as a distinct relevant market. Doing so can be appropriate.

4.3 Paragraphs 89–93 discuss market definition with 'significant investments in R&D.' Paragraph 90 states that the Commission defines ordinary product markets for pipeline products, while Paragraphs 91–93 indicate that the Commission might do something different in other scenarios. The Commission should clarify its practice, which should be to define ordinary product markets (possibly for future products) unless competitors sell technology rather than products.

4.4 Paragraphs 94–98 discuss market definition with 'multi-sided platforms.' Paragraph 95 states that the Commission might, and might not, combine multiple sides in a single relevant market. The Commission is wise not to take an absolutist position because platforms compete in different ways in different contexts, but the Commission should state its general inclinations. Cross-platform feedback does not justify combining multiple sides, but that is appropriate if individual platform customers make use of all sides combined into a single relevant market.

Paragraphs 97–98 discuss platforms with a nominal price of zero on one side. The Commission is correct to say that a relevant market can be defined for a no-revenue product, but it does not follow that abuse of dominance over a no-revenue product can be analyzed just as with any other market. The owners of platforms built around no-revenue products need scope to monetize their platforms through activities involving revenue-generating products. The Notice should not get into the competitive assessment of abuse cases with two-sided platforms, but it should state that the Commission pays careful attention to cross-platform feedback in defining the relevant market and in the ensuing competitive assessment.

Paragraph 98 (also paragraph 32 and footnote 47) suggests that the HMT cannot be applied in defining the relevant market for a no-revenue product and indicates that the Commission might use an alternative to the HMT positing an arbitrary reduction in quality. But any such an alternative has only a superficial resemblance to the HMT because it ignores how market power is exercised and against whom.

In market economies, one always should follow the money in trying to understand how economic actors behave. The owner of a platform built around a no-revenue product exercises market power just as anyone else—by raising price or restricting output for a revenue-generating product. See Gregory J. Werden, The Foundations of Antitrust: Events, Ideas, and Doctrines 355–59 (2020).

In principle, the HMT can be applied rigorously to a platform built on a no-revenue product. Consider a free service supported by advertising: The platform owner's problem is to select an optimal price and quantity for advertising while managing the free service in a manner that optimizes the value of the platform to advertisers. The platform owner accounts for the impact of advertising on usage of the free service, and for the impact of free-service usage on the value of advertising. All this can be modeled, at least in theory.

In exercising market power, the platform owner almost certainly would reduce the quantity of advertising provided, which would increase the quality of the free service. The arbitrary imposition of a 'small but significant non-transitory decrease of quality' would both go the wrong direction and focus on the wrong product.

5. MARKET SHARES

Paragraphs 104–11 discuss how the Commission has assigned shares in a variety of circumstances, but they should say more about the Commission's rationale.

The proper assignment of shares depends on whether the relevant market is defined around supplier or customer locations. When the relevant market is defined around the locations of suppliers, shares should be assigned at the point of production. When the relevant market is defined around the locations of consumers, shares should be assigned at the point of consumption.

Paragraph 104 appears to state that the Commission always assigns shares at the point of consumption. The reason might be that the Commission always defines the geographic market around the locations of consumers. In some cases, however, a better approach is to define the geographic market around locations of suppliers.

The marginal supplier in the EEA can be located outside. In such instances, shares assigned on the basis of sales in the EEA is apt to understate the significance of the outside supplier that sets the market price. A marginal supplier accounting for a small fraction of sales in the EEA could wield power over price in the EEA commensurate with that associated with a dominant market position. Although the Commission can make correct enforcement decisions using misleading market shares, it cannot achieve 'increased predictability,' which is the goal of the Notice.

Paragraph 106 states: 'The Commission usually relies on market shares based on sales. Conversely, in procurement markets, the Commission usually relies on market shares based on purchases.' The reference to 'procurement markets' might have been intended as a reference to 'purchasing markets,' defined in paragraph 6.

Paragraph 106 states that 'both the value of sales or purchases and the volume of sales or purchases provide useful information,' yet the Commission 'usually relies on market shares based on sales' (meaning revenue). Paragraph 108 states that, with significantly heterogeneous products, the Commission 'usually' uses revenue-based shares, although in some cases, doing so could 'underestimate the competitive importance' of merging firms 'offering a product at a much lower price than others.' The Commission should explain its thinking more fully, lest the reader infer that the Commission does whatever results in the highest market shares for the parties of interest.

Paragraph 107 usefully observes that the best means for assigning shares depends on a variety of factors and can be idiosyncratic. The Notice, however, does set out general principles. The Commission should consider articulating principles such as these:

- The basis for assigning market shares depends on the facts of each case, and unique facts can cause shares to be assigned on a unique basis.
- Practicality is paramount: the basis for assigning shares must be objectively observable and measured in a reasonably consistent manner across competitors.
- Shares are assigned on a basis that serves as a common denominator, so sales revenue is an obvious choice, although another output-based measure sometimes is preferred.
- When past output is not indicative of future competitive significance, an asset-based measure of capability, such as productive capacity, is used.

See Gregory J. Werden, Assigning Market Shares, 70 Antitrust Law Journal 67 (2002).

Paragraph 109 refers to the Commission's practice of focusing on shares within 'segments of the relevant market,' and it should indicate how the Commission justifies this practice. If the segments are not themselves relevant markets, segment shares should not be employed in assessing competition, but they can be useful in describing an industry.