Chapter 14
EU Competition and State Aid Policy

Overview

- Competition policy:
  - Anti-competitive conduct
  - Abuse of dominance
  - Merger control

- State aid policy (subsidies)
  - Restructuring prevention
  - Unfair competition

Relevance

- Exclusive competency of EU
  - Commission controls

- Justification for putting competition policy at the EU level.
  - Need belief in 'fair play' if integration is to maintain its political support
  - Negative effects of one Member's subsidies on other Members' industry

- Concerns:
  - "As the number of firms falls, isn't there a tendency for the remaining firms to collude in order to keep prices high?"
  - "Since industrial restructuring can be politically painful, isn't there a danger that governments will try to keep money-losing firms in business via subsidies and other policies?"

- Answer: "Yes"

EU Competition Policy

- Antitrust and cartels. The Commission tries:
  a) to eliminate anti-competitive conduct (e.g. price-fixing arrangements and cartels). (Article 81 EC Treaty)
  b) to eliminate abusive behaviour by firms that have a dominant position. (Article 82 EC Treaty)
  - Ex post regulation (reactive)
  - Behaviour of firms

- Merger control. The Commission seeks:
  - to block mergers that would create firms that would dominate the market.
  - Ex ante regulation (proactive)
  - Structure of market

Economics of cartels

- Suppose price without cartel would be \( P = AC \).
- Cartel raises price to \( P' \).
- \( \Delta \) Consumer Surplus = \( -a - b \);
  \( \Delta \) Profit = \( a \)
- Net welfare effect: \( -b \)
- Outcome: 'ripoff' + inefficiency effect

Cartels

- Common types of prohibited agreements:
  - Price-fixing (sale or purchase)
  - Exchange of certain confidential information
  - Limiting production
  - Sharing markets or sources of supply
  - Bidding cartels

- Efficiency defence:
  1) The agreement creates economic efficiencies
     - Economies of scale
     - Lower transaction costs (e.g. better coordination)
     - Product development (avoid duplication)
  2) It is the only way of obtaining those efficiencies
  3) It also benefits consumers
  4) It does not eliminate effective competition from a significant part of relevant markets
Case: Cement manufacturers

- European-wide building materials cartel, fined in 1994
- National cartels too: Germany (2003), Poland (2009), France (2007)
- New case: numerous participants (from Austria, Belgium, the Czech Republic, France, Germany, Italy, Luxembourg, The Netherlands, Spain, and the UK)
- Claims: restrictions of imports into the EEA from countries outside the EEA, market sharing, price coordination and connected anticompetitive practices
- Investigation started in December 2010.

Abuse of dominant position

- 2 questions:
  1. Is there a dominant position?
  2. Has it been abused?
- (1) Dominance =
  a) Significant control over price level
  b) Significant control over terms of delivery
  c) Other significant influence over competitive conditions
- Rules of thumb: market share
  - Below 40% → no dominant position
  - 40–60% → grey area (depends on entry barriers etc.)
  - Over 60% → dominant position
- Concept of relevant market (not precise)

Abuse of dominant position

- (2) Abuse =
  A. Pricing practices
     - Unfair pricing (considerable monopoly power)
     - Price discrimination (without acceptable reason)
     - Predatory pricing (pushing competition out)
  B. Non-pricing practices
     - Refusal to deal (without acceptable reason)
     - Tying (2 distinct products, without acceptable reason)
     - Exclusive sales or purchasing agreements (without acceptable reason)
Case: Deutsche Telekom

- Until liberalization in 1996, Deutsche Telekom enjoyed a legal monopoly in retail fixed-line telephone markets in Germany.
- Afterwards: dominant position.
- Concern: “margin squeeze” – charging competitors prices for network access services that were higher than the retail prices of Deutsche Telekom’s end-users
- Fine: €12.6 million

Case: Microsoft

- Refused to supply information that other firms needed to update their products so as to make them compatible with new versions of Windows
- Also harmed competition by tying its separate Windows Media Player to its Windows PC operating system
- Some issues:
  - Economics: differing opinions & theories (were consumers harmed?)
  - Efficacy: are the fines enough?
    - Microsoft didn’t obey and was fined 3 times (total €1.7 billion)
    - Low probability of ‘getting caught’

Merger control

  - Ex ante regulation (proactive)
    - “a concentration that would significantly impede effective competition in the common market”
- Clearance procedure:
  a) Full acceptance
  b) Acceptance with conditions (e.g., Sale of a unit, IPR licensing)
  c) Prohibition
- Lots of cases all the time
- Economies scale → efficiency defence?
  - Oliver Williamson (Nobel Prize 2009)

Criticism of competition policy

- Heavy, expensive procedures
- Uncertainties
- Delays (M&A)
- Fines not strong enough?
  - ‘Low probability of getting caught’
- European competition law ignores economics?
  - ‘Protects competitors, not consumers’

State aid economics

- 1957 Treaty of Rome bans state aid that provides firms with an unfair advantage and thus distorts competition.
  - Commission to enforce
  - Exceptions (social policy, natural disaster aid, economic development aid to regions)
  1. Restructuring prevention
  2. Unfair competition
(1) Restructuring prevention

- Idea: all states pay **subsidies** to prevent restructuring
  - **Short term:**
    - Taxpayers support inefficient firms
    - Still better than not opening markets
  - **Long term:**
    - Closer ties between firms and state \(\rightarrow\) politics, danger of corruption
    - Unhealthy, stagnant business culture \(\rightarrow\) firms likely to fall behind in international competition

(2) Unfair competition

- One/Some states pay subsidies to protect national firms
- Other states don’t pay \(\rightarrow\) firms more likely to fail
- Unfair
- Danger of escalation (all start to protect)
- Example: airlines