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Chapter 1

Introduction

European competition policy is one of the success stories of the European integration process. This is not to say, however, that the policy always works effectively; that it is always transparent and legitimate; nor indeed that its constituents and stakeholders universally approve of the framework which structures the policy, the procedures that govern its implementation, or the way it is enforced from day to day. Nevertheless, European competition policy is perhaps the most supranational of all EU policies and has become something of a flagship for the EU. For that reason alone it is important for students of European integration and EU politics, among others, to engage with this policy area.

But there are other reasons too. Competition among firms is central to the effective functioning of market economies. Competition policy therefore constitutes a crucial instrument of regulation for governments (or in our case, the EU) keen to ensure that a competitive environment persists. This is particularly important since firms may wish to dominate or fix markets, undermining competition in the process. However, competition policy may serve a variety of ends, and even where the stated policy goal is the maintenance or encouragement of competition, there are a number of different ways such a general ambition may be translated into a workable policy and subsequently enforced.

Where the regulator is not a government but a supranational institution, the formulation and implementation of competition policy is yet more complex. In the case of the European Union, which is the subject of this study, it is the European Commission which takes the lead both in shaping and in setting the policy, and also in establishing the parameters within which it is applied in practice. Even though certain aspects of policy enforcement have been decentralized, and despite the fact that the Commission now sits within a network of competition actors and institutions to which it has delegated some of its earlier responsibilities, it remains the dominant player in the European competition policy game.

This short introduction offers some basic information about

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competition, competition policy and, more specifically, European competition policy, providing a contextual foundation for the chapters that follow. The first section begins by examining the meaning of competition, and then goes on to unpack what competition policy is. The second section introduces the key elements of European competition policy, and focuses on four themes that highlight the ways the policy has evolved since the 1980s. The final section explains the organization of the book.

Competition and competition policy

The belief that economic competition is a good thing is something of an act of faith in countries where the economy operates on the basis of free-market principles. The commitment to competitive markets is rarely questioned, although the pervasive pro-competition rhetoric reflects more of an aspiration than a reality.

Competition has been defined as the ‘struggle or contention for superiority, [which] in the commercial world ... means a striving for the custom and business of people in the market place’ (Whish 1989:3; see also Bishop and Walker 2002; van den Bergh and Camasasca 2006). However, it is not always clear whether it is competition itself, or the function that competition is said to perform, which justifies its status as the most important organizing principle in the capitalist world. Theoretically speaking, in the language of neo-classical economics, this function is explained by the theory of perfect competition, where many small firms compete in the supply of a single product and where no one firm can affect prices or conditions of sale. The theory demonstrates how, in conditions of perfect competition, consumer welfare is maximized. It also shows how this leads to allocative, productive and distributional efficiency, allowing goods and services to be supplied in exactly the form and quantities desired by consumers and at the lowest cost possible. At the same time, monopoly, where there is only one supplier, is shown to restrict the supply of goods and services, and to charge higher prices. Thus, while competition ‘magically and surreptitiously orders society’s resources in the optimal way’ (Whish 1989:7), monopoly is deemed to be the epitome of inefficiency.

However, even Adam Smith, with his talk of the ‘invisible hand’ of the market, recognized that competition was an abstract notion

which could not exist in its purest form in the real world. Moreover, competition may even create as many problems as it solves. But although there can be some uncertainty about the merits and demerits of competition, there is all the same an acceptance within market economies that the advantages of competition generally outweigh the disadvantages. Rather than relying on some abstract notion of perfect competition, however, the looser concept of ‘workable competition’ has become the benchmark by which markets are assessed (Clark 1940; Sosnick 1958). This is theoretically a much vaguer notion, but one which is much more grounded in the real world. Competition within markets – even workable competition – should not be taken for granted, however. As Doern and Wilks (1996:1) have affirmed, ‘[n]either competition nor the market is inevitable or natural. Markets have to be created through processes of social change and public regulation’ and while there is indeed some consensus that competition is a good thing, there is little agreement about what ‘workable competition’ implies in concrete policy terms.

Competition policies allow for the development of a regulatory framework within which governments can maintain or encourage competition. Such policies are clearly based on an assumption that enhanced economic performance will ultimately result from such an approach. Competition policies are deemed to be necessary, as firms (and indeed governments) sometimes behave in a manner which is harmful to competition. They do this for a number of reasons. Industrial actors often perceive competitive pressure as a constraint upon their freedom of manoeuvre. Competition causes uncertainty, and anti-competitive behaviour is one way of making the future more predictable. In addition, firms may also be keen to increase or maintain their profit margins. By acting collusively or by abusing a dominant market position, they may be able to charge higher prices and reap substantial gains. Competition policies are therefore drafted to prevent, deter or persuade firms from acting in such a fashion. They are negative policies, in the sense that they seek to *prevent* rather than to *promote* certain activities, so that it is by limiting the extent of anti-competitive practice, rather than by more positive means, that competition is encouraged.

So far, it has largely been taken for granted that the rationale behind *competition policy* is a desire to promote *competition* and thus consumer welfare. This may not always be the case, as competition policies can serve a multitude of different ends. While almost

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all policy-makers will happily agree that there is a need for structures and procedures which protect and maintain competition, the many different policy options on offer demonstrate the potential for disagreement over the objectives and functions of these structures and procedures, and in particular over the extent to which cooperation rather than competition ought to be encouraged. This is what makes the formulation of competition rules so controversial. Rules may be drafted in such a way as to leave few options open to the policy-maker, though this is rare. More often than not, a variety of objectives are pursued within a single competition regime. These may be objectives that are at times mutually incompatible. Likewise, the practical implementation and enforcement of competition policy often leads to controversy, when the implications of policy decisions become highly politicized. Discretion in decision-making can be contentious, but so too can the absence of discretion in cases where outcomes resting on an 'objective' technical analysis are politically unacceptable.

It is possible to identify a number of objectives that are often associated with competition policies. These are:

- *Consumer welfare.* This is a technical function of competition policy which assumes a direct and formal relationship between the promotion of competition and improved economic performance.
- *Protection of the consumer.* This involves the defence of the individual against big business, usually for moral or political reasons.
- *Redistribution of wealth.* This is an attempt to inhibit a small number of firms from accumulating a large amount of wealth, an inherently political objective which implies that monopolies and cartels are undemocratic.
- *Protection of small and medium-sized enterprises.* This does not just imply the protection of infant industries, but also assumes that a large number of small firms in a market is in itself a good thing.
- *Regional, social and industrial considerations.* These reflect the frequent use of competition policy as an instrument working for non-competition policy ends, such as the development of regions in decline, the reduction of unemployment or the attainment of a global presence in a particular sector.
- *Market integration.* This is a particularly European phenomenon

in which competition policy is used to break down privately constructed barriers to trade between the EU member states, thus contributing to the creation of a Single European Market (SEM).

- *Promotion of competitiveness.* This has become particularly important since the end of the 1990s, with the introduction of the Lisbon Strategy in 2000 (and especially in its post-2005 form) which subsumes competition policy within a broad framework of economic development.

Just as there are many different competition policy objectives, so there is no one competition policy. As anti-competitive practices take a number of different forms, various of corresponding policy responses are required.

- Firms may engage in restrictive practices such as the setting up of **cartels**. These agreements, which may be informal and unwritten, might involve setting prices above the market price (price-fixing), or carving up a market so that each firm acts as a monopolist in its part of the market (market-sharing). Agreements can involve similar firms, that is, direct competitors within a market (horizontal agreements or restraints), or firms operating at different stages in the production/distribution process (vertical agreements or restraints). Vertical agreements could take the form of exclusive distribution ties, for example, where suppliers are allowed to buy their products from only one approved source. Restrictive practices policy or some form of cartel policy is often developed to deal with such cases.
- The existence of a monopoly (one firm dominating a market) or an oligopoly (a very small number of large firms dominating a market) may also have a detrimental effect on competition. In such cases, dominant firms (either on their own as monopolists or together as oligopolists) can abuse their position, using their market power to cut prices and drive out competitors (predatory pricing) or to charge high prices where consumers have little alternative but to pay up. Monopoly policies exist to deal with behaviour such as this.
- Mergers and joint ventures may have anti-competitive implications because they could lead to a situation where a monopoly or oligopoly is formed (a process of *concentration*). Merger policies thus allow authorities to assess the potential impact on com-

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petition, and to decide whether the merger should be allowed to go ahead.

While these three elements are the building blocks of most competition policies, there is no agreement over what exactly a competition policy should include or on what basis decisions should be taken. Definitions of what a competition policy is, and the distinctive characteristics of different policies, vary therefore from regime to regime. In Japan, for example, trade associations and holding companies have been a particular cause for concern; while in the EU regime, as we see below, subsidy control (state aid policy) falls under the rubric of competition policy.

Introducing the European competition regime

European competition policy can be segmented into four main sub-policy areas. Restrictive practices policy focuses on the regulation of cartels; monopoly policy is directed towards the abuse of a dominant position by firms in a particular market; and mergers policy, a relative newcomer (since 1990), has mergers and acquisitions (M&A) as its target. Finally, state aid policy is of a different order and deals with the potentially anti-competitive effects of national grants of subsidy to industry within the context of the EU's single market. It might also be possible to further differentiate the policy by highlighting the EU's strategy towards particular types of firm – for example, what in EU-speak are referred to as 'services of a general economic interest' (SGEIs), such as rail transport or electricity, although this is not the approach adopted in this book.

While this study sticks to the above distinction and includes chapters on restrictive practices policy, monopoly policy, merger policy and state aid policy, it also acknowledges that the EU – and more specifically the Commission – has sought to make these four aspects of European competition policy more coherent. One way it has sought to do this has been by reorganizing, between 2002 and 2004, the department (or 'Directorate-General') in the European Commission responsible for most competition matters (DG Competition). With some exceptions (see Chapter 3) this reform created units which deal with various aspects of competition regulation, structuring their workload in terms of cases and markets, rather than 'type' of competition policy.

Even without this organizational innovation, there have been various trends in competition regulation within the European Commission since the late 1980s, which have affected all aspects of the institution's work in this policy area. Four particularly notable trends serve as intellectual threads that weave their way through the chapters of this book. These are 'modernization', 'Europeanization', 'decentralization' and 'liberalization'. Although these do not constitute a conceptual framework for the book, they do represent recurring themes. And although it is in the concluding chapter that a spotlight will be cast on the threads, both individually and in terms of how they relate to each other, it is worth considering, albeit with some brevity, what is meant by these concepts within this study.

Modernization was the label given to the Commission's competition policy reform of the mid 2000s, which primarily related to cartel and mergers policy; but which has also since 2005 been adopted as a mantra for state aid reform. The reforms were driven by calls for changes in the substantive analysis that constituted competition decision-making, in part emanating from the European Courts who had frequently criticized the Commission for inadequate economic reasoning in their competition decisions; and by pressure to reduce the administrative burden that the ex-ante notification requirement placed on the Commission, and which was likely to be exacerbated by the accession of twelve new member states in 2004 and 2007. The use of the word 'modernization' is not neutral, however, and has certain normative connotations. At its most basic level it concerns bringing the policy, assumed to be out of date, up to date. But in addition, modernization is often associated with new public management (NPM) ideas, which denote a shift from traditional forms of public administration towards a more varied role for civil services, within which the boundaries of public and private are blurred, in which effectiveness trumps public service values, and where what counts as policy is what can be measured and quantified. As such, modernization suggests the overturning of traditional ways of working and the introduction of new basic assumptions which can be controversial, not least as they may lead to a new configuration of winners and losers, in our case as a consequence of competition enforcement.

The second theme which runs through this book is Europeanization. This is a widely used and very fashionable concept in the field of European Studies which is contested, in the sense that there

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is no agreement on what Europeanization means or how it might be used (whether as a research agenda or a theory, for example). In this study Europeanization is generally used in two interrelated ways. Both imply a top-down (or perhaps a horizontal) process, in which EU rules and norms are either imposed or diffused across the Union. In the first case, the imposition of EU rules, aside from in the early years of the policy, has been a consequence of rounds of enlargement, the last of which were in 2004 and 2007. In this case, applicant states wishing to join the EU had to adopt the *acquis communautaire*, a core part of which were the competition provisions and supporting legislation. In the second case, the mechanism of change is less tangible and comprises a diffusion of norms and ideas about the operation of market economies, and more specifically of competition and competition policy. Here, the Commission seeks to promote a sharing of experience and to provide guidance on how to interpret EU competition rules so as to prevent the fragmentation of the system.

Decentralization in this study refers to a process begun in the early 1990s and continued with the modernization reforms, whereby aspects of competition enforcement were removed from direct Commission control and granted to national competition authorities and domestic courts. Decentralization may be understood, therefore, as delegation of authority from supranational-level principals to nationally based agents. However, decentralization can also imply a pluralist dispersal of decision-making which has normative connotations. In other words, the assumption may be that to decentralize – or to deal with matters of policy at the lowest possible level – is a good thing. This is a characteristic embedded in EU policy-making through the formalized use of the subsidiarity principle.

Finally, liberalization, meant in its economic sense here, has become closely associated with European competition policy, as it implies an opening up of sectors that have traditionally be devoid of competition, and – for various reasons – have been exempt from competition regulation. In this context, therefore, liberalization points to the widening scope of the competition regime. While exemptions are still possible, sectoral exceptions to the general competition rule are few and far between. Liberalization is not the same as privatization, however, as it is neutral on the question of state or private ownership, even if the Commission might keep a closer eye on state-owned firms, and assume that they ought to

behave much the same as if they were in the private sector. Where exceptions are made, they are for SGEIs, as noted above. This does not mean that anti-competitive conduct is tolerated without question in these sectors; just that specific rules may need to be formulated to cover the specific context within which these firms operate and to encourage reform in a pro-competition direction.

Whether we are discussing modernization or liberalization, Europeanization or decentralization, the context in which the study of (European) competition policy takes place is always the negotiated relationship between state and industry. This relationship is not a given, but reflects particular assumptions at particular points in time about the public sphere and the private sphere, and the responsibilities that each owes to the other within liberal-democratic market economies. There is no doubt that competition policy is a matter of economics, just as it is a matter of the law. What is often forgotten, however, is that the reasons for having a competition policy, the form that policy takes – both substantively and procedurally – and how the policy is implemented and enforced are all at the core questions of politics. A political dimension demands that we stand back from the micro- and mesoanalyses of the competition economists and lawyers to address broader questions of state, economy and indeed society. This latter point may at times seem like background information as we launch into our chapters on the policy detail. But the reader should remember that while others will push the boundaries of the political further in their analysis of competition policy (see Wigger 2008, for example), the motivation behind this book (both in its first edition and in this current edition) was to contribute to an emerging political and policy literature on the European competition regime.

Organization of the book

The chapters that follow begin with an account of the evolution of European competition policy. Thus Chapter 2 identifies the origins of the policy as well as the various stages in that evolution, times when different dimensions of competition regulation were in the ascendant. It also accounts for the increasing importance of the policy in the mid 1980s, its metamorphosis at that time, and some of the more recent developments associated with the modernization agenda of the 2000s. Chapter 3 examines the institutional frame-

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work which governs the EU competition regime, and touches on key elements in competition decision-making. It focuses in particular on the European Commission, and on the network of domestic bodies which now, together with the EU institutions, comprise the EU's quasi-federal system of competition governance.

When identifying the main components of a competition policy, restrictive practices (or cartel) policy and monopoly policy spring immediately to mind. These two central strands in the EU's policy fall under Articles 81 and 82 of the EEC Treaty and are dealt with in Chapters 4 and 5, respectively. In each chapter, an account of the legal framework goes hand in hand with an assessment of policy substance, which is illuminated by a number of key case examples. Chapter 6 then explores the evolution, the characteristics and the decision-making elements of EU merger policy which has existed as a discrete element of the EU's competition regime only since 1990. Chapter 7, which focuses on the Commission's state aid policy, also explores historical, substantive and procedural matters in this unique area.

Chapter 8 introduces a theoretical perspective into the study of competition policy, something often lacking in the literature in this field. Finally, Chapter 9, which presents the conclusions to the book, identifies key themes dominating the current debate on EU competition policy. It does this by assessing the policy's reform agenda, using reform as a window on to current policy trends and controversies. This final chapter also considers the challenges likely to face the European competition regime in the years to come.

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